A Comparison of the Most Favored Lender and Exportation Rights of National Banks, FSLIC-Insured Savings Institutions, and FDIC-Insured State Banks

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Consumer credit transactions today are increasingly conducted across state lines. Interstate lending enables financial institutions to expand their loan portfolios and offer borrowers new sources of credit. Consequently, the interstate consumer lending market is becoming ever more competitive.[1] At the same time, the increasing frequency of interstate consumer credit transactions has propelled financial institutions, government regulatory agencies, and their legal counsel into strenuous and often complex debate over the legal requirements applicable to these transactions.[2] The complexity of this debate is not surprising, due to the presence of a variety of state and federal regulatory agencies overseeing financial institutions, as well as the broad range of state laws and the growing number of federal laws applicable to consumer credit transactions.[3] Principles of federalism and choice-of-law accordingly play a prominent role in attempting to resolve the issues that may arise as a result of interstate lending programs.[4]

Interstate lending by federally-insured financial institutions involves one central issue: exportation of interest rates and other credit terms. What legal restrictions should govern an interstate credit transaction? May a financial institution "export" rates and terms to out-of-state borrowers by charging the rates and fees and imposing other contract terms authorized by the laws of the state where it is located? Is the financial institution subject to provisions of the law of the borrower's home state that may be more restrictive? To what extent does federal law preempt state law?

Despite nearly two decades of analysis and debate,[5] only one issue has been conclusively resolved: a national bank may "export" the interest rate permitted by the law of the state where it is located to borrowers residing in other states.[6] Some state regulators continue to assert that national banks and other federally insured financial institutions may not "export" fees and other terms, claiming that the "exporting" lender remains subject to all state law restrictions other than the interest rate.[7] In two recently-filed actions against national banks,[8] the Iowa Attorney General has asserted that several of the non-rate credit terms included in the defendants' credit card agreements[9] violate Iowa law. These are

1. Cocheo, *Bank Cards at the Crossroads*, ABA Banking J., Sept. 1987, at 66, 68-69, 71-72, 75; McCoy and Swartz, *Plastic Battle: Big Credit Card War May Be Breaking Out, to Detriment of Banks*, Wall. St. J., Mar. 19, 1987, at 1, 20.
2. *See, e.g.*, Burgess and Ciolfi, *Exportation or Exploitation? A State Regulator's View of Interstate Credit Card Transactions*, 42 Bus. Law. 929 (1987) [hereinafter cited as Burgess]; Rosenblum, *Exporting Annual Fees*, 41 Bus. Law. 1039 (1986) [hereinafter cited as Rosenblum]; Pulles, *Exporting Non-Interest-Rate Provisions*, 39 Bus. Law. 1271 (1984); Culhane and Kaplinsky, *Trends Pertaining to the Usury Laws*, 38 Bus. Law. 1329 (1983) [hereinafter cited as Culhane and Kaplinsky]; Burke and Kaplinsky, *Unraveling the New Federal Usury Law*, 37 Bus. Law 1079 (1982) [hereinafter cited as Burke and Kaplinsky]; Arnold and Rohner, *The "Most Favored Lender" Doctrine for Federally Insured Financial Institutions — What Are its Boundaries?*, 31 Cath. U.L. Rev. 1 (1981) [hereinafter cited as Arnold and Rohner].
3. *See* Burgess, *supra* note 2, at 939-41.
4. *Id.* at 939. *See, e.g.*, *infra* text accompanying notes 48-51, 177-186, 252-260, 270-275, & 305-316.

* The views expressed in this article are those of the authors and do not necessarily represent the views of Household Finance Corporation or its affiliates.

5. *See* Shanks, *Special Usury Problems Applicable to National Banks*, 87 Banking L.J. 483 (1970) [hereinafter cited as Shanks], for an early treatment of some of these issues.
6. Marquette Nat'l Bank v. First of Omaha Serv. Corp., 439 U.S. 299, 313-19 (1978).
7. *See generally* Burgess, *supra* note 2. *But see* Letter from Sam Kelley, Texas Consumer Credit Commissioner, to George E. Henderson (Mar. 14, 1985) (unpublished) [hereinafter cited as Kelley opinion].
8. Iowa ex rel. Miller v. Citibank (South Dakota), Civ. No. 88-189-E (S.D. Iowa, filed Apr. 11, 1988); Iowa ex rel. Miller v. First Nat'l Bank, Civ. No. 88-20 (D. Del., filed Jan. 19, 1988, dismissed Apr. 15, 1988). The *First National Bank* suit has been settled, with the bank agreeing to comply prospectively with Iowa law on fees and charges on accounts held by Iowa residents, subject to amendments to federal or Iowa statutes, Comptroller of the Currency (OCC) regulations, Iowa regulations, or supervening case Law. SO BNA's Banking Rep. 711 (1988); at 4; telephone interview with Walter Tuthill, attorney for First National Bank, Wilmington, Del. (Apr. 12, 1988). At least one private suit challenging the exportation of non-rate terms has been filed in the rural South. The suit developed from collection efforts by two banks against the same customer. Newman, *Iowa Nears Settlement in Card Fee Suit*, Am. Banker, Mar. 28, 1988, at 30.
9. The Attorney General challenged First National Bank of Wilmington's, Delaware choice-of-law provision, late charge, returned check charge, overlimit charge, court costs and attorney's fees provision, and notice of change of terms provision. Citibank (South Dakota), N.A.'s South Dakota choice-of-law provision, late charge, returned check charge, definition of "default," attorney's fees and collection costs provision and notice of change of terms provision are being challenged.

among the first cases in which a national bank's (or any other federally-insured institution's) authority to export non-rate terms has been challenged.

State legislatures have adopted conflicting positions concerning these institutions' rate and other term exportation rights. The Connecticut legislature has enacted a law regulating the interest rates that certain types of out-of-state financial institutions having offices or affiliates with offices in the state may charge to Connecticut borrowers,[10] despite the clear[11] or arguable[12] rate exportation rights of various federally-insured financial institutions. Conversely, the South Dakota legislature has declared that virtually all fees and charges are deemed "interest."[13] The Pennsylvania legislature, while continuing to limit sellers and holders of retail installment accounts to an 18% rate ceiling on accounts issued to buyers domiciled in the state, has deregulated rates on such accounts issued to buyers domiciled outside the state.[14]

This article will compare the most favored lender and exportation rights of national banks, federally-insured savings institutions, and federally-insured state banks. In the process, this article will examine recent developments regarding the application of the most favored lender doctrine to these institutions and analyze many of the theories offered in support of the exportation of fees and terms other than the interest rate. This article will not attempt to resolve all of the unanswered questions relating to these institutions' interstate lending operations. Rather, it will describe a matrix of issues and considerations that national banks and other federally-insured financial institutions must analyze thoroughly and weigh carefully as a part of any decision to engage in interstate consumer lending.

I. National Banks

A. Section 85 and the Most Favored Lender Doctrine

1. Interpretation of Section 85

The National Bank Act,[15] at 12 U.S.C. section 85 (section 85),[16] establishes the interest rate that a national bank may charge on extensions of credit. The maximum rate chargeable by a national bank is thus a federal question.[17] Section 85 incorporates state law to determine the maximum rate[18] through application of three clauses.

First, a national bank generally may charge interest at the greater of "the rate *allowed* by the laws of the State . . . where the bank is located," or one percent in excess of the discount rate on ninety-day commercial paper in effect at the Federal Reserve Bank in the district where the bank is located.[19] In *Tiffany v. National Bank*,[20] the United States Supreme Court interpreted the "allowance clause" to refer not to the rate allowed for state banks, but to the rate allowed for "lenders generally,"[21] even if such rate exceeds the rate permitted to state banks under state law.[22] *Tiffany* did not determine whether the term "laws" referred to in the "allowance clause" encompasses a state regulated lender statute which characteristically constitutes an exception to a general state usury law and authorizes such lenders to charge higher rates than those permitted to "lenders generally" under state law.[23] It was left for the Comptroller of the Currency (OCC) to issue an interpretation of section 85 (the OCC Ruling) providing that a national bank may charge the highest rate authorized under state law for any competing state-chartered or licensed lender, without becoming licensed under such state law.[24] The OCC Ruling codifies what has come to be known as the "most favored lender" doctrine. The alternative rate of one percent over the discount rate contained in the first clause of section 85, added in 1933,[25] represents a federal rate which preempts lower rates provided for

10. An Act Concerning the Activities of Foreign Banking Corporations, 1987 Conn. Pub. Acts No. 87-205, § 5 (effective July 1, 1987). To the extent that this law attempts to regulate the Connecticut activities of out-of-state financial institutions in a way that would infringe on those institutions' rights granted under federal law, it would appear to violate the supremacy clause and the commerce clause. *See* Lewis v. BT Inv. Managers, Inc., 447 U.S. 27 (1980); U.S. Const. art. 1, § 8, cl. 3; art. VI, cl. 2. *But see* Sears, Roebuck & Co. v. Brown, 806 F.2d 399 (2d Cir. 1986) (Connecticut statute regulating holding companies and their subsidiaries held not to violate commerce clause or supremacy clause).

11. *See Marquette*, 439 U.S. at 313-19 (national banks).

12. *See* Letter from General Counsel to the Federal Home Loan Bank Board (Aug. 6, 1982), *reprinted in* [Current] Fed. Banking L. Rep. (CCH) para. 82,022 (federally-insured savings institutions); Letter from Kathy A. Johnson, Attorney to the Federal Deposit Insurance Corporation (FDIC) (Mar. 17, 1981) (unpublished) (federally-insured state banks) [hereinafter cited as Johnson letter]; Letter from Peter M. Kravitz, Senior Attorney to the FDIC (Oct. 20, 1983) (unpublished) (federally-insured state banks) [hereinafter cited as Kravitz letter].

13. An Act to Revise Certain Statutes Pertaining to Interest and Charges Between Debtors and Creditors, 1987 S.D. Sess. Laws ch. 360. Similar legislation is pending in Delaware. O'Connor, *Interstate Credit Cards and Other Products*, in Fischer, Retail Financial Services: Current Developments 182, 271-76 (1987) (outline prepared for distribution at June 11-12, 1987, Practising L. Inst. program, New York, N.Y.). The Delaware legislation also would declare virtually all fees, charges, and other statutory provisions to be "material to the determination of the interest rate." *See* 12 C.F.R. § 7.7310(a) (1987).

14. 1988 Pa. Laws. Act 15 (effective Feb. 26, 1988). The distinction between rates chargeable to in-state and out-of-state borrowers raises constitutional questions under the commerce clause, equal protection clause, and privileges and immunities clause. U.S. Const. art. 1, § 8, cl. 3; art. 4, § 2, cl. 1; amend. XIV, § 1.

15. 12 U.S.C. §§ 21-200 (1982 & Supp. V 1987).

16. *Id.* § 85 (1982). Section 85 provides in pertinent part:

> Any association may take, receive, reserve, and charge on any loan or discount made, or upon any notes, bills of exchange, or other evidences of debt, interest at the rate allowed by the laws of the State, Territory, or District where the bank is located, or at a rate of 1 per centum in excess of the discount rate on ninety-day commercial paper in effect at the Federal reserve bank in the Federal reserve district where the bank is located, whichever may be the greater, and no more, except that where by the laws of any State a different rate is limited for banks organized under State laws, the rate so limited shall be allowed for associations organized or existing in any such State under this chapter. When no rate is fixed by the laws of the State, or Territory, or District, the bank may take, receive, reserve, or charge a rate not exceeding 7 per centum, or 1 per centum in excess of the discount rate on ninety-day commercial paper in effect at the Federal reserve bank in the Federal reserve district where the bank is located, whichever may be the greater, and such interest may be taken in advance, reckoning the days for which the note, bill, or other evidence of debt has to run.
> *Id.*

17. *Marquette*, 439 U.S. at 308 (citing Farmers' & Mechanics' Nat'l Bank v. Dearing, 91 U.S. 29, 34 (1875)).

18. Evans v. Nat'l Bank, 251 U.S. 108, 111 (1919). *But cf.* City Nat'l Bank v. Edmisten, 681 F.2d 942 (4th Cir. 1982) (no federal question jurisdiction under section 85 when declaratory judgment sought that annual fee would not violate state usury law if added to interest charged). *See infra* text accompanying notes 48-51, 177-186, & 252-262 for a discussion of the extent to which state law is incorporated in section 85.

19. 12 U.S.C. § 85 (1982) (emphasis added).

20. 85 U.S. (18 Wall.) 409 (1874).

21. *Id.* at 411. The Court also used the term "natural persons" to refer to "lenders generally" because individuals frequently operated as private bankers during that time. *See* Comment, *Extension of the Most Favored Lender Doctrine Under Federal Usury Law: A Contrary View*, 27 Vill. L. Rev. 1077, 1083 n.34 and authority cited therein (1982) [hereinafter cited as *A Contrary View*].

22. 85 U.S. (18 Wall.) at 411.

23. Such a statute was not at issue. *Id.* at 411. *See A Contrary View*, *supra* note 21, at 1095-96; Burke and Kaplinsky, *supra* note 2, at 1096.

24. 12 C.F.R. § 7.7310(a) (1987). The OCC Ruling provides:

> A national bank may charge interest at the maximum rate permitted by State law to any competing State-chartered or licensed lending institution. If State law permits a higher interest rate on a specified class of loans, a national bank making such loans at such higher rate is subject only to the provisions of State law relating to such class of loans that are material to the determination of the interest rate. For example, a national bank may lawfully charge the highest rate permitted to be charged by a State-licensed small loan company or morris plan bank, without being so licensed.
> *Id.* The OCC Ruling was initially issued as an opinion letter in 1936 and was finally promulgated as an interpretive ruling in 1971 and codified in 1972. For the history and development of the OCC Ruling, *see A Contrary View*, *supra* note 21, at 1089-91 & nn.82-89; Burke and Kaplinsky, *supra* note 2, at 1100-01 n.121; Arnold and Rohner, *supra* note 2, at 6-7. For a discussion of the OCC Ruling's validity, scope, and interpretation, *see infra* text accompanying notes 56-226.

25. Act of June 16, 1933, ch. 89, § 25, 48 Stat. 191 (1933) (amending National Bank Act, ch. 106, § 30, 13 Stat. 108 (1864)) (current version at 12 U.S.C. § 85 (1982)). *See A Contrary View*, *supra* note 21, at 1078 n.7, 1081 n.24 for a history of the amendments to section 85.

under state law.[26]

The second clause is an exception to the first which provides that "[w]here by the laws of *any* State a *different* rate is *limited* for [state banks], the rate so limited shall be *allowed* for [national banks] organized or *existing* in any such State."[27] The *Tiffany* Court held that the "exception clause" applies only where the rate permitted to state banks is higher than that allowed for lenders in general.[28] The combination of the "any State" and "existing" phraseology in the "exception clause" has led national banks to contend that they may "import" the rate allowed by a borrower's home state's laws if it is higher than the rate in the bank's home state.[29]

Finally, section 85 states that where no rate is fixed by state law, national banks may charge the greater of seven percent or one percent over the discount rate.[30] In *Daggs v. Phoenix National Bank*,[31] the United States Supreme Court held that this clause does not apply if state law allows creditors to contract for any rate under a written agreement.[32] Similarly, the Ninth Circuit held in *Hiatt v. San Francisco National Bank*[33] that a national bank was authorized to charge any rate even though California law exempted state and national banks from its usury restrictions, which could have meant that no rate was fixed by state law.[34] Consequently, the third clause of section 85 is essentially meaningless.[35]

The interpretation of five other terms or phrases in section 85 is important in determining the most favored lender and exportation rights of national banks. A national bank is authorized to "take, receive, *reserve*, and charge [interest] on any *loan* or *discount* made."[36] In *Evans v. National Bank*,[37] the United States Supreme Court noted that national banks are authorized to discount promissory notes[38] and determined that discounting implies reservation of interest in advance.[39] The National Bank Act thus may permit the charging of discount interest at the maximum state rate, even though the maximum state rate is established in terms of a simple interest rate and discounting is specifically prohibited.[40]

Moreover, the rate chargeable under section 85 may be imposed on "*any* loan[,] discount . . . , notes, bills of exchange or *other evidences of debt*."[41] In construing the term "specified class of loans"[42] contained in the OCC Ruling, the court in *United Missouri Bank v. Danforth*[43] determined that retail credit sales and loans constitute an interchangeable class of debt.[44] The court based its conclusion on the "other evidences of debt" language in section 85.[45] To the extent adopted by the courts, a broad classification of transactions will enhance a national bank's flexibility in establishing the terms under which it will operate a particular type of loan program.

Third, section 85 empowers national banks to charge *"interest"* at the highest rate allowed under the laws of the state where it is located.[46] The largely unresolved issues regarding the definition of "interest" and whether the definition should be obtained from federal law, the law of the bank's home state, or the law of the borrower's home state, are critical in delineating national banks' rights to export fees and other contract terms in addition to the interest rate.

Fourth, "interest" may be imposed at the "*rate* allowed by the *laws*" of the bank's home state.[47] There have been differing views as to whether the state law incorporated in section 85 encompasses only the numerical rate,[48] the method of calculating the rate as well,[49] or even the entire case law interpreting limitations on usury,[50] including common law conflict of laws rules.[51]

Finally, a national bank obtains its maximum rate by reference to "the laws of the State where the bank is *located*."[52] In *Marquette National Bank v. First of Omaha Service Corp.*,[53] the Supreme Court held that a national bank is located in the state named in its organization certificate.[54] This decision underlies the establishment in *Marquette* of national banks' authority to "export" interest rates in interstate lending programs.[55]

26. *Marquette*, 439 U.S. at 318 n.31; OCC Interpretive Letter No. 71 from John G. Heimann, Comptroller of the Currency (Dec. 1, 1978), *reprinted in* [1978-1979 Transfer Binder] Fed. Banking L. Rep. (CCH) para. 85,146.

27. 12 U.S.C. § 85 (1982) (emphasis added).

28. *Tiffany*, 85 U.S. (18 Wall.) at 411-12. The Court noted that section 85 "speaks of allowances to National banks and limitations upon State banks, but it does not declare that the rate limited to State banks shall be the maximum rate allowed to National banks." *Id.* at 412. The Court effectively substituted "higher" for "different" in the "exception clause" based on the absence of the "and no more" language found in the "allowance clause." *Id. See A Contrary View*, *supra* note 21, at 1083 & nn. 36-37 and authorities cited therein. The Court emphasized the need to protect national banks against unfriendly state legislation. 85 U.S. (18 Wall.) at 412-13.

29. *See infra* text accompanying notes 236-246 for a discussion of national banks' rights to "import" rates.

30. 12 U.S.C. § 85(1982). The one percent over the discount rate option was added in 1933. Act of June 16, 1933, ch. 89, § 25, 48 Stat. 191 (1933) (amending National Bank Act, ch. 106, § 30, 13 Stat. 108 (1864)) (current version at 12 U.S.C. § 85 (1982)).

31. 177 U.S. 549 (1900).

32. The Court construed the phrase "no rate is fixed" to refer only to circumstances where no rate is "allowed" by state law, i.e., where state law prohibits the charging of any interest. *Id.* at 555.

33. 361 F.2d 504 (9th Cir.), *cert. denied*, 385 U.S. 948 (1966), *rehearing denied*, 385 U.S. 1021 (1967).

34. Under state law there was thus no limit on the rate a state bank could charge. The court interpreted this usury exemption to mean that rates were "fixed" as without limitation except as agreed to by the parties, and concluded that national banks should be accorded the same treatment. 361 F.2d at 507. *See* Cal. Const. art. XV, § 1 (West Cum. Supp. 1987).

35. *See* OCC Interpretive Letter No. 138 from John E. Shockey, Chief Counsel (Feb. 8, 1980), *reprinted in* [1980-1981 Transfer Binder] Fed. Banking L. Rep. (CCH) para. 85,219, at 77,328 (citing Shanks, *supra* note 5, at 488 (suggesting that "for all practical purposes, the 7 percent ... limit ... may be ignored.")).

36. 12 U.S.C. § 85 (1982) (emphasis added).

37. 251 U.S. 108.

38. *See* 12 U.S.C. § 24 (Seventh) (Supp. V 1987) (national banks have the power to discount promissory notes, drafts, bills of exchange, and other evidences of debt).

39. 251 U.S. at 114. The case involved the discounting of short-term single payment commercial paper. *See infra* note 40.

40. *See infra* text accompanying notes 100-104 & 187-200 for a discussion of whether or not national banks may charge discount interest on installment credit.

41. 12 U.S.C. § 85 (1982) (emphasis added).

42. 12 C.F.R. § 7.7310(a) (1987). *See supra* note 24 for text of the OCC Ruling. *See also infra* text accompanying notes 76-81 & 130-155 for a discussion of this term.

43. 394 F. Supp. 774 (W.D. Mo. 1975).

44. *Id.* at 783. The court held that the bank could charge the Small Loan Act rate on credit sale transactions governed by the Retail Credit Sales Act (RCSA), even though the RCSA exempted licensed small loan companies from its provisions. *Id.* at 784.

45. *Id. See infra* text accompanying notes 130-155 for a discussion of the classification of transactions.

46. 12 U.S.C. § 85 (1982) (emphasis added).

47. *Id.*

48. *Evans*, 251 U.S. at 111. *See* Nat'l Bank v. Johnson, 104 U.S. 271, 277-78 (1881); *Dearing*, 91 U.S. at 34.

49. This includes all prohibitions on enlarging the rate, even if the resulting charge is within the legal limit if imposed properly. Citizens' Nat'l Bank v. Donnell, 195 U.S. 369, 374 (1904); Att'y Gen. v. Equitable Trust Co., 294 Md. 385, 417, 450 A.2d 1273, 1291-92 (1982).

50. First Nat'l Bank v. Nowlin, 590 F.2d 872, 876 (8th Cir. 1975). *See* Union Nat'l Bank v. Louisville, N.A. & C. Ry., 163 U.S. 325, 331 (1896).

51. OCC Interpretive Letter No. 325 from Peter Liebesman, Assistant Director of the Legal Advisory Services Division (Jan. 22, 1985), *reprinted in* [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) para. 85,495, at 77,754. *See* Shanks, *supra* note 5, at 489-91. *But see* Morosani v. First Nat'l Bank, 539 F. Supp. 1171, 1173 (N.D. Ga. 1982), *rev'd on other grounds*, 703 F.2d 1220 (11th Cir. 1983).

52. 12 U.S.C. § 85 (1982) (emphasis added).

53. 439 U.S. 299.

54. *Id.* at 310. The Court engaged in a federal common law choice-of-law analysis concerning Omaha Bank's Bank-Americard program to confirm that Omaha Bank was "located" in Nebraska. *Id.* at 309-13. *See infra* text accompanying notes 229-235 for further discussion of the "location" question relating to national banks.

55. *Id.* at 313-19.

Unfortunately, for national banks this analysis of section 85 resolves neither the scope of the most favored lender doctrine nor many of the issues which arise in the context of interstate lending operations. A national bank also must explore the validity, scope, and interpretation of the OCC Ruling, which necessarily involves further examination of section 85, in order to determine the bank's authority to export the highest interest rate, or the most advantageous fees and other contract terms, allowed in its home state to borrowers residing in other states.

2. The OCC Ruling

a. Validity and Scope

A federal appellate court first upheld the OCC Ruling[56] in 1972 in *Northway Lanes v. Hackley Union National Bank & Trust Co.*[57] Its validity has since been confirmed and its criteria applied implicitly or explicitly by the Courts of Appeals for the Fifth,[58] Seventh,[59] and Eighth[60] Circuits, as well as several other courts.[61] Only two state trial courts have declined to adopt the OCC Ruling.[62] The Supreme Court cited the OCC Ruling with apparent approval in *Marquette,* at least to the extent of the Ruling's incorporation of the most favored lender doctrine,[63] but declined to address its validity. The Court still has not decided this issue, and, based on the scope of the OCC Ruling detailed below, it is unclear whether the Court would uphold it as a reasonable interpretation of section 85.[64]

Perhaps the most useful basis for examining the validity of the OCC Ruling as an interpretation of section 85 is to determine whether the Ruling is broader or more restrictive than section 85. This determination will be based on an analysis of the following key concepts and terms contained in the OCC Ruling.[65]

(1) The Need for a "Borrowing"

The OCC Ruling clearly is applicable when a national bank is borrowing the rate authority set forth in section 85 from a state-supervised lender. It is therefore important to determine when a national bank is borrowing its rate. A national bank always may contend that it is borrowing its rate, unless the highest rate is applicable only to national banks under a particular state's laws.[66] National banks may even borrow a usury exemption available to a state-chartered lender. In *Hiatt v. San Francisco National Bank,*[67] national banks held the same exemption from state usury laws as state banks. The Ninth Circuit applied the allowance and exception clauses of section 85 to allow a national bank to borrow the state bank's rate exemption rather than rule that no rate was "fixed" by state law.[68]

State rate structures generally are established in one of four different ways: (1) by class of loans (i.e., consumer versus commercial, closed-end versus open-end, direct lending versus sales finance, real estate mortgages versus automobile loans versus bank credit cards, etc.); (2) by class of lenders (i.e., banks versus savings and loans versus licensed lenders); (3) in a nondiscriminatory manner (i.e., under an undifferentiated Uniform Consumer Credit Code or usury law); or (4) in some combination of the first three alternatives. Based on *Hiatt,* national banks may borrow a rate established under any of these four schemes.

Several commentators have argued that to the extent that national banks have independent authority under state law to charge the highest state rate, and another class of lender has the same authority, national banks are not borrowing their authority from that class lender. In that case, the commentators assert that the OCC Ruling does not apply.[69] Under this interpretation, the OCC Ruling is merely a borrowing regulation.[70] In order to obtain its benefits, a national bank cannot already be the most favored lender in the state. This reading of the OCC Ruling is too rigid and ignores the language of section 85. Section 85 does not require borrowing; rather, it authorizes a national bank to borrow rates in order to become a most favored lender. As *Tiffany* and the OCC Ruling have indicated, section 85 recognizes three classes of lenders: "lenders generally," state banks, and other state-chartered or licensed lenders.[71] National banks may either have parity with one or more classes under state law or be accorded parity pursuant to section 85. Thus, the better view under *Tiffany* and *Hiatt*, as partially codified[72] in the OCC Ruling, is that a national bank is always deemed to be borrowing its rate from the "highest rate" lender in the state, even if the national bank also is a most favored lender.

(2) "Competing Lender"

Section 85 on its face does not contain a "competing lender" test. The *Tiffany* Court did not require national banks to compete with the highest rate lender in order to charge such a rate.[73] Subsequent decisions by courts and state regulators, with few exceptions, and an OCC staff letter have ruled that the OCC Ruling does not require actual competition.[74] Even if this test merely requires that the most favored lender may engage in the same type of credit transaction as a national bank,[75] it expands the plain language of section 85. By incorporating

56. *See supra* note 24 for text of the OCC Ruling.

57. 464 F.2d 855, 864 (6th Cir. 1972). The court determined that it should defer to a reasonable interpretation of the National Bank Act promulgated by the OCC, the agency charged with the Act's administration. *Id.* (citing Udall v. Tallman, 380 U.S. 1, 17 (1965); FHA v. Darlington, Inc., 358 U.S. 84, 90 (1958); Unemployment Compensation Comm'n v. Aragan, 329 U.S. 143, 153-54 (1946)).

58. Partain v. First Nat'l Bank, 467 F.2d 167, 174 (5th Cir. 1972).

59. Fisher v. First Nat'l Bank (Fisher/Chicago), 538 F.2d 1284, 1290 (7th Cir. 1976), *cert. denied*, 429 U.S. 1062 (1977).

60. Fisher v. First Nat'l Bank (Fisher/Omaha), 548 F.2d 255, 259-60 (8th Cir. 1977). *See Nowlin*, 590 F.2d 872 (never referred to OCC Ruling, although used term "most favored lender").

61. *See, e.g.*, Ray v. American Nat'l Bank & Trust Co., 443 F. Supp. 883 (E.D. Tenn. 1978); *Danforth*, 394 F. Supp. 774; *Equitable Trust*, 294 Md. 385, 450 A.2d 1273; Comm'r of Small Loans v. First Nat'l Bank, 268 Md. 305, 300 A.2d 685 (1973); First Bank v. Miller, 131 Mich. App. 764, 347 N.W.2d 715 (Mich. App. 1984) (case involved state banks, but OCC Ruling invoked for comparative purposes).

62. Deak Nat'l Bank v. Bond, 89 Misc. 2d 95, 390 N.Y.S.2d 771 (Sup. Ct. 1976); Colo. Nat'l Bank v. Coder, [1969-1973 Transfer Binder] Cons. Cred. Guide (CCH) para. 99,018 (Mont. Dist. Dec. 29, 1972) (still applied "competing lender" test).

63. 439 U.S. at 314 n.26.

64. *See supra* note 57 and authorities cited therein. *See also infra* text accompanying notes 112-115.

65. The other important question regarding the scope of the OCC Ruling is whether it should apply to interstate loans or only to intrastate loans. *See infra* text accompanying notes 296-300 for an analysis of this issue.

66. An analysis of the statutory schemes of all 50 states is beyond the scope of this article. It seems unlikely, however, that any such state statutory scheme exists.

67. 361 F.2d 504.

68. *Id.* at 507.

69. *See* Burgess, *supra* note 2, at 938-39; *A Contrary View*, *supra* note 21, at 1093.

70. Burgess, *supra* note 2, at 938.

71. 85 U.S. (18 Wall.) at 411-12; 12 C.F.R. § 7.7310(a) (1987).

72. *See infra* text accompanying notes 82-83.

73. 85 U.S. (18 Wall.) at 411-412.

74. *See infra* text accompanying notes 116-124 and authorities cited therein for a more thorough analysis of the "competing lender" standard.

75. *Danforth*, 394 F. Supp. 774, 784.

this test, the OCC Ruling is therefore more restrictive than section 85.

(3) "Specified Class of Loans"

Section 85 also does not provide for a "specified class of loans" test. As interpreted in *Tiffany*, section 85 does not recognize distinctions among classes of loans, but only among classes of lenders: "lenders generally" and state banks.[76] In the course of interpreting the OCC Ruling, a state supreme court[77] and the OCC staff[78] have applied the "class of loans" standard rigorously to restrict national banks' use of the most favored lender doctrine.[79] Conversely, interpreting the OCC Ruling in light of the "other evidences of debt" language in section 85, a federal district court essentially has expunged the test from the Ruling.[80] The latter approach seems more faithful to both the wording and the intent of section 85.[81] Again, in this instance, the OCC Ruling is more restrictive than section 85.

(4) "Class of Lender"

Section 85 and the OCC Ruling both incorporate a "class of lender" standard. Under *Tiffany*, national banks may obtain rate parity with natural persons or state banks.[82] The OCC Ruling is more restrictive than section 85 to the extent that natural persons are not required to be chartered or licensed by a state in order to extend credit. Otherwise, section 85 and the OCC Ruling essentially provide for an identical standard.

Section 85 has established one percent over the discount rate as a federal alternative rate, but has not directly incorporated other federal usury laws.[83] Advantageous rates which may be charged by other federally-chartered lenders are therefore available to national banks only if directly incorporated by state law.[84] The OCC Ruling reaches the same conclusion.[85]

A national bank may contend that the state law relied on under section 85 indirectly incorporates federal usury laws pursuant to the supremacy clause.[86] A court probably would reject this argument, however, due to the references to state law and the insertion of a specific federal alternative rate in section 85. The OCC staff already has rejected this argument.[87]

(5) State Licensing Exemption

The federal banking laws and an OCC regulation exempt national banks from state licensing requirements.[88] Thus, under section 85, a national bank is permitted to charge the highest rates available to any state-licensed lender without being licensed by that state. The OCC Ruling so provides,[89] and the statute and the Ruling consequently contain an equally broad licensing exemption.

(6) "Material to the Determination of the Interest Rate"

The inquiry under section 85 as to what constitutes "interest" and the query under the OCC Ruling as to which provisions of a law governing a class of loans are "material to the determination of the interest rate" are quite distinct. The answer to the former determines which fees and other terms are charges for the use or forbearance of money,[90] while the response to the latter specifies which fee and other provisions of the governing law a national bank must comply with in order to borrow the most favored lender's rate. Moreover, the responses to these questions depend on which law (federal or state, and, if state law, the law of the bank's home state or the borrower's home state) and what type of construction of the OCC Ruling (strict or broad) is applied. Finally, a particular bank's views concerning the applicable law and the degree to which it should apply may depend on whether the fees and terms allowed under such law are considered attractive or burdensome to the bank.[91]

The "materiality" test applies in fewer situations than the test as to what constitutes "interest" under section 85. Under the OCC Ruling, it only applies when "state law permits a higher rate on a specified class of loans [and] a national bank [is] making such loans at such higher rate."[92] Section 85, on the other hand, includes no class of loans test.[93] Nevertheless, when the "materiality" test is applicable, and the expansive interpretation of the test established in *Attorney General v. Equitable Trust Co.* is followed, the OCC Ruling requires a national bank to comply with considerably more provisions of its home state's law than section 85. Under *Equitable Trust*, provisions are "material" if they are "material to judicial determination of whether or not the interest charged in a given transaction is unlawful."[94] In applying this test, the court ruled that every provision of the Maryland Consumer Loan Law (MCLL)[95] was material except one that subjected the lender to the borrower's claims and defenses against a seller of goods.[96] No federal or state definition of "interest" is this expansive.[97]

76. 85 U.S. (18 Wall.) at 411-12. The absence of classes of loans under Missouri law in the early 1870s may explain why the Court did not draw such distinctions. *Id.* at 411. *See Equitable Trust*, 294 Md. at 397, 450 A.2d at 1281 and authorities cited therein, for a brief history of the development of installment and open-end credit in the U.S.

77. *Equitable Trust*, 294 Md. 385, 450 A.2d 1273.

78. OCC Interpretive Letter No. 178 from Richard V. Fitzgerald, Director of the Legal Advisory Services Division (Jan. 12, 1981), *reprinted in* [1981-1982 Transfer Binder] Fed. Banking L. Rep. (CCH) para. 85,259.

79. Credit card cash advances and purchases were determined to be different classes of loans. *Equitable Trust*, 294 Md. at 413-14, 450 A.2d at 1290; OCC Interpretive Letter No. 178, *supra* note 78.

80. *Danforth*, 394 F. Supp. at 784-85.

81. *See* 12 U.S.C. § 85 (1982). *But see Northway Lanes*, 464 F.2d at 862 (citing Cong. Globe, 38th Cong., 1st Sess. 2123-26 (1864) (remarks of Sen. Grimes)).

82. *See supra* text accompanying note 76.

83. *See* 12 U.S.C. § 85 (1982).

84. *See infra* text accompanying notes 127-128.

85. 12 C.F.R. § 7.7310(a) (1987).

86. *See* U.S. Const. art. VI, cl. 2.

87. OCC Interpretive Letter No. 255 from Peter Liebesman, Assistant Director of the Legal Advisory Services Division (Jan. 19, 1983), *reprinted in* [1983-1984 Transfer Binder] Fed. Banking L. Rep. (CCH) para. 85,419. *Contra*, Culhane and Kaplinsky, *supra* note 2, at 1336-39.

88. 12 U.S.C. §§ 24 (Seventh), 484 (Supp. V 1987); 12 C.F.R. § 7.6025(b) (1987). *See also infra* text accompanying notes 221-226.

89. *See* 12 C.F.R. § 7.7310(a) (1987).

90. *See* Rosenblum, *supra* note 2, at 1044 n.24; Burke and Kaplinsky, *supra* note 2, at 1106.

91. *See, e.g.*, Rosenblum, *supra* note 2, at 1042-43 n.20.

92. 12 C.F.R. § 7.7310(a) (1987). *See infra* text accompanying notes 130-152. The "materiality" test also has been applied in several Minnesota state court cases involving state banks. *See infra* text accompanying notes 427-430.

93. *See supra* text accompanying notes 76-80. *See also infra* text accompanying notes 148-150.

94. 294 Md. at 418, 450 A.2d at 1292.

95. The MCLL, a closed-end loan statute, was being applied to open-end cash advances. *Id.* at 417, 450 A.2d at 1292.

96. *Id.* at 418-24, 450 A.2d at 1292-95. *See infra* text accompanying notes 159, 161, 175, & 208-217 for a listing of material provisions.

97. The recently-enacted South Dakota revolving loan law amendments, which permit banks located in that state to impose virtually any type of charge and deem all such charges to be "interest," may most closely approach the scope of *Equitable Trust*. An Act to Revise Certain Statutes Pertaining to Interest and Charges Between Debtors and Creditors, 1987 S.D. Sess. Laws ch. 360. An OCC staff letter provides that "all charges permitted or prohibited by state law in connection with particular types of loans may be defined as 'interest.'" "OCC Interpretive Letter from Richard V. Fitzgerald, Director of the Legal Advisory Services Division (Nov. 24, 1980) (unpublished) (construing *Northway Lanes*, 464 F.2d 855) [hereinafter cited as Fitzgerald letter].

The scope of state law coverage under the OCC Ruling and section 85 is more comparable under the three-part test of "materiality" enunciated in an OCC interpretive letter issued by Peter C. Liebesman, then Assistant Director of the Legal Advisory Services Division, four months after the *Equitable Trust* decision (the Liebesman letter).[98] The Liebesman letter states that (1) state law provisions which establish "the characteristics—such as size, maturity and classes of borrowers—of a category of loans are . . . material"; (2) state laws which "establish the manner in which the numerical rate of interest is determined" (i.e., prohibitions against compounding interest) also are "material"; and (3) "because of conflicting judicial opinions, it is less clear whether [section 85] incorporates state laws which do not determine the allowed numerical rate . . . but affect the ultimate return on loan proceeds."[99]

These conflicting opinions reflect concern whether state law prohibitions on discounting interest apply to national banks, when discounting "would provide an effective yield greater than [the] interest permitted."[100] The Liebesman letter cites *Evans*[101] and *Northway Lanes*,[102] apparently to the effect that section 85 preempts conflicting state law, and *First National Bank v. Nowlin*,[103] apparently for the proposition that *Evans* should be limited to cases involving single payment short-term paper.[104] Among the other state law provisions that seemingly would be covered by the third category in the Liebesman letter are additional charge authorizations, free-ride periods, balance calculation methods (except for prohibitions on compounding), change of terms and other notice requirements, and restrictions on acceleration and account cancellation.[105] Thus, the Liebesman test incorporates a greater variety of state law provisions than virtually any federal or state definition of "interest."[106]

Even under the *Equitable Trust* "materiality" standard, some provisions of a national bank's home state's laws, such as disclosure requirements,[107] will not apply to the bank. A recent article suggests that the limited applicability of state law to a national bank under this standard "is arguably in conflict with" Supreme Court precedent that "national banks are subject to state law except to the extent that such law conflicts with or frustrates the purpose of federal legislation or disrupts the banks in the performance of their duties as federal instrumentalities."[108] Close analysis reveals that this "federal instrumentality" doctrine represents a principle of both federal preemption *and* broad applicability of state law in the *absence* of either federal preemption or impairment of national banks' efficiency as federal agencies.[109] In an intrastate loan,[110] general applicability of state law under the federal instrumentality doctrine must yield to the specific federal preemption contained in the OCC Ruling. Because the OCC Ruling incorporates state law only to a limited extent, however, the doctrine seemingly requires national banks to comply with *other* applicable home state laws which (1) are not preempted by other federal laws, or (2) do not contravene the doctrine itself, i.e., disrupt national banks in the performance of their duties. There is thus no conflict; the federal instrumentality doctrine operates independently of and in addition to the OCC Ruling.[111]

(7) Would the Supreme Court Uphold the OCC Ruling?

The OCC Ruling, although an apparently well-intentioned effort to interpret section 85, nevertheless represents a more restrictive statement of the most favored lender doctrine than the statute in almost every respect. The Ruling parallels section 85 only in its state licensing exemption, and is broader than the statute only as to the range of state law provisions with which a national bank must comply. Moreover, the Ruling requires compliance with a broader range of state laws than section 85 only if a national bank is extending credit at the most favored lender rates on a specified class of loans.[112] Moreover, in an intrastate loan, the operation of the federal instrumentality doctrine equalizes the scope of state law applicable to national banks under section 85 and the OCC Ruling.

Thus, given the generally restrictive interpretation that the OCC Ruling accords section 85, it seems that the Ruling should not be entitled to great deference by the courts.[113] The Supreme Court, if it were to interpret the language of the Ruling literally, could well find it incompatible with the broad policy of the National Bank Act to encourage the development of a modern interstate banking system.[114] Conversely, the Court might simply disregard the portions of the OCC Ruling which it deems objectionable and apply the remainder of the Ruling, as lower courts have done.[115]

National banks therefore may not be able to rely on the OCC Ruling to determine which provisions of their home states' laws they must comply with in order to borrow the most favored lender's rate. In situations where the borrowed law contains burdensome provisions, however, national banks may

98. OCC Interpretive Letter from Peter C. Liebesman, Assistant Director of the Legal Advisory Services Division, to Jean M.E. Mille, Staff Counsel to the South Carolina Department of Consumer Affairs (Feb. 4, 1983) (unpublished) [hereinafter cited as Liebesman letter].

99. *Id.* at 3.

100. *Id.* at 3-4.

101. 251 U.S. 108.

102. 464 F.2d 855.

103. 590 F.2d 872.

104. *Id.* at 876. *See infra* text accompanying notes 197-200.

105. *See infra* text accompanying notes 178-179 & 201-220 for a more detailed listing of provisions falling into the third category.

106. *See infra* text accompanying notes 159-220. *But see supra* note 97.

107. *See infra* text accompanying notes 218-220.

108. Rosenblum, *supra* note 2, at 1044 n.26 (citing Anderson Nat'l Bank v. Luckett, 321 U.S. 233 (1944); Davis v. Elmira Savings Bank, 161 U.S. 275 (1896)). *See A Contrary View*, *supra* note 21, at 1113 & nn. 217-218, for a discussion as to whether the federal instrumentality doctrine has become an anachronism since the enactment of the "federal usury" provisions of Title V of the Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDMCA), Pub. L. 96-221, Title V, Part C, §§ 521-529, 94 Stat. 164 (Mar. 31, 1980).

109. First Nat'l Bank v. Missouri, 263 U.S. 640, 656 (1924); *Davis*, 161 U.S. at 283.

110. *See infra* text accompanying notes 303-304 for a discussion of the interplay between the federal instrumentality doctrine and the OCC Ruling in an interstate loan.

111. This analysis is invalid only if subjecting national banks to other applicable state laws would frustrate the purpose of the OCC Ruling and section 85. Section 85 at most requires national banks to comply with their home states' usury laws; it does not appear to prohibit the application of other state laws to a national bank. *See* OCC Interpretive Letter No. 333 from Charles F. Byrd, Assistant Director of the Legal Advisory Services Division (Mar. 20, 1985), *reprinted in* [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) para. 85,503.

The interplay between the federal instrumentality doctrine and section 85 would operate in the same manner. The scope of state law made applicable to a national bank due to the doctrine's operation, however, probably would be greater than in the case of the OCC Ruling. *See supra* text accompanying notes 97 & 106.

112. *See supra* text accompanying notes 92-93.

113. *See supra* note 57 and authorities cited therein. *See also A Contrary View*, *supra* note 21, at 1114 n.223 and authorities cited therein.

114. *See Marquette*, 439 U.S. at 312, 318-19.

115. *See, e.g.*, *Danforth*, 394 F. Supp. at 783-85 ("class of loans" and "competing lender" tests).

not want to rely on the Ruling. They may prefer to operate within the generally less inclusive scope of section 85. Nevertheless, when the borrowed law includes beneficial fee and other provisions, national banks may seek to embrace the expansive *Equitable Trust* "materiality" standard. Consequently, it is important to examine thoroughly the interpretation that the courts, the OCC, and state regulators have assigned to the key terms which comprise the OCC Ruling.

b. Interpretation

(1) "Competing Lender"

The predominant view of the courts and regulators is that it is irrelevant whether state-supervised lenders actually engage in the same class of credit transaction as "borrowing" national banks.[116] For example, the court in *United Missouri Bank v. Danforth*[117] declared that "[t]he important determination is whether competing state licensed or chartered lenders *may* engage in the particular type or class of loan, and the rate of interest they *may* charge in connection therewith."[118] Similarly, in authorizing national and state banks to borrow rates applicable to state credit unions, the Michigan Court of Appeals concluded: "[w]e do not consider only the actual membership of credit unions, but also their potential membership. The *potential* for competition in the areas of business and personal loans is sufficiently great that state credit unions must generally be considered as competing lenders of national banks as a matter of federal law."[119] In rejecting an actual competition standard, the OCC staff has noted that imposing such a standard "would result in an unnecessary and complicated evaluation of the geographic banking market in which the national bank is located and a determination of which classes of lenders are offering which types of loans in that market."[120]

In *Fisher/Omaha,*[121] the Eighth Circuit did not even require potential competition. The Court permitted a national bank to borrow Nebraska Small Loan Act rates for credit card purchase and cash advance transactions despite the absence of authorization in the Act for licensees to offer revolving credit.[122] Only one state trial court[123] and one state attorney general[124] have required actual competition in order for a national bank to borrow rates applicable to state-supervised lenders. Nevertheless, the OCC staff's rationale seemingly validates the majority view that a national bank need not compete with a state-supervised lender in order to charge rates permitted to that lender.

(2) "Class of Lender"

The general rule is that a national bank may borrow the interest rate allowed to state-supervised lenders,[125] but not the rate established for other federally-chartered lenders.[126] Where state law permits a state-supervised lender to charge the rates permitted to a federally-chartered lender, however, the OCC staff has opined that a national bank may do likewise.[127] Several states have enacted so-called "rate parity" laws which purport to authorize certain state-chartered lenders to charge rates permitted to any other regulated lenders.[128] Under the OCC Ruling and section 85, national banks therefore should be entitled to apply these parity provisions in order to charge rates permitted to federally-chartered lenders when the state-chartered lenders from which they are borrowing their rates may do so.[129]

(3) "Specified Class of Loans"

The central issue in interpreting the OCC Ruling is whether the term "specified class of loans" should be construed to authorize broad or narrow classification of transactions. Obviously, the broader the classification, the greater the number of laws a national bank is likely to be able to choose among in borrowing its rate (and other "material" terms). *Danforth*[130] is the leading case espousing a broad classification of loans. The Missouri Retail Credit Sales Act (RCSA) exempts a licensed Small Loan Act (SLA) lender from the definition of "retail seller."[131] The *Danforth* court interpreted this exemption to mean that SLA licensees could engage in credit sale transactions covered by the RCSA while charging higher SLA rates.[132] The court ruled that national banks could impose SLA rates on credit card advance and purchase transactions.[133] In reaching its conclusion, the court determined that retail credit sales and loans represent the same class of loan.[134] *Danforth* suggests that all types of consumer credit are fungible under section 85.[135] In *Fisher/Omaha,*[136] the Eighth Circuit also permitted a national bank to borrow the closed-end installment loan rate on open-end credit card purchase and cash advance transactions.[137]

In the most comprehensive analysis of the meaning and scope of the OCC Ruling, the Maryland Court of Appeals[138] narrowly construed "class of loans" in *Attorney General v. Equitable Trust Co.*[139] As in *Danforth* and *Fisher/Omaha,* the plaintiff national banks[140] attempted to apply favorable small loan law rates to credit card purchase and advance transactions. In contrast to the statutory scheme in *Danforth,* however, the Maryland Consumer Loan Law, from which the banks sought to borrow rates, governs only loans. Credit card

116. *Fisher/Omaha*, 548 F.2d at 260; *Danforth*, 394 F. Supp. at 784; *Miller*, 131 Mich. App. at 773, 347 N.W.2d at 719; OCC Interpretive Letter No. 336 from Charles F. Byrd. Assistant Director of the Legal Advisory Services Division (Apr. 16, 1985), *reprinted in* [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) para. 85,506.

117. 394 F. Supp. 774.

118. *Id.* at 784 (emphasis supplied).

119. *Miller*, 131 Mich. App. at 773, 347 N.W.2d at 719 (emphasis added).

120. OCC Interpretive Letter No. 336, *supra note* 116, at 77,789.

121. 548 F.2d 255.

122. *Id.* at 260.

123. *Coder*, [1969-1973 Transfer Binder] Cons. Cred. Guide (CCH) para. 99,018 (Mont. Dist. Dec. 29, 1972).

124. Op. Tenn. Att'y Gen. No. 221 (July 30, 1982), *reprinted in* [5] Cons. Cred. Guide (CCH) para. 96,824.

125. *See, e.g.*, *Fisher/Omaha*, 548 F.2d at 260; *Northway Lanes*, 464 F.2d at 862-64; *Danforth*, 394 F. Supp. at 784; *Comm'r*, 268 Md. at 315, 300 A.2d at 691-92; OCC Interpretive Letter No. 255, *supra* note 87.

126. OCC Interpretive Letter No. 255, *supra* note 87.

127. OCC Interpretive Letter No. 333, *supra* note 111.

128. *See e.g.*, Fla. Stat. Ann. § 687.12 (West Cum. Supp. 1987) (as to "loans ... made ... in the State of Florida"); Pa. Stat. Ann. tit. 7, § 6020-101(a)(26) (Purdon Cum. Supp. 1987); Tenn. Code Ann. § 45-4-602(a)(2) (Supp. 1987).

129. *See* Culhane and Kaplinsky, *supra* note 2, at 1336-39.

130. 394 F. Supp. 774.

131. *Id.* at 780-81.

132. *Id.* at 778, 784. The court could instead have interpreted the exemption to prohibit licensed lenders from offering credit sale financing.

133. *Id.* at 784-85.

134. *Id.* at 783. *See supra* text accompanying notes 41-45.

135. *See* Arnold and Rohner, *supra* note 2, at 18.

136. 548 F.2d 255. *See Partain*, 467 F.2d at 173-74 ("[o]bviously, national bank loans are not required in all their characteristics to fit snugly into the mold used by State lending institutions to shape their loans.").

137. 548 F.2d at 259-61.

138. The court is the state's highest court.

139. 294 Md. 385, 450 A.2d 1273.

140. State banks were also party plaintiffs in the case. *Id.* at 388-89, 450 A.2d at 1276-77.

purchases, as opposed to cash advances, are subject to the Retail Credit Accounts Law (RCAL).[141] The court held that unsecured cash advances and credit card purchases constitute different classes of "loans" under section 85 and the OCC Ruling.[142] It distinguished *Danforth* on the basis that the Missouri usury framework discriminated in favor of licensed lenders as to retail sales financing, while Maryland law did not.[143] The *Equitable Trust* court criticized *Fisher/Omaha* for applying a "transactional homogenization analysis" to compensate for the absence under Nebraska law of the type of discrimination which existed in *Danforth*.[144]

The OCC staff also narrowly construed the "class of loans" test in an opinion letter issued after the *Danforth* opinion but before the *Equitable Trust* decision.[145] It noted that the Michigan Retail Installment Sales Act (RISA) did not apply to transactions involving money, and concluded that a national bank could not apply the RISA's rates to cash advance transactions under a credit card program.[146] Thus, as in *Equitable Trust*, the OCC staff treated credit card cash advances and purchases as different classes of loans. The only distinction is that in Michigan the RISA was inapplicable to loans generally, while in Maryland the RCAL was applicable to lenders in credit sales, a separate class of loan.

This OCC staff letter raises questions concerning the *Danforth* court's application of the OCC Ruling. The *Danforth* court assumed without analysis that Missouri SLA rates were applicable to closed-end and open-end credit sales.[147] Reconciling the *Danforth* and OCC staff approaches ultimately depends on the interpretation of section 85 and the applicability and persuasiveness of the OCC Ruling, *Equitable Trust*, and the OCC staff letter. These matters turn on whether section 85 was designed to achieve parity between national banks and other lenders or transactional homogenization. Based on *Tiffany*, it is clear that competitive equality between national and state banks was not intended when lenders in general could charge a higher rate than state banks.[148] It also is clear that competitive equality between national banks and lenders in general does not exist when the exception clause applies; in that case, only national banks have parity with state banks.[149] In fact, the "any loan . . . or other evidences of debt" language of section 85, when read in light of *Tiffany*, strongly suggests that Congress focused on different classes of lenders, rather than different classes of loans.[150]

On the other hand, national banks inevitably borrow their rates directly or indirectly from, and are thus in an equal competitive position with, some other type of lender.[151] When a state establishes its rate structure according to types of credit transactions rather than groups of lenders, rate parity still should exist among at least some classes of lenders.[152] In this situation, national banks arguably should be limited to the rates prescribed for a particular type of transaction when engaging in such a transaction so as to promote competitive equality.[153] In *Danforth*, however, the court's decision that SLA rates were applicable to credit card purchase transactions necessarily determined that the Missouri rate structure for credit sales was organized by classes of lenders rather than classes of loans. *Danforth* and the OCC letter are consistent because the respective statutory structures differ.

The apparent lesson of *Danforth* and subsequent OCC and court decisions is that there is no generally accepted method of classifying consumer credit transactions. While the *Danforth* court's approach seems more consistent with the language of section 85,[154] a court interested in preserving strict competitive equality based on classes of transactions is likely to opt for the analysis of *Equitable Trust* or the OCC staff letter.[155] National banks therefore should be cautious in selecting a state law from which to borrow rates and terms.

(4) "Material to the Determination of the Interest Rate"

The three-part test of "materiality"[156] established by the Liebesman letter[157] permits an organized examination of the provisions of state law a court would be likely to consider as "material to the determination of the interest rate." Many of the cases discussed below were decided based on an analysis of section 85 rather than the OCC Ruling.[158] Nevertheless, they offer some guidance regarding the scope of state law coverage under the Ruling.

(a) State laws establishing characteristics of loan categories

State laws that establish loan characteristics are clearly "material to the determination of the interest rate." Both the *Equitable Trust*[159] court and the OCC staff[160] have ruled that statutory loan ceilings are material. Similarly, *Equitable Trust*[161] and the OCC staff[162] have considered maximum maturity restrictions material. Finally, provisions establishing classes of borrowers, either according to the class of loan sought[163] or the nature of security required,[164] are material.

141. *Id.* at 406, 450 A.2d at 1285.

142. *Id.* at 413-14, 450 A.2d at 1290. *Cf.* Acker v. Provident Nat'l Bank, 512 F.2d 729, 734 (3d Cir. 1975) (credit card purchase is not a "loan" under Pennsylvania Bank Code).

143. *Id.* at 404-406, 450 A.2d at 1285-86.

144. *Id.* at 408-09, 450 A.2d at 1287. The court even suggested that *Marquette* applied a "class of loans" analysis in describing the rate structures under the Nebraska and Minnesota bank credit card laws. *Id.* at 411-12, 450 A.2d at 1288-89. It seems more likely, however, that the parties and the Court purposely did not mention the rates available under the Minnesota Small Loan Act so as to avoid presenting the issue of whether a national bank may import the rates allowed in the borrower's home state. *Marquette*, 439 U.S. at 308.n.19. In fact, the posture of the case narrowed the issue solely to whether Omaha Bank was "located" in Nebraska under section 85. *Id.* at 308.

145. OCC Interpretive Letter No. 178, *supra* note 78.

146. *Id.* at 77,390. The letter also admonished the bank "to establish controls to ensure that higher rates are not charged on excluded transactions." *Id.* at 77,390-91.

147. *See supra* note 132 and accompanying text. *See also* Arnold and Rohner, *supra* note 2, at 20.

148. *See supra* text accompanying notes 21-22.

149. *See supra* text accompanying notes 27-28.

150. *See supra* text accompanying notes 80-81. *But see* Northway Lanes, 464 F.2d at 862 (citing Cong. Globe, 38th Cong., 1st Sess. 2123-26 (1864) (remarks of Sen. Grimes)).

151. *See supra* text accompanying notes 66-72. *See also infra* text accompanying notes 383-408 regarding the extent to which section 521 of DIDMCA, 12 U.S.C. § 1831d (1982), was intended to accord state banks rate-charging parity with national banks.

152. A case could occur where all classes of lenders except one (i.e., small loan law licensees) are prohibited from engaging in a certain kind of transaction (i.e., a $500 loan) at the highest available rate. *See supra* note 129. Even in this case, however, a national bank is entitled to borrow the small loan licensees' rate.

153. *See* Arnold and Rohner, *supra* note 2, at 20.

154. *See supra* text accompanying notes 80-81 & 150.

155. *See supra* text accompanying notes 77-78 & 151-153.

156. *See supra* text accompanying note 99.

157. *Supra* note 98.

158. Several state courts have applied the "materiality" test in cases involving state banks which sought to operate as most favored lenders. *See Equitable Trust*, 294 Md. 385, 450 A.2d 1273. *See also infra* text accompanying notes 421-430.

159. 294 Md. at 419, 450 A.2d at 1292.

160. OCC Interpretive Letter No. 178, *supra* note 78, at 77,391.

161. 294 Md. at 421-22, 450 A.2d at 1293-94. The court applied a closed-end loan maturity provision to open-end credit card transactions.

162. OCC Interpretive Letter No. 333, *supra* note 111.

163. *Id.* (purchase money loans); Liebesman letter, *supra* note 98 (consumer loans versus business loans).

164. OCC Interpretive Letter No. 333, *supra* note 111 (first lien on residential property that is borrower's principal dwelling).

(b) State laws establishing manner in which numerical rate is determined.

Except where otherwise noted, the courts or the OCC have determined that rate computation laws are "material" to the rate determination. In two separate letters, the OCC staff has stated that the authority to charge a variable interest rate[165] and the provisions that restrict the variation of the rate[166] are material.

The leading case for the proposition that a restriction or prohibition against compounding interest is, in effect, material is *Citizens' National Bank v. Donnell.*[167] The Supreme Court held in *Donnell* that the bank violated a state law prohibiting the compounding of interest more than once a year even though the rate remained within the usury limit.[168] The Courts of Appeals for the Third[169] and Fifth[170] Circuits have followed *Donnell.*

Court decisions also indicate that state restrictions on day-count methods are material. In *American Timber & Trading Co. v. First National Bank,*[171] the Ninth Circuit held that a national bank may not use the 365/360 day-count method when that method would yield a rate in excess of the state usury limit.[172] Conversely, a federal district court upheld the use of the 365/360 method where permitted by state law.[173] Additionally, the OCC staff has permitted national banks to use the 365/360 method in calculating interest pursuant to the option in section 85 permitting national banks to charge one percent over the discount rate.[174]

Finally, concerning miscellaneous rate calculation issues, the *Equitable Trust* court held that the after maturity rate, which would take effect six months following the maturity date of a loan, was material.[175] Moreover, the OCC staff has suggested that a national bank may be entitled to charge the rate permitted by state law at the time a loan commitment is made, rather than the lower rate authorized at closing.[176]

(c) State laws affecting ultimate return on loan proceeds

(i) Discounting interest

The controversy concerning whether and to what extent section 85 authorizes the charging of discount interest and therefore preempts conflicting state laws is one of the most important unresolved issues in the interstate lending area. It has highlighted the most fundamental issue in this area: to what extent is state law incorporated in section 85?[177] Although discounting clearly is a rate calculation issue, and thus normally would fit into the Liebesman letter's second category,[178] this controversy and the larger issue of the reach of state law caused Liebesman to create a third category covering state law provisions which merely affect the yield on loan proceeds.[179]

The case which engendered this controversy is the 1919 decision in *Evans v. National Bank.*[180] In *Evans*, the Supreme Court held that a national bank may discount short-term single payment commercial paper at the maximum rate permitted by state law, although the effective rate will exceed the usury limit.[181] The Court relied on its earlier decisions in *Farmers' & Mechanics' National Bank v. Dearing*[182] and *National Bank v. Johnson*[183] for the proposition that the National Bank Act adopts state laws only to the extent that they fix the numerical rate of interest.[184] Another pre-*Evans* line of cases[185] culminating in *Citizens' National Bank v. Donnell*[186] provides that the intent of section 85 is to adopt state law generally.

This dichotomy apparently was submerged for more than fifty years until it reemerged in *Northway Lanes v. Hackley Union National Bank & Trust Co.*[187] and *First National Bank v. Nowlin.*[188] Michigan law permitted discounting, so the Sixth Circuit in *Northway Lanes* did not have to confront limiting *Evans.* Nevertheless, the court observed that under the reasoning of *Evans*, the right to charge interest in advance "arises independent of state laws which are binding on state banks."[189] In contrast, the Eighth Circuit in *Nowlin* faced the issue and limited *Evans* to "its own facts of single payment short-term paper."[190] The court therefore held that a national bank violated Arkansas usury law by discounting interest at the maximum rate on an installment loan.[191] The OCC has issued two staff letters since *Northway Lanes* and *Nowlin* that discuss discounting. The first provides that national banks may discount interest pursuant to the option in section 85 permitting national banks to charge one percent over the discount rate.[192] The latter declines to determine whether a national bank may discount interest on installment loans when its state-chartered competitors cannot.[193]

Although section 85 is not clear regarding national banks' authority to discount interest, the National Bank Act taken as a whole and the federal preemption incorporated in the Act support discounting of interest at the maximum rate allowed by state law. The "powers" section of the National Bank Act specif-

165. OCC Interpretive Letter No. 354 from Roberta W. Boylan, Director of the Legal Advisory Services Division (Nov. 18, 1985), *reprinted in* [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) para. 85,524 (equates variable rate lending authority with absence of restriction on frequency of rate changes, but locates "no judicial pronouncements on point."). *See Hiatt*, 361 F.2d at 507 (even where national and state banks were exempt from state usury laws, a "rate" was "fixed" by state law under section 85).

166. OCC Interpretive Letter No. 333, *supra* note 111.

167. 195 U.S. 369 (1904) (decided under section 85).

168. *Id.* at 374.

169. Haas v. Pittsburgh Nat'l Bank, 526 F.2d 1083, 1094-95 (3d Cir. 1975) (decided under section 85); Acker, 512 F.2d at 740-42 (decided under section 85).

170. *Partain*, 467 F.2d at 173-78 (national bank may "borrow" appropriate state law, but still violate state's prohibition against compounding) (decided under section 85). *But see* Fourchon, Inc. v. Louisiana Nat'l Leasing Corp., 723 F.2d 376, 382-86 (5th Cir. 1984) (interest chargeable as agreed by the parties under Preferred Ship Mortgage Act, 46 U.S.C. § 926(d) (1982), so national bank not bound by state restrictions on compounding).

171. 511 F.2d 980 (9th Cir. 1973) *cert. denied*, 421 U.S. 921 (1974) decided under section 85).

172. 511 F.2d at 983-85.

173. Voitier v. First Nat'l Bank, 514 F. Supp. 585, 594 (E.D. La. 1981).

174. OCC Interpretive Letter No. 102 from John E. Shockey, Chief Counsel (May 30, 1979), *reprinted in* [1978-1979 Transfer Binder] Fed. Banking L. Rep. (CCH) para. 85,177.

175. 294 Md. at 419-20, 450 A.2d at 1293.

176. OCC Interpretive Letter No. 81 from Richard V. Fitzgerald, Director of the Legal Advisory Services Division (Feb. 8, 1979), *reprinted in* [1978-1979 Transfer Binder] Fed. Banking L. Rep. (CCH) para. 85,156.

177. *See supra* text accompanying notes 38-40, 48-51, & 100-104.

178. *See supra* text accompanying note 99.

179. *See supra* text accompanying notes 99-105.

180. 251 U.S. 108.

181. *Id.* at 114.

182. 91 U.S. 29.

183. 104 U.S. 271.

184. 251 U.S. at 111.

185. *Daggs*, 177 U.S. 549; *Union Nat'l Bank*, 163 U.S. 325.

186. 195 U.S. 369 (compounding).

187. 464 F.2d 855.

188. 590 F.2d 872.

189. 464 F.2d at 860-61. *See Ray*, 443 F. Supp. at 887-88 (relied on *Northway Lanes*).

190. 590 F.2d at 876.

191. *Id.* at 876-80. *See* Cohen v. District of Columbia Nat'l Bank, 382 F. Supp. 270, 283-84 (D.D.C. 1974) (combination of discounting with interest-only installment payments at maximum rate held usurious) (decided under section 85).

192. OCC Interpretive Letter No. 101 from John E. Shockey, Chief Counsel (May 9, 1979), *reprinted in* [1978-1979 Transfer Binder] Fed. Banking L. Rep. (CCH) para. 85,176.

193. *Id.* No. 115 from Ford Barrett, Assistant Chief Counsel (August 10, 1979), *reprinted in* [1978-1979 Transfer Binder] Fed. Banking L. Rep. (CCH) para. 85,190.

ically authorizes banks to discount promissory notes and other evidences of debt.[194] Further, section 85 allows national banks to "reserve" interest on loans, discounts, or other evidences of debt.[195] Under this theory, state law only determines the rate of interest, but federal law determines how the rate is to be charged. This argument is appealing based on a literal reading of section 85. It becomes even more appealing assuming that *Marquette* stands for federal preemption,[196] under which state law establishing the rate obtains the status of federal law, which already permits national banks to discount loans.

This argument has several weaknesses, however. First, the third clause of section 85, which was emasculated by *Daggs* and *Hiatt*, provides that "interest may be taken in advance" at the "federal" rate set forth therein.[197] While the introductory language to the allowance and exception clauses permits reserving of interest, it does not expressly authorize the charging of interest in advance. Moreover, *Nowlin* recognizes a substantial difference between the effective rate in discounting installment notes versus discounting short-term single payment notes.[198] It is not clear that Congress contemplated installment lending when it enacted the National Bank Act; accordingly, *Evans* should not extend to installment lending.[199] Finally, to the extent that Congress was concerned about competitive equality among lenders, extending *Evans* in this way would contravene congressional intent.[200]

These countervailing arguments demonstrate the difficulty of resolving the discounting authority of national banks. This issue is unlikely to be resolved until the larger issue of the extent of the incorporation of state law in section 85 is settled.

(ii) Fees and charges

The courts and the OCC staff have treated several fees commonly charged in loan transactions as "material." The leading case is *Northway Lanes*,[201] in which the court permitted a national bank to charge "reasonable and necessary" closing costs on a commercial real estate loan pursuant to a Michigan law authorizing a state-chartered savings and loan association to impose such costs.[202] The statute at issue expressly provided that these closing costs were not "interest."[203] Despite this provision, in a subsequent letter (Fitzgerald letter), Richard V. Fitzgerald, then Director of the Legal Advisory Services Division of the OCC, cited *Northway Lanes* to the effect that "all charges permitted or prohibited by state law in connection with particular types of loans may be defined as 'interest.' "[204] The Fitzgerald letter permitted a national bank to charge an annual fee on the basis that it was "interest" under the borrower's home state's laws, not that it was "material" to the rate.[205] A state court held that a national bank may not charge attorney's fees when such fees are prohibited under "borrowed" state law.[206] Finally, a federal district court held that a national bank is subject to a prohibition against assessing fees and service charges on overdraft checking accounts if such fees are not included in a written agreement.[207]

The *Equitable Trust* court held the following fees or prohibitions against charging fees to be "material": bad check charges,[208] credit insurance charges,[209] fees received from a third party for making a loan,[210] disguised service charges,[211] and prohibitions against charging prepayment penalties[212] and unauthorized fees.[213]

(iii) Miscellaneous requirements

The court in *Equitable Trust* also deemed a variety of other statutory provisions to be "material." These provisions include a prohibition on loan splitting to obtain higher rates,[214] limitations on the interest includible in the principal balance or deductible from the proceeds on refinancing,[215] application of payments requirements,[216] and a requirement to credit the loan balance with the amount received on the sale of security.[217]

(iv) Consumer protections

The OCC staff has stated in two opinions that disclosure requirements are not material.[218] Moreover, the *Equitable Trust* court held that a provision subjecting a lender to the claims and defenses which a borrower may have against a seller of goods is not material.[219] The requirement of disclosing lawful fees in writing in order to exclude them from the calculation of interest may, however, be material.[220]

(5) State Licensing Exemption

The last sentence of the OCC Ruling provides that national banks may charge the most favored state-supervised lender's rates without being licensed by the state.[221] This merely recognizes the federal banking laws' virtually complete exemption of national banks from state licensing, supervision, and examination requirements.[222] The National Bank Act broadly authorizes national banks to

194. 12 U.S.C. § 24 (Seventh) (Supp. V 1987).

195. *Id.* § 85 (1982).

196. *See infra* text accompanying notes 252-260. *See also* Schellie, *Marquette: A Sound Legal and Social Result*, J. Retail Banking, June 1979, at 85, 92-93 [hereinafter cited as Schellie].

197. 12 U.S.C. § 85 (1982). *See* Brophy, *State Usury Laws and National Banks*, 31 Baylor L. Rev. 169, 180 n.44 (1979).

198. 590 F.2d at 876.

199. *Id.*

200. *See supra* text accompanying notes 150-153.

201. 464 F.2d 855.

202. *Id.* at 864.

203. *Id.* at 863.

204. Fitzgerald letter, *supra* note 97, at 3.

205. *Id. See* Rosenblum, *supra* note 2, at 1040. *But see id.* at 1044 n.24 and cases cited therein (annual fee traditionally not considered interest because paid by borrower for convenience of using, i.e., credit card account); Burke and Kaplinsky, *supra* note 2, at 1106 & n.146 (same).

206. Rockland-Atlas Nat'l Bank v. Murphy, 329 Mass. 755, 760-61, 110 N.E.2d 638, 641-42 (1953) (decided under section 85). This outcome suggests that if a law permitted these fees to be charged, they would be considered "material," although it is unlikely that they would be deemed "interest."

207. Landau v. Chase Manhattan Bank, 367 F. Supp. 992, 999 (S.D.N.Y. 1973) (may also be viewed as a disclosure provision) (decided under section 85). *See infra* text accompanying note 220.

208. 294 Md. 385, 422, 450 A.2d 1273, 1294.

209. *Id.* at 423, 450 A.2d at 1294. *See* Op. Mich. Att'y Gen. No. 6133 (Mar. 4, 1983) (unpublished).

210. 294 Md. at 422, 450 A.2d at 1294.

211. *Id.* at 418, 450 A.2d at 1292 (i.e., paying discounted price for wage assignment, with difference treated as "interest").

212. *Id.* at 422, 450 A.2d at 1294. *But see* Northway Lanes, 464 F.2d at 864 (prepayment penalty not "interest").

213. 294 Md. at 418, 450 A.2d at 1292. The court noted that, under the rationale of *Donnell*, the charging of an unauthorized fee is a violation even if it does not result in a usury violation. *See* Op. Mich. Att'y Gen. No. 6133, *supra* note 209.

214. 294 Md. at 419, 450 A.2d at 1292. *But see* OCC Interpretive Letter from Richard V. Fitzgerald, Director of the Legal Advisory Services Division, to Alan Kaplinsky (Dec. 15, 1980) (unpublished) (where national bank made two different loans under two different laws with different rates, and there was no intent to evade the law, loan splitting provision was not material).

215. 294 Md. at 420, 450 A.2d at 1293.

216. *Id.* at 422, 450 A.2d at 1294.

217. *Id.* at 418-19, 450 A.2d at 1292-93.

218. OCC Interpretive Letter No. 333, *supra* note 111 (notes that, based on federal instrumentality doctrine, in absence of federal statute or regulation, national banks still subject to law applicable to them, including disclosure requirements); *Id.* No. 178, *supra* note 78.

219. 294 Md. at 422, 450 A.2d at 1294.

220. *Landau*, 367 F. Supp. at 999.

221. *See* 12 C.F.R. §7.7310(a) (1987).

222. 12 U.S.C. § 484(a) (Supp. V 1987). The only limitation on the exemption is that state examiners may review national banks' records "solely to ensure compliance with applicable State unclaimed property or escheat laws upon reasonable cause to believe that the bank has failed to comply with such laws." *Id.* § 484(b). *See* 12 C.F.R. § 7.6025(b) (1987).

exercise "all such incidental powers as shall be necessary to carry on the business of banking."[223] The OCC staff has interpreted the Act to exempt national banks from state licensing and reporting requirements.[224] Commerce clause principles also may be used to attack state licensing requirements. For example, where a state requires licensing for real estate-secured second mortgage lending but denies licensing to out-of-state financial institutions, the restriction may be both discriminatory and burdensome to commerce and, therefore, impermissible absent federal authorization.[225] Thus, based on federal banking laws and constitutional principles, national banks should have an exemption from state licensing, bonding, and reporting requirements under the OCC Ruling at least as broad as that held by federal savings institutions under the Federal Home Loan Bank Board's Interpretive Ruling (the FHLBB Ruling) regarding most favored lender status.[226]

B. Exportation of Interest Rates

The one certainty in the area of interstate lending is that a national bank may "export" the interest rate allowed by the laws of the state where it is located to borrowers residing in other states.[227] This statement may mislead national banks into believing that there are no remaining issues concerning their rate exportation rights. A close reading of the Supreme Court's ruling in *Marquette National Bank v. First of Omaha Service Corp.*,[228] however, reveals several unresolved questions for national banks to consider as their operations become more nationwide in scope with the advent of interstate banking and new banking powers.

1. Where is a National Bank "Located"?

At first glance, the answer to this question seems simple: *Marquette* held that a national bank is "located" for purposes of section 85 in the state named in its organization certificate.[229] The State of Minnesota contended, however, that Omaha Bank's systematic solicitation of Minnesota residents under its BankAmericard program mandated a different conclusion.[230] Although the court could have rested on its holding, it conducted an apparent federal common law choice-of-law analysis[231] before confirming its conclusion.

The Court initially noted that Omaha Bank did not operate any branch banks in Minnesota, nor could it under federal banking laws.[232] It then declared that the Nebraska bank's location did not change merely because it was extending interstate credit; the Court compared receipt of a direct mail loan solicitation to traveling to another state to obtain credit. The Court proceeded to determine where Omaha Bank (1) extended credit by honoring sales drafts, (2) assessed finance charges, (3) received payments, (4) issued credit cards, and (5) approved credit applications.[233] After determining that all of these activities occurred in Nebraska, the Court dismissed the argument that the use of the credit cards at Minnesota merchants' and banks' premises outweighed the Nebraska contacts, declaring:

> If the location of the bank were to depend on the whereabouts of each credit-card transaction, the meaning of the term "located" would be so stretched as to throw into confusion the complex system of modern interstate banking. A national bank could never be certain whether its contacts with residents of foreign States were sufficient to alter its location for purposes of § 85. We do not choose to invite these difficulties by rendering so elastic the term "located."[234]

In the decade since the Court decided *Marquette*, the national banking system has grown more complex. While customers still may use credit cards nationwide and even worldwide, financial institutions now frequently operate branches, transaction processing centers, and affiliates in many different states. While the Supreme Court indicated that it will not engage in a *transaction*-oriented determination of where a national bank is "located" under section 85, it in fact analyzed Omaha Bank's entire credit card *program* to confirm that determination. Consequently, national banks having more than incidental contacts with several states may need to reevaluate where they are "located" for section 85 purposes.[235]

2. Can a National Bank Import Rates?

The Court in *Marquette* declined to address whether Omaha Bank could "import" rates allowed by Minnesota law which were higher than those allowed by Nebraska law in its transactions with Minnesota residents.[236] In a case decided before *Marquette*, however, the Seventh Circuit in *Fisher/Chicago*[237] indicated in dicta that a national bank could borrow and then import the rate allowed for state banks in the borrower's home state.[238] Six months later, in *Fisher/Omaha*,[239] the Eighth Circuit stated in dicta that a national bank would be entitled to import the rate permitted to the most favored lender in the borrower's home state.[240] The Fifth Circuit also has endorsed importing in dicta.[241] All of these courts relied on the "laws of *any* State" and "organized or *existing*" phraseology in the exception clause of section 85[242] in reaching their conclusions. At least one commentator has instead interpreted the term "existing" to refer to state banks that have converted to national charters.[243] This interpretation

223. 12 U.S.C. § 24 (Seventh) (Supp. V 1987). *See id.* § 24 (Fourth) (1982).

224. OCC Interpretive Letter from Roberta W. Boylan, Assistant Director of the Legal Advisory Services Division (Nov. 20, 1980) (unpublished); *id.* from John E. Shockey, Chief Counsel (July 19, 1977) (unpublished). *See* Bank of America v. Lima, 103 F. Supp. 916, 918 (D. Mass. 1952).

225. *See Lewis*, 447 U.S. 27; U.S. Const. art. 1, § 8, cl. 3.

226. 12 C.F.R. § 570.11 (1987).

227. *Marquette*, 439 U.S. at 313-18.

228. *Id.* at 299.

229. *Id.* at 310.

230. *Id.* at 309-310.

231. *See, e.g.*, Seeman v. Philadelphia Warehouse Co., 274 U.S. 403, 407 (1927) (employed a "substantial relationship" test).

232. 439 U.S. at 309.

233. *Id.* at 310-12.

234. *Id.* at 312.

235. *Cf.* Citizens' & S. Nat'l Bank v. Bougas, 434 U.S. 35 (1977) (construed venue provision of National Bank Act, since amended, 12 U.S.C. § 94 (Supp. V 1987), to provide that national bank located either in place designated in its organization certificate or in places where it has established authorized branches).

For example, if an organization certificate listed Delaware as a national bank's home state, but the bank operated a credit card processing center in Illinois at which it conducted payment and sales draft processing, card issuance, and other functions, an Illinois or even a non-Illinois resident-customer might allege that Illinois law applied to the program.

236. 439 U.S. at 308 n.19. *See supra* note 144.

237. 538 F.2d 1284.

238. *Id.* at 1290-91.

239. 548 F.2d 255.

240. *Id.* at 257-58. This extension is unwarranted; the exception clause is clearly limited to permitting national banks to charge the rate allowed for state banks. *See supra* text accompanying note 28.

241. FDIC v. Lattimore Land Corp., 656 F.2d 139, 149-150 n.18 (5th Cir. 1981).

242. *See* Rohner, *Marquette: Bad Law and Worse Policy*, J. Retail Banking, June 1979, at 76, 79 (national bank "exists" in any state into which it makes loans).

243. *See A Contrary View*, *supra* note 21, at 1098-99 n.132.

may cast doubt on the validity of the three federal appellate courts' dicta authorizing rate importation.

A national bank apparently may instead employ general conflict of laws principles to import rates. Under these principles, if the loan contract provides that the borrower's home state's laws will apply, and the law of the bank's home state allows state-chartered lenders to apply those laws, then section 85 permits a national bank to do likewise.[244] The OCC staff has applied this type of choice-of-law analysis to authorize rate importing in two instances.[245] A national bank desiring to employ a choice-of-law analysis to import rates should evaluate carefully whether the choice-of-law rules of its home state will cause the law of the borrower's home state to apply. The inclusion of a carefully drafted choice-of-law provision in a credit agreement is particularly important if a national bank is relying on a conflict of laws analysis to import rates.

Of course, whether a national bank may employ a state, as opposed to a federal, common law choice-of-law analysis depends on whether or not section 85 incorporates the entire case law of the bank's home state, including its choice-of-law rules.[246] To the extent that the federal and state conflict of laws rules are similar, however, the use of a particular set of rules probably will not affect the ultimate determination regarding rate importation.

3. Usury Penalties

The National Bank Act establishes the penalty for a violation of section 85,[247] and that penalty supersedes state usury penalties.[248] A violation is deemed a forfeiture of the entire interest paid and the borrower may recover twice the interest paid.[249] The statute of limitations is two years from the time the borrower makes and the bank receives and appropriates payment of usurious interest, not from the time the entire debt is paid.[250]

C. Exportation of Fees and Other Contract Terms

1. Marquette

Marquette does not address directly the issue of what fees and other contract terms, if any, a national bank may export. *Iowa ex rel. Miller v. Citibank (South Dakota)*[251] may ultimately determine the scope of national banks' exportation rights; pending this determination, however, an examination of some of the key principles underlying the *Marquette* decision offers some guidance in resolving this issue.

a. Federal Preemption

There is substantial authority in the Supreme Court's opinion that *Marquette* stands for federal preemption as opposed to a broad incorporation of state law in section 85.[252] The Court initially notes that a national bank is a federal instrumentality "subject to the paramount authority of the United States."[253] It then cites *Farmers' & Mechanics' National Bank v. Dearing*,[254] previously relied on in *Evans* for the proposition that state law fixes only the numerical rate,[255] to the effect that the rate a national bank may charge is governed by federal law.[256] The court employs a federal common law choice-of-law analysis to confirm that, for the purposes of section 85, a national bank is "located" in the state named in its organization certificate.[257] Thus, in order to prevent "confusion in the complex system of modern interstate banking," the Court determines that section 85 preempts conflicting state law.[258] The Court finally notes that the impairment of states' "ability to enact effective usury laws [is] implicit in the structure of the National Bank Act."[259]

Thus, the effect of the Court's federal choice-of-law analysis concerning where a national bank is "located" is to proclaim the federal preemption of conflicting state law interpretations of the provisions of section 85. Under this preemption analysis, the term "interest" in section 85 is also defined under federal law.[260] Accordingly, a national bank may export not only its interest rate, but also whatever fees and other contract terms are deemed "interest" under federal law. The only question is what federal law establishes the definition of "interest" under section 85. As one commentator has advocated,[261] the policies of promoting stability in the interstate banking system and establishing federal supremacy in usury regulation enunciated in *Marquette* support a broad definition of the term.[262]

b. Choice-of-Law

Even if *Marquette* does not express a broad principle of federal preemption, it implies a choice-of-law rule favoring application of the laws of a national bank's home state. This is the case even when application of the rule results in a conflict with a policy of the borrower's home state favoring extraterritorial application of its laws. The effect of the Court's decision was to invalidate the application of the Minnesota extraterritoriality provision[263] to out-of-state national banks, at least as to interest rates.

The Minnesota statute applied in a nondiscriminatory manner to both state and national banks located in Minne-

244. *See* Arnold and Rohner, *supra* note 2, at 37.

245. OCC Interpretive Letter No. 325, *supra* note 51; *id.* No. 116 from Donald A. Melbye, Special Assistant for Congressional Affairs (Aug. 17, 1979), *reprinted in* [1978-1979 Transfer Binder] Fed. Banking L. Rep. (CCH) para. 85,191.

246. *See supra* text accompanying notes 48-51 & 177-186.

247. 12 U.S.C. § 86 (1982). Section 86 provides as following:

> The taking, receiving, reserving, or charging a rate of interest greater than is allowed by the preceding section, when knowingly done, shall be deemed a forfeiture of the entire interest which the note, bill, or other evidence of debt carries with it, or which has been agreed to be paid thereon. In case the greater rate of interest has been paid, the person by whom it has been paid, or his legal representatives, may recover back, in an action in the nature of an action of debt, twice the amount of the interest thus paid from the association taking or receiving the same: Provided, that such action is commenced within two years from the time the usurious transaction occurred.

Id.

248. McCollum v. Hamilton Nat'l Bank, 303 U.S. 245 (1938); Evans, 251 U.S. at 109; Schuyler Nat'l Bank v. Gadsden, 191 U.S. 451 (1903).

249. McCarthy v. First Nat'l Bank, 223 U.S. 493, 499 (1912) (actual payment of interest necessary to recover twice interest paid); Ellis Nat'l Bank v. Davis, 359 So. 2d 466 (Fla. App. 1976), *cert. denied*, 440 U.S. 976 (1979) (even though loan not usurious at inception, penalty is twice entire amount of interest collected, not just twice the usurious interest). *See* 12 U.S.C. § 86 (1982).

250. McCarthy, 223 U.S. 493. *See* 12 U.S.C. § 86 (1982).

251. Civ. No. 88-189-E (S.D. Iowa, filed Apr. 11, 1988).

252. *See supra* text accompanying notes 48-51 & 177-186 concerning the scope of incorporation of state law in section 85.

253. 439 U.S. at 308.

254. 91 U.S. 29, 34, *cited in Marquette*, 439 U.S. at 308.

255. 251 U.S. at 111.

256. 439 U.S. at 308. If read literally, this conclusion would leave no role for state law under section 85. Obviously, the opinion indicates otherwise. *Id.* at 303.

257. *Id.* at 310.

258. *Id.* at 312-13. *See* Schellie, *supra* note 196, at 92-93.

259. *Id.* at 318-19.

260. *See supra* text accompanying notes 254-256. Moreover, while rates may be a matter of state law under the allowance clause, the language of section 85 does not suggest that the term "interest" is defined under state law. For an analogous situation, *see* First Nat'l Bank v. Dickinson, 396 U.S. 122 (1968), *cited in* Rosenblum, *supra* note 2, at 1041-42 (definition of "branch" under 12 U.S.C. § 36 (Supp. V 1987) as a matter of federal law).

261. Rosenblum, *supra* note 2, at 1042.

262. *See supra* text accompanying notes 258-259. *See also infra* text accompanying notes 276-295.

263. Minn. Stat. § 48.185, Subd. 6 (1976), *cited in Marquette*, 439 U.S. at 302-03 n.4. The statute provided that the Minnesota bank lending law would apply to all open-end credit transactions between a bank or a savings bank and a Minnesota resident.

sota, and purported to apply to out-of-state national (and state) banks.[264] The Supreme Court nevertheless determined, on the basis of *Tiffany* and the legislative history of the National Bank Act, that the Act contemplated the inequalities that occur among in-state and out-of-state national and state banks when a national bank exports its interest rate to borrowers residing in other states.[265]

The effect of exportation, as the Court stated, is to "significantly impair the ability of States to enact effective usury laws."[266] This statement can be interpreted to cast doubt on the validity of not only the interest rate provisions, but all aspects, of a state's loan laws as applied to out-of-state national banks.[267] In fact, the interest rate can be viewed as the most fundamental component of a state's usury scheme. Because section 85 preempts state rate ceilings as applied to out-of-state national banks, a national bank should be entitled to export all aspects of its most favored lender status to other states.[268] A national bank is only accorded true interest rate parity with state-supervised lenders located in its home state if it can borrow fees and other terms which are "material to the determination of the interest rate" under its home state's law.[269] The holding of *Marquette*, however, only applies to interest rates; this dicta merely suggests that the rule of the case may extend to fee, or even other, provisions of state laws.

c. Federal Instrumentality Doctrine

Even assuming a broad incorporation of home state law in section 85,[270] national banks also may contend that their status as federal instrumentalities entitles them not to comply with the laws of the various "foreign" states where their borrowers reside. Under the federal instrumentality doctrine, national banks are not subject to state law if it conflicts with, or frustrates the purpose of, federal legislation or disrupts them in their performance as federal "agencies."[271] The National Bank Act establishes national banks and empowers them to exercise "all such incidental powers as may be necessary" to make loans.[272] Thus, under the doctrine, national banks' compliance with numerous states' laws may either frustrate the Act's intent, as determined by *Marquette*, to create a national banking system,[273] or unduly disrupt their interstate lending operations.

The federal instrumentality doctrine, as applied to interstate lending, transforms the conflict of laws analysis from one that generally determines which of two states' laws applies to one which weighs federal law and policy against the conflicting demands of many states' laws. The enormous burden that confronts national banks which attempt to comply with various states' laws in nationwide lending programs may constitute a sufficient impairment to justify application of *Marquette* to non-rate loan terms.[274] Thus, even the legitimate state interest in regulating non-rate aspects of foreign national banks' operations may yield to the need to preserve national banks' efficacy as federal instrumentalities. Nevertheless, it may be unwarranted to assign too much weight to the general intent of the National Bank Act when Congress has failed to preempt state fee restrictions, as well as many state consumer protection requirements.[275]

2. Scope of "Interest" Under Section 85

The scope of the term "interest" ultimately may depend on whether it is defined under federal or state law, and, in the case of state law, the law of the bank's or the borrower's home state. If *Marquette* represents a federal preemption analysis,[276] then the term "interest" should be defined under federal law. On the other hand, if the case merely favors the application of the bank's home state's laws[277] or the federal instrumentality doctrine,[278] then those home state laws will control the definition. Finally, if general choice-of-law principles prevail, even the borrower's home state's laws may apply.[279]

Marquette provides little guidance concerning the meaning of the term "interest" under section 85. The Supreme Court suggests at one point, however, that at least the annual fee permitted under Minnesota law may be "interest," as it "compensate[s] for the reduced interest."[280] It is unclear whether the Court might be proposing a "yield"-oriented approach to defining "interest." Under this approach, all provisions of applicable law which "affect the ultimate return on loan proceeds" would be deemed "interest."[281] If adopted, this approach would approximate the scope of the "material to the determination of the interest rate" test under the OCC Ruling.[282] This would indeed establish a broad definition of the term.

A logical standard to apply under federal law is the definition of "finance charge"[283] under the Federal Reserve Board's Regulation Z[284] to the federal Truth-in-Lending Act.[285] The Regulation Z standard would provide national banks with an objective means of determining what constitutes "interest." More importantly, a recent change[286] to the Official Staff Commentary to Regulation Z would permit national banks to impose annual or periodic participation fees on credit card customers which would be considered "interest" under section 85. For example, charges for non-use of a credit card, and other charges based on

264. 439 U.S. at 309-10.

265. *Id.* at 313-19.

266. *Id.* at 318-19.

267. Certain state laws, such as those involving real estate, probate, and escheat of property, will remain generally applicable to national banks.

268. The Court apparently cited with approval the most favored lender aspects of the OCC Ruling. 439 U.S. at 314 n.26. *See generally* Rosenblum, *supra* note 2, at 1042.

269. Culhane and Kaplinsky, *supra* note 2, at 1349.

270. *See supra* text accompanying notes 48-51, 177-186, & 252-262.

271. *Luckett*, 321 U.S. 233; First Nat'l Bank v. Missouri, 263 U.S. 640, 656 (1924); *Davis*, 161 U.S. 275, 283.

272. 12 U.S.C. § 24 (Seventh) (Supp. V 1987).

273. 439 U.S. at 314-15.

274. The recent enactment of credit card disclosure laws by several states provides an example of conflicting state laws. *Compare* Cal Civ. Code § 1748.11 (West Cum. Supp. 1987) *with* N.Y. Gen. Bus. Law § 520 (McKinney Cum. Supp. 1988). If laws of a state other than a national bank's home state discriminate against out-of-state lenders and burden interstate commerce, they also may violate the commerce clause. *See supra* text accompanying note 225 and authorities cited therein. *Cf.* Bibb v. Navajo Freight Lines, Inc., 359 U.S. 520, 529-30 (1959) (multiple burdens from conflicting state laws outweigh state interest).

275. *See* Burgess, *supra* note 2, at 939-41; Arnold and Rohner, *supra* note 2, at 29.

276. *See supra* text accompanying notes 252-262; note 260 and authorities cited therein.

277. *See supra* text accompanying notes 263-269.

278. *See supra* text accompanying notes 270-275. The federal instrumentality doctrine would lead to the application of the law of the bank's home state on the assumption that section 85 incorporates the entire case law of the state interpreting limitations on usury. *See supra* text accompanying notes 48-51 & 177-186.

279. *See supra* text accompanying notes 244-246; *see infra* text accompanying notes 311-316 (extraterritorial choice-of-law provision).

280. 439 U.S. at 303-04.

281. *Supra* text accompanying notes 98-99 (Liebesman letter's test of "materiality" under OCC Ruling).

282. *See supra* text accompanying notes 187-220 (examples of terms which may affect yield).

283. 12 C.F.R. § 226.4(a) (1987).

284. *Id.* §§ 226.1-226.30 (1987).

285. 15 U.S.C. §§ 1601-1681 (1982).

286. 52 Fed. Reg. 10,875 (1987) (to be codified in Regulation Z Official Staff Commentary (1). 12 C.F.R. § 226.4(c) (1987)) (Comment 4(c)(4)-2).

either account activity or the amount of credit available are included in the "finance charge."[287]

The Regulation Z standard, however, fails to provide a broad definition of "interest." Moreover, as one commentator has noted, this standard applies criteria directed at disclosing borrowing costs to customers in order to determine what provisions of state loan laws affect a creditor's yield.[288] Thus, the "yield" approach suggested in *Marquette* is preferable from a policy perspective.

An OCC staff letter also proposes a broad federal definition of "interest." The Fitzgerald letter,[289] relying on *Northway Lanes*,[290] concludes that "all charges permitted or prohibited by state law in connection with particular types of loans may be defined as 'interest.' "[291] There are two problems with Fitzgerald's approach, however. First, the closing costs which the national bank in *Northway Lanes* was allowed to charge were not "interest" under Michigan law.[292] Moreover, most state laws do not consider an annual fee to be "interest."[293]

The principal weakness of all of the proposed definitions of "interest" is that they do not cover disclosure and other consumer protection requirements.[294] The use of the word "interest" in section 85 indicates a lack of congressional intent to displace state consumer protections.[295] Thus, even under a federal preemption analysis, some of the borrower's home state's laws might apply to an exporting national bank. The definitions of "interest" under state law, which would apply in any choice-of-law analysis, generally are similarly restricted in scope.

3. The OCC Ruling

The "materiality" test contained in the OCC Ruling generally will allow a national bank to borrow more aspects of its home state's laws than the definition of "interest" in section 85. The only question is whether the Ruling applies to interstate lending.

The OCC staff twice has declared that the OCC Ruling applies to interstate lending. The Liebesman letter authorized a New York-based national bank to export to South Carolina borrowers whatever fees and terms the bank concluded were "material" under the three-part test established therein.[296] The Liebesman letter, however, declined to state which fees and terms met the test.[297] In a 1985 letter, the OCC staff determined that a North Carolina-based national bank could export its variable rate lending authority to South Carolina borrowers, even though South Carolina law prohibited variable rate lending.[298] The staff cautioned the bank, however, that no court had yet decided whether the absence of restrictions on the frequency of interest rate changes constituted an authorization to make variable rate loans.[299]

The OCC staff's conclusion that the OCC Ruling applies to interstate lending clearly seems correct. The Ruling is intended to be an interpretation of section 85, which the *Marquette* Court held to apply to interstate lending.[300] A national bank thus may be able to apply the "materiality" test in the OCC Ruling to export a broad range of fees and terms,[301] particularly if other courts adopt the *Equitable Trust*[302] approach. In the face of a prohibition on the charging of a fee under the borrower's home state's law, the federal instrumentality doctrine may apply.[303] A court might invalidate the fee prohibition if it finds that a national bank's burden of complying with the limitations of the various other states in which the bank solicits customers, in addition to the laws of its home state, constitutes an undue interference with its operations. In such a case, national banks are advised to emphasize the strong federal policy of facilitating a nationwide banking system enunciated in *Marquette*.[304]

4. Choice-of-Law

Even if a court rejects the application of federal preemption, the federal instrumentality doctrine, and a broad reading of the "materiality" test under the OCC Ruling, a national bank still may seek to export non-rate provisions based on a state law choice-of-law analysis. The bank first should establish a basis for applying its home state's laws by arranging the contacts noted in *Marquette*,[305] such as receipt and approval of credit applications, issuance of credit cards, making of advances, billing, and receipt of payments, in its home state. It then should insert a clear and conspicuous home state (and federal law) choice-of-law provision in its credit agreements which recites that these activities shall occur in the bank's home state.[306]

This approach often strengthens a national bank's position that its home state has a "substantial relationship" to the credit agreement and the contractual choice-of-law provision therefore should be upheld.[307] In most states, the courts will honor a choice-of-law provision if the selected state has a substantial relationship to the transaction and enforcement of the agreement will not violate a fundamental policy of the particular state where the bank seeks to enforce the agreement.[308] It is not always clear what constitutes a fundamental policy; consequently, a loan contract generally will not be deemed usurious if the rate is permissible in a state which has a substantial relationship to the contract and does not greatly exceed the rate permitted by the general usury law of the state of the otherwise applicable law.[309]

Some states, however, reject this approach in a usury context. Several states have enacted legislation which addresses the validity of contractual choice-of-law provisions.[310] Others have expressly provided that their laws will apply regardless of the creditor's location.[311] These "extraterritoriality" provisions often are similar to the Minne-

287. *Id.*

288. Arnold and Rohner, *supra* note 2, at 22.

289. *Supra* note 97.

290. 464 F.2d 855.

291. Fitzgerald letter, *supra* note 98.

292. 464 F.2d at 863.

293. *See* Rosenblum, *supra* note 2, at 1044 n.24. *See also* Edmisten, 681 F.2d 942 (no federal question jurisdication as to whether annual fee would violate state usury law if added to interest charged).

294. *See supra* text accompanying notes 218-220.

295. *See* Arnold and Rohner, *supra* note 2, at 29.

296. Liebesman letter, *supra* note 98.

297. *Id.*

298. OCC Interpretive Letter No. 354, *supra* note 165.

299. *Id.*

300. 439 U.S. at 313-19.

301. *See supra* text accompanying notes 159-220.

302. 294 Md. 385, 450 A.2d 1273.

303. *See supra* text accompanying notes 270-275.

304. 439 U.S. at 313-19.

305. *Id.* at 310-12. *See supra* text accompanying notes 232-235.

306. *See* Restatement (Second) of Conflict of Laws § 188 (1971) (lists contacts to be evaluated in order to determine whether chosen state has "substantial relationship" to the contract).

307. *Id.*

308. Restatement (Second) of Conflict of Laws § 187 (1971).

309. *See id.* § 203.

310. *See, e.g.*, Tex. Bus. & Com. Code Ann. tit. 35D, § 35.53 (Vernon 1987).

311. *See, e.g.*, Iowa Code Ann. §§ 537.1201.1.a, 537.1201.2.b. (West 1987); Wis. Stat. Ann. § 421.201(3) (West Supp. 1987).

sota law which the *Marquette* Court invalidated as it concerned out-of-state national banks' rates.[312] Several of these provisions have been upheld, however, in the *Aldens* series of cases[313] involving out-of-state mail-order retailers.

The *Aldens* cases are of questionable validity as to national banks. The *Marquette* Court disregarded the same type of law which the *Aldens* courts upheld. The *Marquette* decision was based on the federal policy favoring exportation found in the National Bank Act, the federal instrumentality doctrine, and the Court's determination that national banks need not engage in a choice-of-law analysis concerning every credit transaction with a non-resident borrower.[314] Neither the Act nor the doctrine apply to mail-order retailers. Moreover, in *Aldens, Inc. v. Packel*,[315] the Third Circuit recognized that to the extent that Congress has made its own choice-of-law or, more specifically, preempted state interest rate limitations, a state usury law unconstitutionally imposes a burden on interstate commerce that is not outweighed by the state's interest in imposing its regulation.[316] In enacting section 85, Congress has acted in precisely this manner; there is consequently a strong argument that extraterritorial application provisions, as applied to national banks, violate the commerce clause.

5. Penalties

The liability that a national bank faces for contracting for or imposing non-rate credit terms depends on whether the terms are characterized as "interest" under section 85 and, based on that determination, whether the terms violate applicable law. If the terms constitute "interest" and are lawful based on applicable law (either federal law or the bank's home state's law), there is no liability. If the terms constitute "interest" but violate the applicable usury restrictions, the federal penalty contained in the National Bank Act will apply.[317] On the other hand, if the terms are not characterized as "interest," the borrower's state's law will determine whether a violation exists and any applicable penalty. Given the uncertainty as to the characterization of non-rate terms, a national bank may want to achieve substantial compliance with the non-rate aspects of its borrowers' states' laws, particularly where those laws include an extraterritoriality provision.[318]

II. Federally-Insured Savings Institutions

A. Does the Most Favored Lender Doctrine Apply to Federally-Insured Savings Institutions?

Any consideration of the interest rate-charging authority of federally-insured, state-chartered or federally-chartered savings institutions must begin with the "federal usury" provisions of the Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDMCA).[319] Section 522 of DIDMCA provides that a federally-insured savings institution may charge interest on any loan at the greater of one percent over the Federal Reserve discount rate on ninety-day commercial paper or the rate allowed by the laws of the state where the institution is located, notwithstanding any state constitution or statute to the contrary (which is preempted) if either of the above two rates exceeds the rate an insured institution would otherwise be permitted to charge.[320]

Part C of Title V of DIDMCA contains parallel provisions preempting the applicable usury rates of federally-insured, state-chartered banks, federally-insured credit unions, and small business investment companies; Part A preempts state usury ceilings on first mortgage loans; and Part B preempts state usury ceilings on business and agricultural loans exceeding $25,000 for three years.[321] All three preemptions of state usury laws also contain opt-out provisions permitting the voters or legislature of any state to determine explicitly that the preemption provisions of DIDMCA will not apply "with respect to loans made in such State."[322] The legislatures of seven states and Puerto Rico have opted out of the usury provisions of sections 521 through 523 of DIDMCA.[323] DIDMCA also provides, in section 528, that if one or more provisions of Title V of DIDMCA, the National Housing Act, or any other provision of law, including the National

312. 439 U.S. at 302-03 n.4, 310-12.

313. Aldens, Inc. v. Miller, 610 F.2d 538 (8th Cir.), *cert. denied*, 446 U.S. 919 (1979); Aldens, Inc. v. Ryan, 571 F.2d 1159 (10th Cir.), *cert. denied*, 439 U.S. 860 (1978); Aldens, Inc. v. LaFollette, 552 F.2d 745 (7th Cir.), *cert. denied*, 434 U.S. 880 (1977); Aldens, Inc. v. Packel, 524 F.2d 38 (3d Cir.), *cert. denied*, 425 U.S. 943 (1975).

314. 439 U.S. at 310-19.

315. 524 F.2d 38.

316. *Id.* at 45-46, 49.

317. *See* 12 U.S.C. § 86 (1982); *supra* text accompanying notes 247-250.

318. *See supra* text accompanying notes 311-316.

319. Pub. L. 96-221, Title V, Part C, §§ 521-529, 94 Stat. 164 (Mar. 31, 1980).

320. Section 522 of DIDMCA states in part as follows:

(a) If the applicable rate prescribed in this section exceeds the rate an insured institution would be permitted to charge in the absence of this section, such institution may, notwithstanding any State constitution or statute which is hereby preempted for the purposes of this section, take, receive, reserve, and charge on any loan or discount made, or upon any note, bill of exchange, or other evidence of debt, interest at a rate of not more than 1 per centum in excess of the discount rate on ninety-day commercial paper in effect at the Federal Reserve Bank in the Federal Reserve District where such institution is located or at the rate allowed by the laws of the State, territory, or district where such institution is located, whichever may be greater.

Pub. L. 96-221, § 522, 94 Stat. 165 (Mar. 31, 1980) (codified at 12 U.S.C. § 1730g (1982)) (prior to 1983 amendment).

The 1983 amendment to section 522 added the following language after the words "insured institution": (which, for the purposes of this section shall include a Federal association the deposits of which are insured by the Federal Deposit Insurance Corporation)"; Pub. L. 97-457, § 33, 96 Stat. 2511 (Jan. 12, 1983) (codified at 12 U.S.C. § 1730g (Supp. V 1987)).

321. Pub. L. 96-221, Title V, 94 Stat. 161 (Mar. 31, 1980). Section 501 of DIDMCA (Part A) permanently preempts state usury ceilings on first mortgage loans made by banks, savings and loans, credit unions, mutual savings banks, mortgage bankers, and HUD-approved lenders, subject to a state override within three years. Section 511 of DIDMCA (Part B) preempts state usury ceilings on business and agricultural loans over $25,000 made by any person for a three-year period, subject to the right of states to override the preemption. Section 521, with respect to state-chartered insured banks, including insured savings banks and insured mutual savings banks or insured branches of foreign banks, is similar to section 522 with two exceptions: (1) the references to the applicable institutions and (2) a statement at the beginning of section 521 stating the intent "to prevent discrimination" against the state-chartered insured banks. With regard to federally-insured state banks, *see infra* text accompanying notes 380-408.

322. Section 525 of DIDMCA provides as follows:

The amendments made by section 521 through 523 of this title shall apply only with respect to loans made in any State during the period beginning on April 1, 1980, and ending on the date, on or after April 1, 1980, on which such State adopts a law or certifies that the voters of such State have voted in favor of any provision, constitutional or otherwise, which states explicitly and by its terms that such State does not want the amendments made by such sections to apply with respect to loans made in such State, except that such amendment shall apply to a loan made on or after the date such law is adopted or such certification is made if such loan is made pursuant to a commitment to make such loan which was entered into on or after April 1, 1980, and prior to the date on which such law is adopted or such certification is made.

Pub. L. 96-221, § 525, 94 Stat. 167 (Mar. 31, 1980) (codified at 12 U.S.C. § 1730g note (1982)).

323. The states of Colorado, Iowa, Massachusetts, Maine, Nebraska, North Carolina, and Wisconsin and the Commonwealth of Puerto Rico have formally opted out of sections 521-523. Colo. Rev. Stat. § 5-13-104 (Supp. 1986); 1980 Iowa Acts ch. 1156, § 32 (not codified); 1981 Mass. Acts ch. 231, § 2 (codified at Mass. Gen. Laws. Ann. ch. 183, § 63 note; repealed in 1986 Mass. Acts ch. 177); Me. Rev. Stat. Ann. tit. 9A, § 1-110 (Supp. 1986); Neb. Rev. Stat. § 45-1.104 (Cum. Supp. 1982), amended by 1988 Neb. Laws 913; N.C. Gen. Stat. § 24-2.3 (1986); 1981 Wis. Laws ch. 45, § 50 (not codified); P.R. Laws Ann. tit. 10, § 9981(c). Due to the rarity of a federal law permitting a state override of its provisions, there is no court decision construing the true effects of section 525 or a similar provision. Section 525 indicates that the state law should explicitly and by its terms indicate that the state does not want the amendments and sections to apply with respect to loans made in such state. The validity of the state opt-out may be in question if the state opt-out provision does not specifically name the section of the statute overriden. For example, Nebraska's provision indicates only that the "federal limits on interest rates as provided in Pub. L. 96-221" shall not apply to loans made in Nebraska. Moreover, the issue arises whether a state may be permitted to rescind its override provision, as Massachusetts and Nebraska have attempted to do. *See infra* text accompanying notes 363-370.

Bank Act (12 U.S.C. section 85),[324] apply with respect to the same loan or advance, the loan or advance may be made at "the highest applicable rate."[325]

Most authorities and commentators agree[326] that section 522 incorporates the most favored lender doctrine originally enunciated by the United States Supreme Court in *Tiffany*.[327] The Federal Home Loan Bank Board, the regulatory agency governing federally-insured savings institutions, stated in an opinion letter dated September 29, 1980,[328] later withdrawn, and in an Interpretive Ruling dated February 13, 1981 (the FHLBB Ruling),[329] that section 522 allows insured institutions to charge the greater of one percent over the Federal Reserve ninety-day discount rate or the rate allowed to the most favored lender under state law, whenever the greater of either rate exceeds the rate that the institution is permitted to charge by state law. The FHLBB Ruling is based on two rationales: the legislative intent of section 522 to "provide insured institutions with competitive equality with national banks" and judicial construction of the phrase "rate allowed by the laws of the State." The phrase "rate allowed by the laws of the State, territory, or district where such institution is located" is virtually identical to the same phrase in section 85, which the courts have interpreted to permit national banks to charge the rate allowed to the most favored lender under state law.[330]

1. Legislative History of Section 522

The legislative history surrounding section 522 of DIDMCA is sparse. In fact, the House Conference Report on Part C of Title V includes an obvious error of interpretation.[331] Although no specific intent to incorporate the most favored lender doctrine into section 522 can be drawn from the legislative proceedings, an examination of the circumstances surrounding the passage of DIDMCA and reasoned analysis lead to the conclusion that the most favored lender doctrine is available to federally-insured savings and loan associations.

Sections 521-525 of DIDMCA have their origins in S. 1988,[332] introduced by Senators Pryor and Bumpers of Arkansas in late 1979. In remarks made on the Senate floor on October 15, 1979, before introduction of the bill and in hearings before the Committee on Banking, Housing, and Urban Affairs on S. 1988 held on December 17, 1979,[333] both senators and Senator Proxmire, Chairman of the Committee, emphasized their mission to provide "competitive equality" for all federally-insured financial institutions. Senator Bumpers indicated in hearings that S. 1988 was introduced "[i]n order to equalize the monetary situation so that one type of financial institution would not have an unfair advantage over another."[334] He continued: "[s]o this is simply a parity bill, and that's all it is. It's an equalization bill to put the two banks on equal footing, allow them to compete with each other."[335]

At the time S. 1988 was introduced, the Federal Reserve discount rate stood at 12%, permitting national banks to charge a rate of 13% under the National Bank Act; at the same time, many state banks and savings institutions were limited by state law to usury rates of 10% to 12%.[336] In reacting to the economic exigency and the "usury inequality" that existed in late 1979 and early 1980, Congress clearly intended to create parity between national banks and other federally-insured financial institutions with respect to the charging of interest.

The use of the phrase "the rate allowed by the laws of the State, territory, or district where such institution is located," which is virtually identical to the language of section 85, coupled with direct references in the congressional debate to section 85 and to the alternative interest rates authorized by the final bill,[337] indicate that Congress intended to permit federally-insured savings institutions to charge the same most favored lender rates allowed to national banks.[338] If Congress did not intend the application of the most favored lender doctrine to federally-insured savings institutions, it could have so limited the usury preemption in section 522 of DIDMCA. As it is, section 522 clearly refers to three rates: the rate "permitted" in the absence of section 522, the rate of one percent over the Federal Reserve discount rate, and the rate "allowed by the laws of the State, territory, or district where such institution is located." The use of three rates in section 522 does not make sense unless the third rate refers to the most favored lender rate of the state.

2. The Bank Board's Interpretive Ruling

In the FHLBB Ruling of February 13, 1981, the Federal Home Loan Bank Board determined that section 522 allows federally-insured savings institutions to charge interest at the greater of one percent over the Federal Reserve discount rate or the rate allowed to the most favored lender under state law, whenever the greater of these rates exceeds the rate the institution is otherwise permitted to charge by state law.[339] The FHLBB Ruling followed an opinion letter of the General Counsel to the Bank Board dated September 29, 1980,[340] later withdrawn, which analyzed the legislative history and concluded that section 522 incorporates the most favored lender doctrine. The FHLBB probably withdrew the September 29, 1980 opinion letter because the letter stated that section 522 permitted adding on or discounting interest.

The FHLBB Ruling includes several significant limitations which must be evaluated by a federally-insured savings institution considering use of the most favored lender doctrine. The FHLBB Ruling indicates that federally-insured savings institutions "borrowing" a rate

324. 12 U.S.C. § 85 (1982).

325. Pub. L. 96-221, § 528, 94 Stat. 168 (Mar. 31, 1980) (codified at 12 U.S.C. § 1735f-7 note (Supp. V 1987)).

326. *See* Burke and Kaplinsky, *supra* note 2; Arnold and Rohner, *supra* note 2; *but see A Contrary View*, *supra* note 21.

327. 85 U.S. (18 Wall.) 409; *see infra* text accompanying notes 392-397.

328. Letter from the General Counsel to the Federal Home Loan Bank Board (Sept. 29, 1980), *reprinted in* [1979-1980 Transfer Binder] Fed. Banking Law Rep. (CCH) para. 98,447.

329. 46 Fed. Reg. 13,987 (April 1, 1980) (codified at 12 C.F.R. § 570.11 (1987)).

330. *See supra* text accompanying notes 20-22, 28, 56-63.

331. H. Conf. Rep. No. 96-842, 96th Cong., 2nd Sess. 78-79, *reprinted in* 2 [1980] U.S. Code Cong. & Ad. News 308-09. The House Conference Report indicates in error that the preemption is subject to a "ceiling" of 1% above the appropriate Federal Reserve discount rate, ignoring the alternative language of the statute indicating the words "whichever may be greater" as they apply to the alternative rate of 1% over the Federal Reserve discount rate and the rate "allowed by the laws of the State."

332. S. 1988, 96th Cong., 1st Sess. (1979).

333. *Usury Lending Limits: Hearing on S. 1988 before the Comm. on Banking, Housing, and Urban Aff.*, 96th Cong., 1st Sess. (1979).

334. *Id.* at 42 (statement of Sen. Bumpers).

335. *Id.* at 43 (statement of Sen. Bumpers).

336. 125 Cong. Rec. 30655 (1979) (remarks of Sen. Pryor).

337. 126 Cong. Rec. 6907 (1980) (remarks of Sen. Bumpers).

338. Two witnesses referred to the most favored lender doctrine in their written statements. *Hearings on S. 1988*, *supra* note 333, at 64-65 (written statement of Joseph W. Cugini); *id.* at 151 (written statement of Kenneth Irwin).

339. *Supra* note 329.

340. *Supra* note 328.

from state law may only charge the most favored lender rate when making the same type of loans as the most favored lender.[341] As an example, the FHLBB Ruling states that a federally-insured savings institution borrowing the maximum loan rate permitted to small loan companies must comply with "substantive state law requirements" governing small loan companies as to the "loan term, amount, use of proceeds, identity of borrower, etc."[342] The FHLBB Ruling further states that "consumer protections specifically required in such loans when made by the most favored lender would also be considered substantive and must be included in loans made by insured institutions which desire to use most favored lender rates."[343] In a significant departure from the OCC Ruling, the FHLBB Ruling does not require compliance only with state law requirements pertaining to the class of loans being made that are "material to the determination of the interest rate."[344] Finally, the FHLBB Ruling indicates that procedural or regulatory requirements applicable to the state's most favored lender do not apply to federally-chartered savings institutions. Examples of procedural restrictions include licensing, bonding, and reporting requirements. State-chartered, federally-insured savings institutions must comply with such procedural or regulatory restrictions to the extent required by their state supervisors.[345]

In one sense, the FHLBB Ruling puts federally-insured savings institutions at a competitive disadvantage with national banks, when each utilizes its respective most favored lender doctrine. National banks must comply only with state law requirements that are "material to the determination of the interest rate," while federally-insured savings institutions must comply with all substantive restrictions of the most favored lender statute, whether or not they are material to the determination of the interest rate. To the extent that a state permits its most favored lender to make preferential charges that might not be construed as material to the determination of the interest rate, however, the FHLBB Ruling would be more beneficial than the OCC Ruling. In that event, a federally-insured savings institution is permitted to impose all "substantive" charges that are permitted by the state law applicable to the most favored lender, including annual fees, delinquency charges, bad check charges, overlimit fees, minimum transaction fees, origination fees, and other fees.

Savings institutions considering use of the most favored lender doctrine under section 522 of DIDMCA also must consider the possible judicial weight given to the FHLBB Ruling. In *Fidelity Federal Savings and Loan Association v. de la Cuesta*,[346] the United States Supreme Court held that a FHLBB regulation permitting savings institutions to enforce due-on-sale provisions of real estate mortgages despite conflicting state legal requirements was a valid exercise of the Bank Board's plenary power to regulate the lending practices of federally-chartered savings institutions,[347] and thus the regulation preempted conflicting state limitations on enforcing a due-on-sale clause.[348] Significantly, the Court stated in *de la Cuesta* that the Bank Board was not bound by conflicting state law in enacting regulations concerning the lending practices of federal savings institutions.

The FHLBB Ruling is entitled to be given the same weight by the Court as the Bank Board's due-on-sale regulation; both are statements of policy promulgated by the Bank Board pursuant to its broad mandate to govern the operation of federally-chartered savings institutions. A court probably would uphold the FHLBB Ruling as a valid regulation of the lending authority of federally-chartered savings institutions. The *de la Cuesta* preemption ruling for Bank Board regulations is inapplicable to state chartered savings institutons, however. State-chartered savings institutions must evaluate the persuasiveness of the FHLBB Ruling as an interpretation of Section 522.[349]

3. Usury Penalties

Section 522 also provides for a federal usury penalty of forfeiture of the interest agreed to be paid and recovery of twice the amount of the interest paid.[350] It is likely that the federal penalty applies only when the institution utilizes the most favored lender rate or the floating rate; state usury penalties are likely to apply if the savings institution utilizes the rate "permitted" by state law in the absence of section 522.

B. Can Federally-Insured Savings Institutions Export Interest Rates?

Although no court has addressed whether a federally-insured savings institution may export the interest rate ceilings of its home state when extending credit to residents of other states, the General Counsel to the Bank Board has stated in an opinion letter that section 522 of DIDMCA "necessarily includes"

341. 12 C.F.R. § 570.11(a) (1987), indicates that federally-insured savings institutions may charge the "rate allowed to the most favored lender on the particular class of loans under state law" and section 570.11(b) indicates that federally insured savings institutions may only charge the most favored lender rate if they "are making the same type of loans as the most favored lender." Section 570.11(b) continues, "accordingly, insured institutions could not charge the maximum loan rates permitted for small loan companies unless that loan met the substantive state law requirements as to loan term amount, use of proceeds, identity of borrower, etc." *Id.* For a discussion of the same "class" of loans, *see supra* text accompanying notes 130-155.

342. 12 C.F.R. § 570.11(b) (1987).

343. Section 570.11(b) indicates as follows: "Consumer protections specifically required in such loans when by the most favored lender would also be considered substantive and must be included in loans made by insured institutions which desire to use most favored lender rates." *Id.*

344. 12 C.F.R. § 7.7310(a) (1987). *See supra* text accompanying notes 159-220.

345. Section 570.11(c) states as follows:

> Federally-chartered insured institutions would not be required to submit to state most-favored-lender restrictions that are primarily procedural or regulatory in nature. Such restrictions would include licensing, bonding, and reporting to State authorities. The degree to which state-chartered insured institutions must comply with such restrictions will be determined by their State supervisors.

Id.

346. 458 U.S. 141 (1982).

347. Section 5(a) of the Home Owner's Loan Act now provides as follows:

> In order to provide thrift institutions for the deposit and investment of funds and for the extension of credit for homes and other goods and services, the Board is authorized, under such rules and regulations as it may prescribe, to provide for the organization, incorporation, examination, operation, and regulation of associations to be known as Federal savings and loan associations, or Federal savings banks, and to issue charters therefor, giving primary consideration to the best practices of thrift institutions in the United States. The lending and investment authorities are conferred by this section to provide such institutions the flexibility necessary to maintain their role of providing credit for housing.

12 U.S.C. § 1464(a) (Supp. V.1987).

348. 458 U.S. at 160-70. *See also* Independent Bankers Ass'n v. FHLBB, 557 F. Supp. 23, 25-28 (D.D.C. 1982) (upholding Bank Board's approval of statements of policy which allowed federally-chartered savings institutions to establish interstate branches); and People v. Coast Fed. Sav. & Loan Ass'n, 98 F. Supp. 311, 316 (S.D. Cal. 1951) (affirming Bank Board's plenary power).

349. *See supra* note 57 and cases cited therein.

350. Sec. 522 of DIDMCA states in part:

> (b) If the rate prescribed in subsection (a) exceeds the rate such institution would be permitted to charge in the absence of this section, and such State fixed rate is thereby preempted by the rate described in subsection (a), the taking, receiving, reserving or charging a greater rate of interest than that prescribed by subsection (a), when knowingly done, shall be deemed a forfeiture of the entire interest which the note, bill, or other evidence of debt carries with it, or which has been agreed to be paid thereon. If such greater rate of interest has been paid, the person who paid it may recover, in a civil action commenced in a court of appropriate jurisdiction not later than two years after the date of such payment, an amount equal to twice the amount of the interest paid from the institution taking or receiving such interest.

Pub. L. 96-221, § 522, 94 Stat. 165 (codified at 12 U.S.C. § 1730g (Supp. V 1987)).

the ability to export interest rates.[351] The General Counsel's Interpretive Letter of August 6, 1982 relies on the holding of the *Marquette*[352] decision and the intention of Congress in enacting section 522 of DIDMCA to promote competitive equality between national banks and other federally-insured institutions. The letter therefore concludes that the most favored lender status conferred by section 522 on federally-insured savings institutions includes the ability of the institution to export interest rates pursuant to *Marquette*.

Although there are several questions regarding which terms may be exported by a federally-insured savings institution, whether an interest rate may be exported into a state that has opted-out of the provisions of section 522, and where a federally-insured savings institution is "located" for the purposes of determining which state's laws can be exported, it seems clear that federally-insured savings institutions should be able to charge out-of-state borrowers the rates permitted by section 522 of DIDMCA. On its face, section 522 clearly permits federally-insured savings institutions to charge the applicable rates "notwithstanding *any* State constitution or statute which is hereby preempted for the purposes of this section."[353] By its plain language, section 522 preempts the laws of *any* state, including an out-of-state borrower's state, that would impede a federally-insured savings institution from charging the applicable interest rate.

As such, it is clear that section 522 should apply to an interstate loan even if the rate permitted in the absence of section 522 is equal to the most favored lender rate. Exportation of interest by a federally-insured savings institution does not require a "borrowing" of the most favored lender rate of the state in which the institution is located. Even if the rate permitted in the absence of section 522 is equal to the most favored lender rate but greater than the rate of an out-of-state borrower's state, section 522 and the opinion letter of August 6, 1982 both imply that the out-of-state rate is still preempted by section 522.

Moreover, the language of section 522 permits federally-insured savings institutions to charge the rate of the state "where such institution is located."[354] If Congress had intended to preempt only the laws of the state where institutions were located, or if it had intended to restrict savings institutions to the usury ceilings of the borrower's state, Congress could have clearly so provided in section 522. Maxims of statutory construction render the failure of Congress to clearly restrict the application of *Marquette* as to federally-insured savings institutions to mean that Congress implicitly accepted and legitimized its application.[355]

DIDMCA also provides in section 528, subtitled "Effect on Other Law," that if one or more provisions of Title V of DIDMCA, the National Housing Act, or "any other provision of law" applies with respect to a loan, the loan "may be made at the highest applicable rate."[356] Although this section does not address interstate loans specifically, it supports the exportation of the rates specified in section 522 despite any provision of the borrower's state's law. If the borrower or a state regulator argues that rate restrictions of the borrower's state apply to a loan, section 528 of DIDMCA indicates, in a contest between conflicting rate restrictions, that the loan may always be made at the highest applicable rate.

Further, as the Bank Board General Counsel indicated in the opinion letter of August 6, 1982, the congressional purpose to promote parity between national banks and other financial institutions is only served, with respect to interstate transactions, if savings institutions are permitted to export the same interest rates that national banks are permitted to export. Given this intent, a federally-insured savings institution clearly should be able to charge out-of-state borrowers the most favored lender rate of its home state.

C. Can Federally-Insured Savings Institutions Export Annual Fees and Other Contract Terms?

In contrast to the ambiguity of the OCC Ruling with respect to the ability of national banks to export annual fees and other contract terms, the FHLBB Ruling[357] supports the ability of federally-insured savings institutions to export annual fees and all contract terms permitted by the substantive state law governing the most favored lender on the class of loans being made, because it apparently permits savings institutions to export all "substantive state law requirements."[358] The FHLBB Ruling does not specifically define the word "substantive," although it provides several examples of substantive requirements, including requirements regarding the loan term, amount, use of proceeds, identity of borrower, and consumer protections. Applying a commonsense interpretation of the dichotomy between substantive and procedural provisions of state law, it can hardly be argued that provisions permitting charging of annual fees and other charges, as well as provisions governing terms of the contract—such as change of terms and other notice provisions; default, acceleration and account cancellation requirements; and balance calculation methods, free-ride periods, and other open-end lending restrictions—would be "procedural" in nature. Such provisions are no more "procedural" than the traditional "consumer protections" identified by the FHLBB Ruling.

Moreover, the ability to include substantive provisions, including consumer protections, of the savings institution's home state means that savings institutions should not be subject to conflicting provisions of the law of the borrower's state. This is particularly relevant if the law of the savings institution's home state does not have significant consumer protections. The FHLBB Ruling may not support the exportation of an *absence* of consumer protections, however, because it indicates that "consumer protections specifically required"[359] are substantive; the issue becomes whether consumer protections of the borrower's state are applicable.

A federally-insured savings institution seeking to export contract terms should have three concerns in mind. The FHLBB Ruling may exceed the Federal Home Loan Bank Board's rulemaking authority, under the arguable proposition that

351. FHLBB General Counsel letter, Aug. 6, 1982, *supra* note 12.

352. 439 U.S. 299.

353. Pub. L. 96-221, § 522, 94 Stat. 165 (Mar. 31, 1980)(codified at 12 U.S.C. § 1730g (1982)) (prior to 1983 amendment) (emphasis added).

354. *Id.*

355. *See* Burke and Kaplinsky, *supra* note 2, at 1104-05.

356. Pub. L. 96-221, § 528, 94 Stat. 168 (Mar. 31, 1980), codified at 12 U.S.C. § 1735 f-7 note (Supp. 1987).

357. *Supra* note 329.

358. *Supra* note 341.

359. 12 C.F.R. § 570.11(b) (1987).

it interprets section 522 more expansively than the specific terms of the statute. Reliance on the FHLBB Ruling is therefore potentially problematic; the Ruling may be construed as overstepping the limited reach of section 522 because that section relates solely to interest rates. This concern is lessened with respect to federally-chartered savings institutions, because of the extent to which the Federal Home Loan Bank Board has plenary power under *de la Cuesta*[360] to preempt conflicting provisions of the law of the state where the out-of-state borrower resides.[361] The only challenge to the exportation of fees and contract terms would likely be from a borrower residing in a state with more restrictive provisions.

A second concern is the stated intent of Congress in enacting section 522. If national banks exporting interest rates are subject only to provisions that are "material to the determination of the interest rate" pursuant to the OCC Ruling, the intent of Congress to provide parity for federally-insured savings institutions with respect to national banks might lead a court to assume that exportation by a federally-insured savings institution would also be limited to provisions that are "material to the determination of the interest rate." This concern is lessened to the extent that provisions "material to the determination of the interest rate" are also considered "substantive" provisions of state law.[362]

Finally, the rationale of the FHLBB Ruling as to exportation of fees and other contract terms may not apply if the savings institution is not "borrowing" the most favored lender rate. If the rate permitted in the absence of section 522 is equal to the most favored lender rate, and the rate permitted by the out-of-state borrower's state is equal to or greater than the permitted rate, there is no preemption under section 522 as to the "applicable rate." Unless the term "rate" is broadly defined to include "substantive state law requirements"—the leap made by the FHLBB Ruling—there is no preemption and arguably no right to export more permissive fees and other terms.

D. What is the Effect of a State Override on Exporting into that State?

Seven states and the Commonwealth of Puerto Rico have adopted provisions opting out of the usury preemption of sections 521 through 523 of DIDMCA.[363] The application of a state override provision to an interstate loan made by an institution not located in an opt-out state to a borrower residing in an opt-out state is as unclear as the congressional intent behind the adoption of section 525 to permit a state override. Because Congress adopted Title V of DIDMCA in order to combat the economic exigencies of the time,[364] and to permit lenders to lend at reasonable rates above their cost of funds despite state usury ceilings to the contrary, it would seem that the opt-out provision should apply only to lenders located in the opt-out state, rather than to loans made to borrowers residing in the opt-out state. Section 525 obviously represented a compromise between senators interested in preserving states' rights to enact usury limits and senators interested in achieving parity.[365] This compromise shows Congress' intention to permit states to reassert their interest rate ceilings "with respect to loans made" in their states. Section 525, as a result, does not apply to borrowers residing in opt-out states or to the exportation of another state's interest rate into those states but applies only "with respect to loans made"[366] by lenders located in an opt-out state.

The issue as to which state a loan is "made" in is subject to conflicting interpretations. This determination may involve a conflict of laws analysis,[367] and a choice-of-law provision in a consumer credit contract may be enforceable if the lender's home state has a substantial relationship to the transaction and the rate charged does not greatly exceed the rate permitted by the opt-out state.[368]

Although the interest rate-charging language of section 522 is similar to the language of section 85, the National Bank Act does not include a provision permitting states to override the interest rate-charging provisions of section 85 with respect to national banks. Although the stated legislative intent of section 522 was to provide federally-insured savings institutions with "parity" with respect to the rates charged (and exported) by national banks, a court might not extend the "parity" rationale to a federally-insured savings institution which attempts to export a most favored lender rate and other fees and terms into an opt-out state. Moreover, a court might determine that Congress intended section 525 to permit opt-out states to reassert control over rates charged to borrowers residing in such states.

Two of the opt-out states, Massachusetts and Nebraska, have repealed their opt-out provisions.[369] The effect of a repeal is unclear. Although section 525 does not prohibit a repeal of the override provision, it indicates that sections 521 through 523 are applicable only with respect to loans made in a state during the period beginning on April 1, 1980 and ending on the date on which a state adopts an override provision. A court would probably uphold Massachusetts' repeal because its literal effect is to void the override provision as if it had never taken effect. The Nebraska repeal merely changes the language of the opt-out provision. The literal language of section 525, however, indicates that sections 521 through 523 might no longer be applicable with respect to loans made in Massachusetts and Nebraska because those states had adopted override provisions.

E. Where is a Savings Institution Located?

Section 522 permits as an alternative rate "the rate allowed by the laws of the State, territory, or district where such

360. 458 U.S. 141.

361. *Id; see supra* text accompanying notes 316-317.

362. *See A Contrary View, supra* note 21, at 1089-90 nn.84-85 and authorities cited therein (earlier versions of what was to become the OCC Ruling referred to "limitations of substance" rather than provisions "material to the determination of the interest rate").

363. *Supra* note 323.

364. *Supra* note 336.

365. 125 Cong. Rec. 30655 (1979) (Remarks of Sen. Bumpers). Senator Bumpers indicated as follows: "I understand the problem other senators have in their respective States with overriding State law. I do not think it is particularly healthy to be overriding State law... However, these are very unique, difficult, and unprecedented times in the money markets of this country." *Id.* at 30655-56. The remainder of the legislative history indicates a preference among the senators to preempt state law but permit a state to reassert its state usury law, if necessary.

366. Pub. L. 96-221, § 525, 94 Stat. 167 (codified at 12 U.S.C. § 1730g note (1982)).

367. *See supra* text accompanying notes 305-314.

368. *See supra* text accompanying notes 305-314.

369. 1986 Mass. Acts ch. 177; 1988 Neb. Laws 913 (to be codified at Neb. Rev. Stat. § 45-1,104) (effective Apr. 7, 1988). The Nebraska bill indicates that "[s]ections 521-523 of Pub. L. 96-221 are not rejected.".

institution is located."[370] In construing similar language in the National Bank Act, the Supreme Court determined in *Marquette* that a national bank is located in the state where it is chartered.[371] The Court recited several factors related to the locale of various aspects of the credit transaction, however, including the extension of credit, issuance of credit cards, receipt of payments, assessment of finance charges, and the credit decision—activities that took place in the bank's home state—and concluded that the bank did not have substantial contacts with the state of the borrower. The Court specifically noted that the exporting national bank did not operate branch banks in the borrower's state and had no legal authority to do so.[372] A federally-chartered savings institution, on the other hand, is not barred by the McFadden Act from operating branches in states other than the state where it is chartered, although interstate branching is subject to restriction by the Federal Home Loan Bank Board.[373]

The General Counsel to the Bank Board has indicated that a multistate savings and loan institution is located in the state in which its home office is located.[374] The General Counsel indicated in a subsequent letter that a multistate savings institution is located in *each state* in which it has branches, and that the institution may export the interest rate of the state in which the branch where the loan is "booked" is located.[375] The subsequent letter notes that an out-of-state branch office confronts local competition from other savings institutions and commercial banks and thus should not be restricted to the rates permitted by the state in which the home office is located. The two letters conflict to the extent that the institution attempts to utilize a higher rate for loans "booked" at its branch offices than would be permitted by the state in which the home office is located. The two letters do not necessarily conflict with regard to loans "booked" at the home office and made to residents of a state in which a branch office is located. The General Counsel's subsequent letter appears to state the correct interpretation of the word "located" as including states where a savings institution has offices.[376]

F. Can a Federally-Insured Savings Institution Import Rates?

In an opinion letter dated February 25, 1981, the Senior Associate General Counsel to the Bank Board indicated that a lender is not permitted by virtue of section 522 of DIDMCA to charge an out-of-state borrower the rate permitted by the borrower's state.[377] Section 522 permits federally-insured savings institutions to charge the most favored lender rates only of the state "where such institution is located." Court decisions which permit national banks to charge rates established in their out-of-state borrowers' states do not apply to federally-insured savings institutions, because the authority for national banks to "import" rates depends on statutory language in the exception clause of section 85 that is not replicated in section 522 of DIDMCA.[378]

Although the language of section 522 does not permit "importation" of rates, section 528 of DIDMCA[379] and traditional choice-of-law analysis may support the authority of a lender to charge borrowers the rates that a lender would be permitted to charge in the borrower's state without the effects of section 522. If the law of the borrower's state includes an extraterritoriality provision, or if the contract contains a choice-of-law clause naming the borrower's state, there is more than one provision of law applicable with respect to the loan, and section 528 indicates in such circumstances that the loan may be made at the highest applicable rate.

III. Federally-Insured State Banks

A. Does the Most Favored Lender Doctrine Apply to Federally-Insured State Banks?

Section 521 of DIDMCA[380] provides that federally-insured state-chartered banks may charge interest on any loan at the greater of one percent over the Federal Reserve discount rate on ninety-day commercial paper or the rate allowed by the laws of the state where the institution is located notwithstanding any state constitution or statute to the contrary, if either of the above two rates exceeds the rate an insured institution would otherwise be permitted to charge.[381] DIDMCA contains parallel provisions covering the interest rate-charging ability of federally-insured savings institutions, federally-insured credit unions, and small business investment companies, and an opt-out provision permitting the voters or legislature of any state to determine explicitly that the provisions of DIDMCA shall not apply "with respect to loans made in such State."[382]

In contrast to the absence of court decisions permitting a federally-insured savings institution to lend at the most-favored lender rate, state courts in three states have ruled in several cases that section 521 incorporates the most favored

370. Pub. L. 96-211, § 222, 94 Stat. 165 (Mar. 31, 1980) (codified at 12 U.S.C. § 1730g (1982)) (prior to 1983 amendment).

371. 439 U.S. at 310-13.

372. *Id.* at 309.

373. *See* 12 C.F.R. § 556.5(a)(3) (1987).

374. Letter from Norman H. Raiden, General Counsel to the Federal Home Loan Bank Board (July 23, 1984), *reprinted in* [Current] Fed. Banking L. Rep. (CCH) para. 82,089.

375. Letter from Norman H. Raiden, General Counsel to the Federal Home Loan Bank Board (Dec. 11, 1984) (unpublished). The December 11, 1984 opinion letter states as follows:

It is fundamental that a branch office located in a state other than the Multi-Location Association Home State must ordinarily conform its lending policies and practices to those existing in each of its locations in order to meet local competition from other thrift institutions and commercial banks and to fulfill the expectations of its customers . . . Thus, we conclude that a branch office of a Multi-Location Association should be permitted to carry out its lending policy and conform with the rules applicable to its competitors in the state in which it is located.

Id.

376. The conclusion reached in the General Counsel's subsequent letter is supported by Seattle Trust & Savings Bank v. Bank of California, 492 F.2d 48 (9th Cir.), *cert. denied*, 419 U.S. 844 (1974) (for purposes of 12 U.S.C. § 36(c) (1982), a national bank is "situated" in a state, outside its home state, where a branch is located).

377. Letter from Rebecca H. Laird, Senior Associate General Counsel to the Federal Home Loan Bank Board (Feb. 25, 1981) (unpublished).

378. *See supra* text accompanying notes 236-246.

379. Pub. L. 96-221, § 528, 94 Stat. 168 (Mar. 31, 1980) (codified at 12 U.S.C. § 1735f-7, note (Supp. V 1987)).

380. Pub. L. 96-221, Title V, Part C, §§ 521-529, 94 Stat. 164 (Mar. 31, 1980).

381. Section 521 of DIDMCA states in part as follows:

(a) In order to prvent discrimination against State-chartered insured banks, including insured savings banks and insured mutual savings banks, or insured branches of foreign banks with respect to interest rates, if the applicable rate prescribed in this subsection exceeds the rate such State bank or insured branch of a foreign bank would be permitted to charge in the absence of this subsection, such State bank or such insured branch of a foreign bank may, notwithstanding any State constitution or statute which is hereby preempted for the purposes of this section, take, receive, reserve, and charge on any loan or discount made, or upon any note, bill of exchange, or other evidence of debt, interest at a rate of not more than 1 per centum in excess of the discount rate on ninety-day commercial paper in effect at the Federal Reserve Bank in the Federal Reserve District where such State bank or such insured branch of a foreign bank is located or at the rate allowed by the laws of the State, territory, or district wehre the bank is located, whichever may be greater.

Pub. L. 96-221, § 521, 94 Stat. 164 (Mar. 31, 1980) (codified at 12 U.S.C. § 1831d (1982)).

382. Section 522 of DIDMCA, with respect to federally-insured savings and loan associations, is virtually identical to section 521, with the exception of the first statement stating the intent of the section "in order to prevent discrimination" against state-chartered insured banks. Section 525 of DIDMCA, *supra* note 322, provides that a state may explicitly determine that the provisions of DIDMCA will not apply "with respect to loans made in such State." *See supra* text accompanying notes 319-324.

lender doctrine and permits a federally-insured state bank to lend at the rate allowed to the most favored lender under the law of the bank's home state.[383] Moreover, the Federal Deposit Insurance Corporation (FDIC), the federal regulatory agency supervising federally-insured state banks, has affirmed in several opinion letters the applicability of the most favored lender doctrine with respect to federally-insured state banks.[384] These sources acknowledge the stated legislative history of section 521[385] and the long-standing judicial construction of the National Bank Act in 12 U.S.C. section 85, which permits a national bank to charge the "rate allowed by the laws of the State, territory, or district" where it is located.[386] Given this authority, it seems well settled that the most favored lender doctrine is applicable to federally-insured state banks.[387]

1. Legislative History of Section 521

There is little distinction between the congressional intent of section 521 of DIDMCA and the congressional intent of section 522 of DIDMCA, already discussed.[388] It is clear that Senators Pryor and Bumpers of Arkansas, sponsors of S. 1988, were interested mainly in obtaining parity for state banks in Arkansas, which were then unable to make loans due to the high cost of funds and a constitutional ten percent usury limitation.[389] Indeed, section 521 of DIDMCA contains a prefatory statement indicating the congressional intent "to prevent discrimination against State-chartered insured banks, including insured savings banks and insured mutual savings banks, or insured branches of foreign banks with respect to interest rates,"[390] while section 522 contains no such statement. This statement and the prior discussion of the legislative history of DIDMCA[391] indicate that Congress intended to incorporate the most favored lender doctrine in section 521.

2. Judicial Interpretations

State courts in Maryland, Michigan, and Minnesota have acknowledged the applicability of the most favored lender doctrine to federally-insured state banks pursuant to section 521 of DIDMCA. In *Attorney General v. Equitable Trust Co.*,[392] the Maryland Court of Appeals noted the trial court's unchallenged holding that state banks have most favored lender status pursuant to section 521 of DIDMCA.[393] In *First Bank v. Miller*,[394] a Michigan appellate court held that section 521 of DIDMCA extended the "most-favored lender" doctrine to state-chartered banks.[395] The Minnesota Appellate Court has held in a series of seven cases[396] that the most favored lender doctrine applies to federally-insured state banks. In six of the Minnesota cases, all decided in 1987, the courts held that a state bank is permitted to "borrow" the 21.75% interest rate allowed by state law to industrial loan and thrift companies making agricultural loans.

The Minnesota state banks confronted several creative arguments raised by the borrowers. The borrowers argued that the state bank could only use the most-favored lender doctrine on the same "class of loan," contending that agricultural loans were governed solely by the Minnesota agricultural loan statute, despite a provision in the industrial loan statute clearly permitting agricultural loans at the rates set forth therein.[397] Additionally, the borrowers argued that Parts A, B, and C of Title V of DIDMCA exclusively govern various types of loans mentioned therein, contending that section 511 of DIDMCA exclusively governed business and agricultural loans and section 521 of DIDMCA, therefore, could not apply to agricultural loans, despite the clear application of section 521 to the specific kinds of lenders named therein, rather than to a particular type of loan.[398] The borrowers also attempted to argue that agricultural loans were exempt from the most favored lender rule pursuant to 1979 amendments to the National Bank Act relating to business and agricultural loans, despite the clear intent of the 1979 amendments to provide a higher alternative interest rate for agricultural loans.[399]

The Minnesota cases also are significant in limiting the applicability of state law requirements as to disclosure, licensing, and lending restrictions.[400] The courts ruled that such restrictions were not applicable to state banks borrowing a rate pursuant to section 521, because they were not "material to the determination of the interest rate."

3. Administrative Interpretations

Several opinion letters issued by the FDIC and state authorities have interpreted section 521 of DIDMCA to incor-

383. *See infra* text accompanying notes 392-400.

384. *See infra* text accompanying notes 401-402.

385. *See supra* text accompanying notes 331-338.

386. 12 U.S.C. § 85 (1982). *See supra* text accompanying notes 20-22, 28, & 56-63.

387. *See* Burke and Kaplinsky, *supra* note 2; Arnold and Rohner, *supra* note 2; *but see A Contrary View*, *supra* note 21.

388. *See supra* text accompanying notes 331-338.

389. Senator Bumpers indicated on November 1, 1979 on the Senate floor:

> It is absolutely imperative that my State get some relief. In Arkansas, if we do not get H.R. 2515 passed, or if we do not get this bill, H.R. 4986 passed with the Cochran amendment, and the people in my State refused to adopt a constitutional amendment raising the usury limit next fall, we are back to square one. The Federal banks are still going to be charging 13 percent, if the Federal rate stays the same, and the State banks 10 percent. We have 210 State banks in my State, and every one of them is going to be applying for a Federal charter if something is not done. I personally think the dual system is a good thing, but we in Arkansas cannot keep it unless we get some relief on this thing.

125 Cong. Rec. 30656 (Nov. 1, 1979) (remarks of Sen. Bumpers).

390. Pub. L. 96-221, § 521, 94 Stat. 164 (Mar. 31, 1980) (codified at 12 U.S.C. § 1831d (1982)).

391. *See* text accompanying notes 331-338.

392. 294 Md. 385, 450 A.2d 1273 (1982).

393. *Id.* at 391, 450 A.2d at 1278.

394. 131 Mich. App. 764, 347 N.W.2d 715 (1984).

395. *Id.* at 744, 347 N.W.2d at 719.

396. The first Minnesota appellate case, First Bank East v. Bobeldyk, 391 N.W.2d 17 (Minn. App. 1986), *pet. for review denied* (Sept. 24, 1986), held that Section 521 incorporated the most favored lender doctrine with respect to state-chartered, federally-insured banks, allowing a state bank to charge the rates permitted by Minnesota's Regulated Loan Act and determining that disclosure requirements in the Regulated Loan Act are not "material to the determination of the interest rate," and thus the state bank is not subject to the disclosure requirements. *See also* Yilek, *Usury and the Most Favored Lender Doctrine: An Important New Minnesota Decision*, Hennepin Law., Nov.-Dec. 1986, at 6.

Since *Bobeldyk*, the Minnesota Appellate Court has decided six cases, all involving agricultural loans: Bandas v. Citizens State Bank, 412 N.W.2d 818 (Minn. App. 1987), *pet. for review granted* (Nov. 24, 1987); Schemmel v. State Bank, 408 N.W.2d 698 (Minn. App. 1987); Walsh v. First State Bank, 409 N.W.2d 5 (Minn. App. 1987), *pet. for review granted* (Sept. 23, 1987); VanderWeyst v. First State Bank, 408N.W.2d 208 (Minn. App. 1987), *pet. for review granted* (Sept. 29, 1987); First State Bank v. Van Ruler, 402 N.W.2d 637 (Minn. App. 1987); Dahl v. Lanesboro State Bank, 399 N.W.2d 621 (Minn. App. 1987), *pet. for review denied* (Mar. 25, 1987).

397. The six courts held that the industrial loan rate applied, despite a separate section of the Minnesota statute governing agricultural loans. The court indicated in each case that the agricultural loan statute, Minn. Stat. § 334.011 (West 1981), is not the exclusive authority under which lenders may make agricultural loans, and that the industrial loan and thrift company statute, *id.* § 53.01 (West 1988), clearly permits industrial loan and thrift companies to make agricultural loans.

398. Section 501 of DIDMCA preempted state usury rates as to first mortgages; section 511 of DIDMCA preempted state usury rates as to agricultural loans; and sections 521-524 of DIDMCA preempted usury rates as to "other loans." Although the title of section C of Title V of DIDMCA was "Other Loans," the text of sections 521-523 (Part C) indicates that the provisions therein apply to all loans made by the particular lenders listed therein, not only to non-business, non-agricultural, or non-first mortgage loans. Further, the text of sections 521-523 applies to "*any* loan or discount made" (emphasis added).

399. Also, the borrowers attempted to argue that 1979 amendments to Section 85 of the National Bank Act, 12 U.S.C. § 85, to partially remove usury restrictions as to agricultural loans exempted agricultural loans from the most-favored lender doctrine of Section 85. *See* Pub. L. 96-184, Tit. I, § 101, 93 Stat. 789 (Nov. 5, 1979), and Pub. L. 96-161, Tit. II, § 201, 93 Stat. 1235 (Dec. 28, 1979), 12 U.S.C. § 85. In the 1979 amendments, Congress intended to remove usury restrictions as to agricultural loans, not to impose further restrictions.

400. *See infra* text accompanying notes 429-432.

porate the most favored lender doctrine with respect to federally-insured state banks. In the first of these letters, dated January 30, 1981, the General Counsel to the FDIC concluded that section 521 incorporates the most favored lender doctrine after reviewing the legislative history of section 521, court decisions interpreting the most favored lender doctrine, and the OCC Ruling. Referring to parallel language in the National Bank Act permitting lenders to charge "the rate allowed by state law," the General Counsel indicated: "it is only logical to conclude that Congress intended those words to have the same meaning."[401] Subsequent letters from the FDIC Office of the General Counsel, addressing related topics, affirmed the incorporation of the most favored lender doctrine in section 521 without much analysis.[402]

The Michigan Attorney General, in an opinion dated May 1, 1981, also ruled that section 521 incorporates the most favored lender doctrine with respect to federally-insured state banks. Discussing the judicial development of the doctrine, as well as the congressional intent to promote parity among competing financial institutions, the Attorney General determined that state-chartered, federally-insured savings and loan associations, credit unions, and banks may charge an interest rate of the greater of one percent over the discount rate in effect for ninety-day commercial paper at the Federal Reserve or the highest rate permitted by law to any lender on the type of loan in question.[403] Addressing related topics, the Texas Consumer Credit Commissioner and the Tennessee Attorney General also have affirmed the incorporation of the most favored lender doctrine in section 521 of DIDMCA.[404]

In addition, Michigan's Attorney General ruled that a lender employing the most favored lender doctrine "must comply with all restrictions as to the loan terms imposed by the state statutes under which such loans are made."[405] Citing *Partain v. First National Bank*[406] in support, the Attorney General indicated that a lender using the most favored lender doctrine to "borrow" an interest rate from state law also becomes subject to the limitations and conditions the state imposes upon the most favored lender "which might affect that rate."[407] Without mentioning the standard of the OCC Ruling subjecting lenders to those terms of the loan statute that are "material to the determination of the interest rate," the Attorney General indicated that "[a] similar interpretation has been given by the Comptroller of the Currency."[408] The standard adopted by the Michigan Attorney General—that the lender must comply with " all restrictions as to the loan terms"—is *broader* than the standard of the OCC Ruling that a lender must comply with restrictions that are "material to the determination of the interest rate."

4. Usury Penalties

Section 521 also provides for a *federal* usury penalty of forfeiture of the interest agreed to be paid and recovery of twice the amount of the interest paid.[409] It is likely that the federal penalty applies only when the institution utilizes the most favored lender rate or the floating rate; state usury penalties would likely apply if the savings institution utilizes the rate "permitted" by state law in the absence of section 521.

B. Can Federally-Insured State Banks Export Interest Rates?

No court has determined whether a federally-insured state bank may "export" the interest rate ceilings of its home state into other states when extending credit to residents of other states. The FDIC Office of General Counsel has indicated in two opinion letters[410] that the rationale of *Marquette*[411] would apply to federally-insured state banks by virtue of section 521, which contains language similar to the National Bank Act, interpreted by the Supreme Court in *Marquette*. In addition, the Texas Consumer Credit Commissioner has suggested a very broad interpretation of section 521. The Commissioner's informal letter states that a state-chartered insured bank "should be permitted to look solely to the laws of its state of domicile to establish the charges and rates of interest on its loans."[412] In an interesting but possibly irrelevant deviation from the language of section 521, the Texas Commissioner used the word "domicile" instead of the phrase "where located," and used the phrase "charges and rates of interest" instead of the word "interest." The Texas Commissioner also indicated that state-chartered insured banks are exempt from any procedural requirements of the out-of-state borrower's state law related to interest rate restrictions, including licensing, otherwise applicable to lenders imposing such interest rates.[413]

Although the FDIC opinion letters regarding exportation are ambiguous, and the Texas Commissioner's opinion letter is persuasive authority only with respect to borrowers residing in Texas,[414] the application of *Marquette* to the language of section 85 and the nearly iden-

401. Letter from Frank L. Skillern, Jr., General Counsel to the FDIC (Jan. 30, 1981) (unpublished).

402. Johnson letter, *supra* note 12; Kravitz letter, *supra* note 12.

403. Op. Mich. Att'y Gen. No. 5894 (May 1, 1981), *reprinted in* [Current] Cons. Cred. Guide (CCH) para. 97,134.

404. Kelley opinion, *supra* note 7; Op. Tenn. Att'y. Gen. No. 221, *supra* note 124 (state banks may charge rate allowed to credit unions on loans that are of the same class made by credit unions).

405. The Michigan Attorney General indicated several examples of such restrictions as to the loan terms:

> The maximum loan amount of $3,000 contained in the Regulatory Loan Act . . . ; the limitations that transactions under the Retail Installment Sales Act . . . . do not include cash loans, loans secured by motor vehicles, or intangible goods; and the limitation found in the Michigan Banking Code . . . . that installment loans made by state banks be limited to a term of eighty-four months and thirty-two days.

Op. Mich. Att'y Gen., *supra* note 403.

406. 467 F. 2d 167 (5th Cir. 1972).

407. Op. Mich. Att'y Gen., *supra* note 403.

408. *Id.*

409. Section 521 of DIDMCA states in part:

> (b) If the rate prescribed in subsection (a) exceeds the rate such institution would be permitted to charge in the absence of this section, and such State fixed rate is thereby preempted by the rate described in subsection (a), the taking, receiving, reserving, or charging a greater rate of interest than that prescribed by subsection (a); when knowingly done, shall be deemed a forfeiture of the entire interest which the note, bill, or other evidence of debt carries with it, or which has been agreed to be paid thereon. If such greater rate of interest has been paid, the person who paid it may recover in a civil action commenced in a court of appropriate jurisdiction not later than two years after the date of such payment, an amount equal to twice the amount of the interest paid from the institution taking or receiving such interest.

Pub. L. 96-221, § 521, 94 Stat. 164 (codified at 12 U.S.C. § 1831d (1982)).

410. Johnson letter, *supra* note 12; Kravitz letter, *supra* note 12. The Johnson letter indicated as follows: "Based on the Supreme Court holding it would seem safe to say that a state bank could charge interest on loans at the rate allowed in the state in which it is organized even though that rate would be usurious in the state where the borrower resides."

The Kravitz letter indicated: "[W]e believe the bank may rely on the federal law that incorporates the interest provisions of the state where the bank is located in extending credit to residents of its state and of other states."

411. 439 U.S. 299.

412. Kelley opinion, *supra* note 7.

413. *Id.* The Texas Consumer Credit Commissioner stated further: "It is the view of this office that § 521, by using language identical to § 85, exempts state-chartered insured banks from any procedural requirement of other states related to interest rate restrictions, including licensing, otherwise applicable to lenders imposing such interest rates." *Id.*

414. Tex. Rev. Civ. Stat. Ann. art. 5069-1.04(p) (Vernon 1987) (lenders do not violate Texas usury laws if practices conform to an interpretation of the consumer credit commissioner).

tical language of section 522 of DIDMCA apparently indicate that federally-insured state banks should be able to charge out-of-state borrowers the rates permitted by section 521. Section 521 clearly permits federally-insured state banks to charge the applicable rates "notwithstanding *any* State constitution or statute which is hereby preempted for the purposes of this section."[415] By this plain language, section 521 preempts the laws of any state that would impede a federally-insured state bank from charging the applicable interest rate. This language suggests that no "borrowing" of a most favored lender rate is necessary in order for a federally-insured state bank to export interest rates. Also, it appears from an FDIC opinion letter and the Texas Commissioner's opinion letter that state banks may export the interest rate of the state of its charter or domicile, without regard to a location analysis possibly suggested by the Supreme Court in *Marquette*.[416]

Additionally, the clear intent of Congress in enacting section 521 "in order to prevent discrimination against state chartered banks,"[417] suggests that Congress intended to permit federally-insured state banks to export the interest rates allowed under section 521 of DIDMCA. Although some commentators question whether Congress was aware of *Marquette* when enacting section 521, language in section 521 virtually identical to language in the National Bank Act and the legislative intent to promote parity between national banks and state banks indicate that state banks should be permitted to export the same interest rate available to national banks located in the same state. A contrary rule (that state banks would be subject to all interest rate limitations of the various states in which its borrowers reside) would be contrary to the specific legislative intent "to prevent discrimination" against state banks vis-a-vis national banks. In addition, section 528 of DIDMCA provides a compelling argument in favor of charging "the highest applicable rate" in the face of conflicting rate restrictions of the borrower's state.[418]

C. Can Federally-Insured State Banks Export Annual Fees and Other Contract Terms?

Although no court has addressed which provisions of state law other than interest rate limitations apply to a lender utilizing the most favored lender doctrine when making loans to out-of-state borrowers, several courts have addressed the applicability of various state law provisions other than interest rate limitations with respect to intrastate loans, and the Texas Commissioner has discussed the applicability of Texas law to interstate loans. Although the approaches of the courts vary with respect to other fees and the substantive requirements of loan statutes governing most favored lenders, it seems clear that consumer disclosure provisions and licensing requirements of those statutes are not applicable to loans made pursuant to the most favored lender doctrine. Addressing interstate loans to Texas borrowers, two Texas Consumer Credit Commissioners determined that out-of-state federally-insured state banks are exempt from the procedural requirements of Texas law with respect to interest rate restrictions and other provisions, including licensing and notice requirements.[419]

The most comprehensive state court decision regarding which non-interest rate provisions of state law are applicable to state banks "borrowing" the interest rate from the most-favored lender's state law is *Attorney General v. Equitable Trust Co.*[420] Although the court in *Equitable Trust* accepted the standard of the OCC Ruling that state law provisions that are "material to the determination of the interest rate" are applicable to lenders "borrowing" state interest rates, the court broadly construed this standard. The court indicated that provisions are "material to the determination of the interest rate" if "they are material to a judicial determination of whether or not the interest charged in a given transaction is unlawful."[421] In applying this principle to the Maryland Consumer Loan Law, the court found most provisions of the law "material" and applicable to the lender "borrowing" the state law.[422]

The trial court in *Equitable Trust*,[423] in language not explicitly adopted by the Maryland appellate court, had indicated that extra fees or charges are material to the determination of the interest rate. The trial court based this decision on its interpretation of the OCC Ruling and its opinion that "a most favored lender may in fact flexibly derive income (from loans/purchases) in the same manner as is possible for other state lenders under a state's [law]."[424] In addition, the trial court cited the FHLBB Ruling as permitting a lender borrowing an interest rate from state law also to "borrow" provisions of state law dealing with permissible and impermissible fees "as substantive state law requirements."[425] In so ruling, the Maryland courts in *Equitable Trust* clearly followed the stated legislative intent of section 521, as the Court of Appeals indicated, "to permit a most favored lender to operate equally with the operations of any state lender as those operations are defined by state law."[426]

First Bank East v. Bobeldyk[427] and the six Minnesota agricultural loan cases contain varying but not inconsistent interpretations of the applicability of state law with respect to fees and other contract terms. The Bobeldyk[428] court indicated that disclosure requirements of the most favored lender statute do not apply to a lender "borrowing" the interest rate permitted under that statute.

415. Pub. L. 96-221, § 521, 94 Stat. 164 (Mar. 31, 1980), codified at 12 U.S.C. § 1831d (1982) (emphasis added).

416. Johnson letter, *supra* note 12; Kelley opinion, *supra* note 7; *see supra* text accompanying notes 370-372; *but see* Kravitz letter, *supra* note 12 ("the FDIC takes no position on that issue").

417. *Id.*

418. *See supra* text accompanying note 356.

419. Kelley opinion, *supra* note 7; letter from Al Endsley, Texas Consumer Credit Commissioner, to Timothy E. Powers (Feb. 13, 1987) (unpublished).

420. 294 Md. 385, 450 A.2d 1273 (1982).

421. *Id.* at 418, 450 A.2d at 1292.

422. The court found the following provisions "material": (a) a prohibition on interest, fees, and charges in excess of those permitted by the Maryland Consumer Loan Law; (b) a maximum loan amount; (c) a provision including the giving of money in exchange for an assignment of wages within the statute's scope; (d) a provision subjecting sale and purchase transactions which are actually loans to regulation by the Maryland Consumer Loan Law; (e) prohibitions on loan splitting; (f) the numerical rate; (g) maximum maturity requirements; (h) provisions dealing with refinancing; (i) prohibitions on discounting and compounding of interest; (j) a maximum maturity for revolving loan advances; (k) provisions allowing bad check charges; (l) prohibitions on prepayment penalties; (m) provisions governing applications of payments; and (n) provisions defining charges, such as kickbacks, received by the lender, as interest. *Id.* at 418-24, 450 A.2d at 1292-95.

423. Equitable Trust Co. v. Sachs, Circuit Court of Baltimore City A-713/ 1981/A-60063 (Sept. 16, 1981); *aff'd in part, rev'd in part, sub. nom.* Attorney General v. Equitable Trust Co., 294 Md. 385, 450 A.2d 1273 (Md. App. 1982).

424. *Id.*

425. *Id. See supra* text accompanying notes 357-361.

426. *Id.*

427. 391 N.W.2d 17.

428. *Id.* at 20.

Although the court stated that the OCC Ruling applies only to national banks and not to state banks, the court ruled that the disclosure requirements were not "material to the determination of the interest rate and not applicable to the state bank." The courts in three of the six 1987 Minnesota agricultural loan cases concluded that "licensing and lending requirements" of the Minnesota industrial loan act do not apply to state banks "borrowing" the industrial loan rate.[429] The Minnesota courts in *Bobeldyk* and these three cases clearly created a restrictive interpretation of the phrase "material to the determination of the interest rate." In another of the seven cases, the Minnesota appellate court held that provisions prohibiting loan splitting and recovery of attorney's fees were not relevant to a determination of the interest rate.[430]

In *Bandas v. Citizens State Bank,*[431] the only decision of the seven that holds in the borrower's favor, the Minnesota appellate court determined that an origination fee permitted by the state industrial loan act was "interest" under the definition of "interest" in that act, and thus rendered the loan usurious under the act.[432] *Bandas*, the most recently decided of the Minnesota agricultural loan decisions, is significant because it utilized a state law definition of "interest" in determining the maximum amount of "interest" chargeable under the most favored lender doctrine established by federal law.[433] The corollary to this decision would be a rule that a lender could export all terms defined as "interest" under the state's most favored lender law. The *Bandas* court did not apply the OCC Ruling's standard of "material to the determination of the interest rate;" it determined that the loan origination fee was "interest" under state law.

After *Equitable Trust* and the Minnesota agricultural loan cases, federally-insured state banks probably are authorized to export state law provisions that are either "interest" (as defined by state law) or "material to the determination of the interest rate" (using either a broad standard such as in *Equitable Trust* or a more restrictive standard such as in the Minnesota cases). A case-by-case analysis of various components of state law, however, is still necessary to determine whether a particular provision is "interest" or "material to the determination of the interest rate." If the provision is not "interest" or is not "material to the determination of the interest rate," exportation may still be feasible under a choice-of-law analysis.[434]

At the same time, federally-insured state banks seeking to export annual fees and other terms must consider the applicability of the "material to the determination of the interest rate" standard contained in the OCC Ruling. While several courts have applied the OCC Ruling to federally-insured state banks, only national banks are bound by its provisions. Use of the OCC Ruling is more persuasive, however, in conjunction with the stated congressional intent of section 521 of DIDMCA to provide state banks parity with national banks. Application of the OCC Ruling to state bank exportation, on the other hand, presupposes the validity of the OCC Ruling.

Additionally, state banks may not be able to export fees and terms in the absence of a "borrowing" of the state's most favored lender rate. If the rate permitted in the absence of section 521 is equal to the most favored lender rate, and the rate of an out-of-state borrower's state is equal to or greater than the permitted rate, there is no preemption as to the "applicable rate." Because there is no preemption, there is arguably no right to export more permissive fees and terms. This concern is lessened only to the extent such fees and terms are considered "interest" or "material to the determination of the interest rate," whether by definition or by application of the legislative intent to create parity with national banks.

D. What is the Effect of a State Override on Exporting into that State?

Seven states and the Commonwealth of Puerto Rico have adopted provisions opting out of the usury preemption of sections 521-523 of DIDMCA.[435] Massachusetts and Nebraska, however, have repealed their opt-out provisions, and the effect of a repeal is unclear.[436] As discussed earlier, the application of a state override provision to an interstate loan made by a federally-insured state bank to a borrower residing in the opt-out state is also unclear.[437]

Although the Bank Board has not issued a regulation or opinion letter regarding the effect of a state override, the Office of General Counsel of the FDIC has issued two separate and conflicting opinion letters regarding the possible effects of a state override.[438] An opinion letter of March 17, 1981, indicated that a borrower's lawsuit on the grounds of usury brought in a state that has opted out of the provisions of section 521 "would be subject to the choice of law provisions of that state" and that "[t]he outcome of such suit would therefore be unpredictable."[439] An opinion letter of October 20, 1983, on the other hand, indicated that a federally-insured state bank "may rely on the federal law that incorporates the interest provisions of the state where the bank is located in extending credit to the residents of its state and of other states," even when making loans to citizens of states that have rejected the federal preemption.[440]

The subsequent letter cited *Marquette* as authority for the proposition that a federally-insured state bank could charge the rate allowed by the laws of the state in which the bank is "located."[441] The subsequent letter apparently agreed with the proposition that the legislative intent of section 521 was to provide "parity" to federally-insured state banks with respect to the rates charged (and exported) by national banks, even when the rates are

429. *Schemmel*, 408 N.W.2d at 700; *Walsh*, 409 N.W.2d at 7; *Dahl*, 391 N.W.2d at 623. Interestingly, all three of these cases were decided by the same judge, Judge Popovich, Chief Judge of the Minnesota Appellate Court.

430. In *VanderWeyst*, 408 N.W.2d 208, the court stated that the only restrictions of state law applicable to the state bank were those "material to determination of the interest rate." The court examined the alleged violations, including loan-splitting and charging of attorney's fees. Because neither alleged violation was "relevant" to a determination of the interest rate, ruled the court, their violation would not preclude application of the most favored lender doctrine.

431. 412 N.W.2d 818 (Minn. App. 1987).

432. Minn. Stat. § 56.001 (1984) defines "interest" as:

> all charges payable directly or indirectly by a borrower which are imposed directly or indirectly by the licensee as an incident to the loan, however denominated, including interest, discount, loan fee, or creditor investigation fee, but shall not include permissible default or deferment charges, lawful fees for any security taken, insurance charges or premiums, court costs, or other charges specifically authorized by law.

Id. The *Bandas* court determined that the loan origination fee is a fee "incident to the loan" under § 56.001 and is included within the definition of interest in Minnesota state law.

433. *See supra* text accompanying notes 276-295.

434. *See supra* text accompanying notes 305-314.

435. *Supra* note 323.

436. *See supra* text accompanying notes 369-370.

437. *See supra* text accompanying notes 363-369.

438. Johnson letter, *supra* note 12; Kravitz letter, *supra* note 12.

439. *Id.*; for a discussion regarding choice-of-law procedures, *see supra* text accompanying notes 305-314.

440. Kravitz letter, *supra* note 12.

441. 439 U.S. 299.

exported into a state that has overridden section 521. Because a court might determine that section 525 was intended to permit opt-out states to reassert control over rates charged to borrowers residing in those states, and because the subsequent FDIC opinion letter is not supported by a thorough analysis of the *Marquette* decision or the legislative history of section 521, federally-insured state banks should carefully evaluate their authority to export interest rates, fees, and contract terms into an opt-out state.

E. Can a Federally-Insured State Bank Import Interest Rates?

In an opinion letter of March 17, 1981, the FDIC indicated that a federally-insured state bank may not charge an out-of-state borrower the rate permitted by the borrower's state, but must instead charge interest on loans at the rate allowed in the state where it is located.[442] This decision appears to be consistent with section 521, which permits federally-insured state banks to charge the most favored lender rate only of the state "where such institution is located."[443] Section 528 of DIDMCA or a traditional choice-of-law analysis, however, may be utilized to charge "the highest applicable rate" when more than one provision of law is applicable with respect to a loan.[444]

IV. Conclusion

National banks and other federally-insured financial institutions confront many difficult questions concerning the scope of the most favored lender doctrine and their exportation rights. Aggressive lenders may wish to adopt some of the arguments presented in this analysis in order to avoid stringent state law restrictions on interest rates, annual fees, and other contract terms. It seems clear that the most favored lender doctrine applies to all federally-insured financial institutions. Apart from the well-defined rate exportation rights of national banks, however, most other exportation issues remain unanswered by any court and subject to contradictory interpretations. Lenders subject to DIDMCA might be prohibited from exporting interest rates to borrowers residing in opt-out states. A federally-insured institution with branches in or contacts with more than one state may be "located" in more than one state for exportation purposes.

The exportation of fees and terms by all federally-insured lenders is fraught with complicated issues regarding the applicability, scope, and conflicting standards of various regulatory opinion letters and court decisions. National banks probably can export non-rate terms if they are "material to the determination of the interest rate"; federally-insured savings institutions probably can export non-rate terms that constitute "substantive state law requirements." To the extent that the courts have adopted the standard of the OCC Ruling with respect to state banks, they probably can export "material" non-rate terms as well. A broad definition of "interest" promotes federal preemption and control with respect to interstate lending by federally-insured financial institutions. Further, traditional choice-of-law analysis may provide additional support for the exportation of non-rate terms. In sum, federally-insured lenders must carefully consider the arguments on both sides of the exportation debate before establishing their interstate lending policies.

442. Johnson letter, *supra* note 12.

443. *See supra* text accompanying notes 377-378.

444. *See supra* text accompanying note 379.