



April 30, 2012

NEW YORK COURT FINDS FEDERAL LAW DOES NOT PREEMPT STATE CONTRACT LAW AND DECEPTIVE ACTS AND PRACTICES CLAIMS

The New York Supreme Court, Appellate Division, held that the federal Home Owners' Loan Act (HOLA) and Office of Thrift Supervision regulations do not preempt breach of contract and deceptive acts and practices claims relating to electronic stored value cards or gift cards. *Sharabani v. Simon Property Group, Inc.*, 2012 WL 1320067 (N.Y. App. Div. Apr. 17, 2012).

In May of 2007 the plaintiff received a gift card, which was issued by the defendant MetaBank, a federal thrift, and marketed and promoted by the defendant Simon Property Group, Inc. The gift card had an initial balance of \$40 and an expiration date of April 2009. The plaintiff used the gift card to make purchases in January of 2008 and January of 2009, leaving an available balance of \$17.71. In July of 2009 the plaintiff attempted to make a purchase using the gift card, but she was advised that a \$15 renewal fee would be assessed, leaving an available balance of \$2.71. The plaintiff did not renew the gift card.

The plaintiff brought action against the defendants as a class action alleging that the literature accompanying the gift card stated that, upon expiration, the gift card would be closed and any unused balance "will be handled according to applicable law." According to the plaintiff, the literature further provided a phone number through which one may request a new gift card containing the remaining balance, minus an "Expired Card Fee." The plaintiff alleged that she was entitled to the return of the unused balance upon expiration, without payment of any fee and that the defendants (i) breached the underlying contract of sale of the gift card by failing to handle the unused balance according to applicable law, (ii) converted the unused funds and (iii) were unjustly enriched by their retention of those funds. The plaintiff also alleged that the defendants deceptively and fraudulently represented that the only option to gain access to the unused balance upon expiration was to pay a fee and renew the gift card, when the defendants knew that, under the applicable law, the plaintiff was entitled to the return of the funds.

The defendants moved to dismiss based on federal preemption under HOLA. The trial court agreed and the plaintiff appealed.

On appeal, the Appellate Division first concluded that the gift card was controlled by the bank, a federally chartered thrift. The court distinguished this case from prior cases involving gift cards in which the servicer controlled aspects of the gift card program. Thus, the court concluded that HOLA and the OTS preemption regulations applied.

The court examined the preemption regulations governing thrifts and relevant case law. The court explained that the scope of preemption depends upon the extent to which state law imposes substantive limitations on the authorized activities of the federal financial institution. The appellate court agreed that the New York Abandoned Property Law was preempted insofar as the law purported to impose requirements regarding abandoned accounts but concluded that an action alleging simple breach of contract or deceptive business practices claims pursuant to the New York General Business Law may be maintained. The plaintiff's causes of action alleging or related to those theories are not preempted, the court said, noting: "[A]s a general principle, the plaintiff is correct that HOLA and the OTS regulations do not preempt state contract or consumer protection laws of general application. . . . 'The duty to refrain from deceptive and misleading conduct is imposed on all businesses. State laws of general application, which merely require all businesses, including [federal thrifts], to abide by contracts and refrain from making misrepresentations to customers, do not impair a [federal thrift]'s ability to exercise its gift-card issuing powers. At most, they incidentally affect the exercise of a [federal thrift]'s powers'" (citing cases). The court modified the order below and remitted the case for a determination of the non-preempted claims on the merits.

This case reflects the trend of recent challenges to programs involving banks and bank partnerships and underscores the importance of reviewing practices, procedures and operations in light of express and implied contract terms and representations. □

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