

Preemption Developments Impacting Interstate Lending by Federally Regulated Financial Institutions

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I. Introduction

The federal banking agencies continued to work overtime in 2003 and early 2004 issuing preemption-related determinations, letters and rules. The Office of the Comptroller of the Currency (OCC) began 2003 with the proposed amendments to its visitorial powers regulation and later in the year issued a more detailed proposed preemption rule. In early 2004 the OCC issued both rules in final

form with few changes, despite strong opposition from certain groups. Over this same period the Office of Thrift Supervision (OTS) found all state predatory lending law provisions that it examined to be preempted. In addition, the courts have continued to address federal preemption with sometimes conflicting results. This article provides a summary of the regulatory issuances and court decisions regarding preemption issued during late 2002, 2003, and the first part of 2004, and discusses how they impact interstate lending by federally-regulated financial institutions.

II. OCC Issues Final Rules on National Bank Preemption and Visitorial Powers

A. Introduction

On January 7, 2004, the OCC issued two long awaited rules. The first clarifies issues related to the OCC's exclusive visitorial powers over national banks, while the second clarifies what types of state laws apply to national banks.¹ The rules took effect February 12, 2004.

B. Preemption Rule

The preemption rule specifies the types of state laws that do not apply to national banks' lending and deposit activities and the types of state laws that generally do apply to national banks. The lists of types of state laws that are not preempted in the final rule are substantively the same as in the proposed rule.

1. 69 Fed. Reg. 1895 (visitorial powers); 69 Fed. Reg. 1904 (preemption) (Jan. 13, 2004).

In the list of laws not preempted, the reference to “debt collection laws” in the proposed rule was revised in the final rule to refer to state laws concerning national banks’ “rights to collect debts.”

The final rule states that except where made applicable by federal law, state laws that “obstruct, impair or condition” a national bank’s exercise of its lending, deposit-taking, or other federal powers do not apply to national banks. In its comments, the OCC stated that the final rule does not entail any new powers for national banks or any expansion of national banks’ existing powers. The OCC stated that the preemption standards in the final rule are consistent with the standards articulated by the United States Supreme Court.²

The OCC final rule contains new provisions prohibiting the making of any type of consumer loan based predominantly on the bank’s possible realization of the foreclosure value of the borrower’s collateral without regard to the borrower’s ability to repay the loan. The final rule also adds a new provision that explicitly prohibits a national bank from engaging in practices that are unfair or deceptive under the Federal Trade Commission Act.³

The OCC stated that, based on existing regulations, the final rule applies to operating subsidiaries. In a chart comparing the scope of national bank, thrift, and credit union preemption, the OCC indicated that its rule has substantially the same scope as the OTS rule for thrifts.⁴

C. Visitorial Powers Rule

The OCC visitorial powers rule is substantively the same as the proposed rule, with a few modifications. The final rule clarifies the scope of the OCC’s exclusive visitorial authority over national banks with regard to activities authorized under federal law. The rule also clarifies the limited exception to the OCC’s ex-

clusive visitorial power as vested in the courts of justice. In its comments, the OCC stated that the final rule is consistent with federal law and the dual banking system.

III. National Bank Operating Subsidiaries Preemption

A. California Decisions on State Auditing Authority

In the *Boutris* cases the United States District Court for the Eastern District of California ruled in favor of Wells Fargo Bank, N.A. and Wells Fargo Home Mortgage, Inc. (a wholly-owned operating subsidiary of Wells Fargo, N.A., a national bank) and National City Bank of Indiana and National City Mortgage Co. (a wholly-owned operating subsidiary of National City Bank of Indiana, a national bank) in determining that the Commissioner of the California Department of Corporations (Commissioner) does not have authority to audit national bank operating subsidiaries.⁵ Both bank operating subsidiaries had obtained California Residential Mortgage Lender licenses. The Commissioner sought to audit the residential mortgage lending activities of the bank operating subsidiaries, including compliance with the California per diem statute.

The banks and their operating subsidiaries argued that the National Bank Act (NBA)⁶ grants the OCC exclusive authority to exercise visitorial powers over national banks and their operating subsidiaries, and that the state Commissioner had no authority to examine or regulate them. They also argued that under the NBA the operating subsidiaries are not required to hold a license under California law to engage in mortgage lending in California. The OCC filed an amicus brief supporting the plaintiffs’ position.

The *Boutris* court gave deference to the OCC’s construction of the NBA, including statements in the OCC’s amicus brief. The court held that the Commissioner had no visitorial powers over the bank operating subsidiaries and that the California license did not affect the right of the operating subsidiaries to conduct federally-permissible banking activities. The court also held that the California law prohibiting the charging of interest on mortgage loans for a period in excess of one day prior to recording (the per diem statute) was preempted by section 501 of the Depository Institutions Deregulation and Monetary Control Act of 1980.⁷ The court found that the state law restricted the time period in which interest can be collected and thus “expressly limits the rate or amount of interest...which may be charged....”

B. OCC Interpretative Letter

The OCC in an interpretive letter stated that national bank operating subsidiaries may impose and export interest charges under the same terms and conditions applicable to the parent national bank.⁸ This conclusion was based on the applicability of 12 U.S.C. section 85 of the NBA to the operating subsidiaries of national banks pursuant to OCC regulations in 12 C.F.R. sections 5.34 and 7.4006.

The OCC held that a wholly-owned operating subsidiary of a national bank, with both the bank and the subsidiary headquartered in Michigan, may rely on the NBA⁹ and export Michigan’s interest rate for real estate-secured loans made by the subsidiary to residents of states other than Michigan or secured by real estate located in states other than Michigan.¹⁰ Based on relevant OCC regulations regarding operating subsidiaries and the

2. 69 Fed. Reg. 1904, 1910.

3. 15 U.S.C. § 45(a)(1) (often called “Section 5”).

4. Available at www.occ.treas.gov/2004-3fcomparisonchart.pdf.

5. National City Bank of Indiana v. Boutris, No. CIV 503655 GEB JFM, 2003 WL 21536818 (E.D. Cal. July 2, 2003); Wells Fargo Bank N.A. v. Boutris, 252 F.Supp 2d. 1065 (E.D. Cal. 2003).

6. 12 U.S.C. §§ 21 et seq.

7. 12 U.S.C. § 1735f-7a.

8. OCC Letter No. 968 from Julie L. Williams, First Senior Deputy Comptroller and Chief Counsel (Feb. 12, 2003).

9. 12 U.S.C. § 85.

10. OCC Letter from Julie L. Williams, First Senior Deputy Comptroller and Chief Counsel (Dec. 16, 2002).

exportation authority of a national bank, and citing *Marquette National Bank of Minneapolis v. First Omaha Service Corp.*¹¹ for the proposition that a national bank is located in the state in which the bank's main office is located, the OCC concluded that, as a national bank operating subsidiary, the subsidiary can export Michigan interest rates under the same terms and conditions applicable to the bank.

IV. Federal Savings Bank Preemption

A. California Consumer Credit Reporting Decision

A California Court of Appeals found that triable issues of material fact existed with regard to a consumer's state law claim against World Savings and Loan Association, a federal savings bank, under the California Consumer Credit Reporting Agencies Act.¹² The *Hussey-Head* court rejected the bank's argument that even if triable issues of material fact existed, the state law restrictions on providing information to credit reporting agencies were preempted by 12 C.F.R. section 560.2. The California law in question prohibits the furnishing of information on a specific transaction or experience to any consumer credit reporting agency if the person knows or should know the information is incomplete or inaccurate.¹³ The statute also contains a disclosure requirement.

The applicable OTS regulation provides that the OTS occupies the entire field of lending regulations for federal savings banks. Section 560.2(b) lists examples of preempted state laws, including laws purporting to impose requirements regarding "access to and use of credit reports," "disclosure and advertising," and "processing, origination,

servicing, sale of, or participation in, mortgages."¹⁴ Despite the specific references in OTS section 560.2(b) to state laws like the California law at issue, the *Hussey-Head* court held that the California law is not preempted by section 560.2 because the California law is not a lending regulation and the bank voluntarily reports credit information to credit reporting agencies.

The *Hussey-Head* court also found that the law does not govern how the bank runs its lending program. Rather, the court found that the law attempts to insure that information reported voluntarily is reported in a fair and accurate manner. The court held that as the state law restriction does not come into play until after a loan is made and does not affect the manner in which the lender services or maintains the loan, it is not inconsistent with federal law. The court also noted that the statute does not on its face purport to regulate federal savings banks and is not specifically directed toward them. The court concluded that any effect the state law has on the bank was "incidental" rather than material and was the result of the bank's voluntary action to report information to credit reporting agencies.

B. Ohio Mortgage Release Decision

The Ohio Supreme Court held that an Ohio law requiring that within ninety days from the date of the satisfaction of a residential mortgage loan the mortgagee must record the satisfaction was not preempted by 12 C.F.R. section 560.2.¹⁵ The *Pinchot* court concluded that a satisfaction recording requirement does not fall within the list of preempted state laws in OTS section 560.2(b).¹⁶ In response to the lender's arguments, the court found that such a law does not impose requirements on the "origination" or "servicing" of mortgages.

Additionally, the *Pinchot* court held that the Ohio law did not affect the lending operations of a federal savings bank, as it regulates the period after the loan is satisfied. The court concluded that the state law was not preempted. Although an analysis under section 560.2(c) was not required given the above holdings, the *Pinchot* court stated that the state law was a real property statute intended to promote efficiency and certainty in clearing and transferring title to property and had only an incidental effect on the federal savings bank's lending practices. Although a state regulator could not enforce the state law against a federal savings bank, the court found no authority forbidding a private individual from enforcing a state law that permitted a private action.

C. Payoff Fees in California

The California Court of Appeals held that federal law preempted a California statute limiting payoff statement fees as applied to a federal savings association.¹⁷ Class action plaintiffs challenged the practice of a federal savings and loan association of charging a fee for the transmission of a payoff statement in excess of the amount permitted under California Civil Code section 2943. The plaintiffs alleged that charging the fee in violation of the California statute was an unfair, deceptive and unlawful business practice in violation of California's Unfair Competition Act. The defendant sought summary judgment on the basis of federal preemption.

The *Lopez* court stated that the OTS was authorized by Congress to promulgate 12 C.F.R. section 560.2 and that federal regulations have no less preemptive effect than federal statutes. The court found that section 560.2 preempts all state laws purporting to regulate any aspect of the lending operations of a federally-chartered savings association, whether or not the OTS has adopted a rule or

11. 439 U.S. 299 (1978).

12. *Hussey-Head v. World Savings and Loan Ass'n*, 4 Cal. Rptr. 3d 171 (Cal. Ct. App. 2003).

13. Cal. Civ. Code § 1785.25(a).

14. 12 CFR § 560.2 (b)(8),(9),(10).

15. *Pinchot v. Charter One Bank, FSB*, 99 Ohio St. 3d 390 (2003).

16. 12 CFR § 560.2(b).

17. *Lopez v. World Sav. and Loan Ass'n*, 105 Cal. App. 4th 729 (2003).

regulation governing the precise subject of the state provision. Thus, the court found that OTS section 560.2 broadly preempts state law restrictions on loan servicing fees, including the payoff statement fees specifically dealt with in the California statute. As the California statute limiting payoff statement fees was preempted, the court held that any claim under the Unfair Competition Act based on a violation of the California statute was also preempted.

D. Forced-Placed Insurance

A California Court of Appeals held that borrowers' actions against a federal savings bank to recover under a state unfair competition statute for charges related to forced-placed insurance were not preempted.¹⁸ The *Gibson* court found that the plaintiffs' claims were predicated on the duties of a contracting party to comply with its contractual obligations and to act reasonably to mitigate damages in the event of a breach by the other party, the duty not to misrepresent material facts, and the duty to refrain from unfair or deceptive business practices.

The contract entitled the defendant to advance a sum necessary to protect its loan security. When the plaintiffs failed to maintain the required insurance on the security, the defendant purchased replacement insurance policies that were much more expensive than the plaintiffs' policies. The *Gibson* court held that the plaintiffs' claims were not based on laws of the type listed in OTS section 560.2 or on laws that affect lending businesses. Rather, the court found that the borrowers' claims involved state laws of general application that affect lending only incidentally. Therefore, the court concluded that the borrower's claims were not preempted by OTS regulations.

V. National Bank Usury Preemption

A. U.S. Supreme Court Usury Decision

The Supreme Court of the United States held that the NBA provides the exclusive cause of action for usury claims against national banks.¹⁹ The Court reversed a decision of the U.S. Court of Appeals for the Eleventh Circuit that found no clear congressional intent to permit removal under 12 U.S.C. sections 85 and 86 of the NBA, and that sections 85 and 86 do not completely preempt state usury claims.²⁰ The Eleventh Circuit responded by issuing an opinion affirming the district court decision and remanding the case to the district court for further proceedings consistent with the Supreme Court's decision.²¹

B. OCC Advisory Letter on Enforcement Authority

The OCC issued an Advisory Letter describing the general principles that apply when determining if a state law applies to a national bank, and if the OCC has the exclusive enforcement authority in regard to national banks.²² The Advisory Letter provides that Congress vested in the OCC broad authority to regulate the conduct of national banks, except where the authority to issue such regulations has been "expressly and exclusively" given to another federal regulatory agency. The Advisory Letter recognizes that state law could be applicable to national banks in limited circumstances, when it does not conflict or interfere with the national bank's exercise of its powers. The Advisory Letter quotes language from *Bank of America*

*v. City and County of San Francisco*²³ noting that, for instance, the federal courts recognize that the states retain some power to regulate national banks in areas such as "contracts, debt collection, acquisition and transfer of property, and taxation, zoning, criminal, and tort law."²⁴ The quote would indicate that the OCC believes that state laws governing the areas referenced by the Ninth Circuit in the quoted language would apply to national banks if the state law does not conflict or interfere with the national bank's exercise of its power.

In the Advisory Letter the OCC advises national banks to consult with the OCC regarding the application and enforcement of state law in a particular instance, due to the often complex nature of such determinations. The Advisory Letter also states that it is the OCC that has the authority to enforce applicable state laws as to national banks and that state officials should contact the OCC if state officials have information or concerns regarding a national bank's potential violation of state or federal law.

VI. National Bank Non-Interest Fee Preemption

A. Kentucky Decision on Non-Interest Fees

The United States District Court for the Western District of Kentucky found complete preemption lacking with regard to non-interest fees charged by a national bank.²⁵ The *Hancock* case involved a challenge to the bank's practice of charging a \$15 fax fee for faxing loan payoff statements. Unlike the interest fees authorized under section 85, which the United States Supreme Court found in *Anderson* to completely preempt state law usury claims (see discussion *supra* at Part V.A.), non-interest fees are permitted based on 12 U.S.C. section 24 (Seventh). The *Hancock* court found

18. *Gibson v. World Savings and Loan Ass'n*, 103 Cal. App. 4th 1291 (Cal. App. 4 Dist. 2002).

19. *Beneficial Nat'l Bank v. Anderson*, 123 S. Ct. 2058 (2003).

20. *Anderson v. H&R Block*, 287 F.3d 1038 (11th Cir. 2002).

21. *Anderson v. H&R Block*, 344 F.3d 1131 (11th Cir. 2003).

22. OCC Letter FL 2002-9 from Julie L. Williams, First Senior Deputy Comptroller and Chief Counsel (Nov. 25, 2002).

23. 309 F.3d 551 (9th Cir. 2002).

24. *Id.*, at 559, citing *Barnett Bank v. Nelson*, 517 U.S. 25 (1996).

25. *Hancock v. Bank of Am.*, 272 F.Supp. 2d 608 (W.D. Ky. 2003).

section 24 (Seventh) to be a broad enabling provision and not a provision that eliminates a state law case of action. Thus, the court found that removal of the suit challenging a \$15 fax fee was improper.

B. Fifth Circuit Decision on Check-Cashing Fees

The Fifth Circuit U.S. Court of Appeals held that national banks are authorized by federal regulation²⁶ to charge non-account holding payees a check-cashing fee.²⁷ The case involved a Texas "Par Value" statute that prohibits banks from charging a fee to non-account holding payees who present a check to the payor bank (the bank that holds the account that the check is drawn against). Wells Fargo Bank of Texas, a national bank, sought a permanent injunction and declaration that the Texas Par Value statute was null and void based on federal preemption, relying on 12 C.F.R. section 7.4002(a).

The court found that the OCC was operating within its power in promulgating section 7.4002. Section 7.4002 provides that national banks may charge "customers" non-interest charges and fees for authorized services. The OCC interprets "customers" to include any person who presents a check for payment.²⁸ Although the court acknowledged that such an interpretation of customer is not the only reasonable interpretation, the court concluded that the OCC's interpretation that customer includes payees who present a check to a drawee bank for payment due is controlling. The court held that because the Texas Par Value statute prohibits the exercise of a power that federal law expressly grants to national banks, the Par Value statute is in irreconcilable conflict with the federal

regulatory scheme and it is preempted by operation of the Supremacy Clause of the U.S. Constitution.

VII. State Debt Collection Act Not Preempted

The National Credit Union Administration (NCUA) issued an opinion letter stating that federal law does not preempt the Texas Debt Collection Act and thus a federal credit union must comply with that law to the extent that it has members who are Texas residents.²⁹ The letter explains that the NCUA's lending regulation specifies that it is not the intent of the NCUA to preempt state laws affecting aspects of credit transactions that are primarily governed by federal laws other than the Federal Credit Union Act, including state laws concerning debt collection practices.³⁰

The NCUA letter refers to the Fair Debt Collection Practices Act (FDCPA), which anticipates that states may also regulate this area.³¹ The FDCPA provides that state efforts to regulate debt collection practices will not be considered inconsistent, for preemption purposes, if the differences in the state law provide relatively greater protection to the consumer. The NCUA concluded that the Texas Debt Collection Act meets this standard. Finally, the NCUA letter states that any state official asserting a claim against a federal credit union involving the Texas law or any other applicable state law relating to lending activities would need to refer the matter to the appropriate NCUA regional office, based on the NCUA's exclusive examination and enforcement jurisdiction. The Texas law has since been amended and the special disclosure requirement no longer applies to a creditor acting on its own behalf in collecting an overdue debt.

VIII. Predatory Lending Laws Preempted

A. OTS Letter *Re* New Mexico Law

The OTS issued a preemption letter finding that federal law preempts the provisions of the New Mexico Home Loan Protection Act and precludes those provisions from applying to federal savings banks and their operating subsidiaries.³² The OTS previously addressed similar provisions of the Georgia, New Jersey, and New York predatory lending laws. The OTS letter on New Mexico states that, for the reasons addressed in prior letters, New Mexico provisions purporting to regulate the terms of credit, loan-related fees, disclosures, mortgage processing, origination, refinancing and servicing, and disbursements are preempted from applying to federal savings banks.

For the same reasons, the OTS stated that the New Mexico Act's compliance scheme could not be applied to a federal savings bank in a manner that would compel compliance with the preempted provisions. The OTS stated that the provisions preempted from applying to federal savings banks in this manner include those: (1) using state foreclosure law as a tool to compel compliance; (2) allowing borrowers to bring civil actions for violations and to assert claims, defenses, counterclaims and actions against creditors or subsequent holders or assignees including in foreclosures actions; (3) deeming violations to be unfair or deceptive trade practices; and (4) providing for administrative enforcement by the Financial Institutions Division of the New Mexico Department of Regulation and Licensing.

26. 12 CFR § 7.4002(a)

27. *Wells Fargo Bank of Texas, N.A. v. James*, 321 F.3d 488 (5th Cir. 2003).

28. *Cf.* the meaning of "customer" as defined in the Uniform Commercial Code at § 4-104(a)(5) (2003 uniform text), or in the Gramm-Leach-Bliley Act implementing regulations at 16 CFR § 313.3(h).

29. NCUA Letter from Sheila A. Albin, Associate General Counsel (Nov. 26, 2003).

30. 12 CFR § 701.21(b)(3).

31. 12 U.S.C. § 1692n.

32. OTS Letter P-2003-6 from Carolyn Buck, Chief Counsel (Sept. 2, 2003).

B. OTS Letter *Re* New Jersey Law

The OTS, in response to a letter from a federal savings bank, concluded that federal law preempts the application of certain provisions of the New Jersey Home Ownership Security Act of 2002, including its compliance scheme, to federal savings banks (FSBs) and their operating subsidiaries.³³ The OTS also concluded that those who purchase or are assigned loans that are originated by a FSB under the New Jersey Act would be subject only to the claims and defenses that would apply to the FSB that originated the loan because the New Jersey Act expressly indicates that purchasers and assignees are subject only to those claims and defenses that a borrower could assert against the original creditor.

The New Jersey Act imposes requirements on the terms of credit, loan-related fees, disclosures, processing, originating and servicing mortgages, and disbursements in connection with home loans. In its response, the OTS concluded that the provisions of the New Jersey Act that purport to regulate the terms of credit, loan-related fees, disclosures, mortgage processing, origination, refinancing, servicing, and disbursements are preempted by federal law from applying to FSBs and their operating subsidiaries. In addition, the OTS concluded that the New Jersey Act's compliance scheme is preempted as to FSBs.

In support of its conclusion, the OTS indicated that the federal Home Owners' Loan Act (HOLA) and regulations issued by the OTS occupy the field of regulation for the lending activities of FSBs. The OTS indicated that such federal regulation is "exclusive, leaving no room for state regulation, conflicting or complementary." In support of its conclusion, the OTS cited section 560.2 of the OTS Regulations, which generally provides that FSBs may extend credit as authorized under federal law without regard to state

laws that purport to regulate or otherwise affect their credit activities. Section 560.2 also sets forth specific types of state laws that are preempted, such as state laws on the terms of credit, loan-related fees, disclosure, processing, servicing, sale, investment and participation in mortgages and disbursements.

The OTS indicated that the New Jersey Act contains a number of restrictions and requirements on home lending that fall within these areas and thus are preempted. According to the OTS, such preemption is necessary because subjecting FSBs to the burdens of complying with a hodgepodge of conflicting and overlapping state lending requirements would undermine the federal objective of permitting FSBs to exercise their lending powers under a single set of uniform federal laws and regulations.

C. OCC Letter *Re* Georgia Law

The OCC, in response to a request by National City Bank and its operating subsidiaries, issued a preemption determination and order concluding that the Georgia Fair Lending Act (GFLA) does not apply to national banks or their operating subsidiaries.³⁴ The OCC stated that its preemption determination and order are supported by the following federal authority:

- National banks' authority to engage in real estate lending activities derives exclusively from federal law;
- the federal statute that broadly authorizes national banks' real estate lending activities, 12 U.S.C. section 371, precludes application of many provisions of the GFLA to national banks as the statute specifically gives the OCC the authority to determine the restrictions and requirements that apply to na-

tional banks' real estate lending activities;

- national banks' real estate lending standards are already subject to a comprehensive federal regulatory framework that addresses the types of abusive and predatory practices that the GFLA seeks to prohibit. The OCC has issued detailed guidance applicable to national banks' mortgage originations, use of mortgage brokers, and purchases of loans from others;
- the OCC regulations implementing 12 U.S.C. section 371 currently provide that certain types of state laws (such as terms of repayment and maturity) do not apply to national banks;
- section 371 and OCC regulations preempt the GFLA provisions that, pursuant to the *Barnett* standards and lower federal court case law applying those standards, impermissibly obstruct, alter or condition a national bank's exercise of its federally authorized real estate lending powers; and
- some provisions of the GFLA purport to limit the interest a national bank may charge for certain types of loans, but as the U.S. Supreme Court has affirmed, the rate of interest that is permissible for national banks is determined exclusively by federal law, under 12 U.S.C. section 85. Section 85 permits national banks to charge the most favorable rate permitted by the laws of the state in which the bank is located, regardless of where the borrower is located.

The GFLA generally restricts the ability of lenders to charge certain fees and engage in certain practices for three

33. OTS Letter P-2003-5 from Carolyn J. Buck, Chief Counsel (July 22, 2003).

34. 68 Fed. Reg. 46264 (2003).

categories of loans: "home loans," "covered home loans," and "high-cost home loans." These categories of loans are defined with respect to the annual percentage rate and the amount of points and fees charged. Under the GFLA, all "home loans" are subject to certain restrictions on the terms of credit and loan-related fees, including prohibitions on the financing of credit insurance, debt cancellation or suspension coverage, and limitations on late fees and payoff statement fees.

D. Georgia Response

The Georgia Department of Banking and Finance (Department) issued a Declaratory Ruling in response to the OCC's preemption determination (discussed above).³⁵ The Department concluded that, as federal law has been determined by the authorized federal agency to preempt the applicability of the GFLA for national banks and their operating subsidiaries, pursuant to section 7-6A-12 of the GFLA the GFLA will not apply to state-chartered banks and their subsidiaries. By the terms of the GFLA, this exclusion extends to state banks regardless of their state of charter.

The Department cautioned, however, that should any part of the OCC's preemption determination be overturned, clarified or revised, state banks would become subject to those provisions to which national banks are subject. In the meantime, the GFLA remains in effect for finance companies, mortgage brokers, mortgage bankers, and various others who make home loans in Georgia. The Department's ruling was supported by an opinion from the Georgia Attorney General issued on August 4, 2003, concluding that the OCC had the requisite authority to preempt the GFLA.³⁶ The Attorney General reviewed the preemption cases since *Barnett*, including the *Sorrell* case in Georgia, observing that "it appears...as long as the OCC's legal conclusions are related to the banking ac-

tivities of national banks the decision will be difficult to challenge successfully."³⁷

E. OTS Letter *Re Georgia Law*

In response to an inquiry, the OTS issued a letter in which it concluded that provisions of the GFLA purporting to regulate the terms of credit, loan-related fees, disclosures, or the ability of a creditor to originate or refinance a loan, are preempted by federal law from applying to federal savings associations and their operating subsidiaries.³⁸ The OTS noted that the GFLA places various restrictions on "home loans," "covered home loans," and "high-cost home loans," each of which are defined by the statute, including: (1) restrictions on the terms of credit and loan-related fees (e.g., prohibiting the financing of credit insurance or debt cancellation or suspension coverage and limiting late fees and payoff statement fees) on "home loans;" (2) restrictions on other terms of credit and refinancing restrictions on "covered home loans;" and (3) additional restrictions on terms of credit and disclosure requirements for "high-cost home loans."

In its letter the OTS again stated that, consistent with the language of the HOLA, OTS regulations give federal savings associations maximum flexibility to exercise their lending powers in accordance with a uniform federal scheme of regulation. That uniform federal scheme occupies the field of regulation for lending activities. Further, the OTS stated, the comprehensive nature of the HOLA language demonstrates that Congress intended the federal scheme to be exclusive, leaving no room for state regulation, whether conflicting or complementary. According to the OTS, its occupation of the field enhances safety and soundness and enables federal savings associations to conduct their operations in accordance with best practices by efficiently delivering low-cost credit to the public free

from any undue regulatory duplication and burden.

The OTS noted that it has described with specificity the scope of its occupation of the field of lending in its regulation at 12 C.F.R. section 560.2 by enumerating the types of state laws encompassed within its preemption. Section 560.2 generally provides that FSBs may extend credit as authorized under federal law without regard to state laws that purport to regulate or otherwise affect their credit activities. Section 560.2 also sets forth specific types of state laws that are preempted, such as state laws governing the terms of credit, loan-related fees, disclosure and advertising, and the processing, origination, servicing, sale, purchase, investment and participation in mortgages. Because the GFLA would regulate areas covered by section 560.2, the OTS concluded that the GFLA does not apply to federal savings associations' home lending. With respect to application of the GFLA to a federal savings association's operating subsidiaries, the OTS similarly concluded that state laws purporting to regulate the activities of a federal savings association's operating subsidiary are preempted by federal law to the same extent such laws are preempted as to the federal savings association itself.

F. OTS Letter *Re New York Law*

The OTS, in response to a letter from a federal savings bank, concluded that federal law preempts the application of the New York Predatory Lending Law (NYPLL) to FSBs.³⁹ The NYPLL imposes requirements on the terms of credit, loan-related fees, disclosure and advertising, and mortgage origination, refinancing and servicing in connection with high-cost home loans.⁴⁰ In its

35. Ga. Dept. of Bank and Fin. Declaratory Ruling, August 5, 2003.

36. Ga. Att'y Gen. August 4, 2003.

37. *Id.*

38. OTS Letter P-2003-1 from Carolyn J. Buck, Chief Counsel (January 21, 2003).

39. OTS Letter P-2003-2 from Carolyn J. Buck, Chief Counsel (January 30, 2003).

40. See, e.g., Joseph W. Gelb and Peter N. Cubita, *The New York State Predatory Lending Law*, 57 Consumer Fin. L. Q. Rep. 135 (2003); Stephen F. J. Ornstein and Matthew S. Yoon, *2003 Amendments to the New York Part 41 Regulations*, id., 139.

response the OTS concluded that the provisions of the NYPLL that purport to regulate the terms of credit, loan-related fees, disclosure, advertising, mortgage origination, refinancing, and servicing, are preempted by federal law from applying to FSBs and their operating subsidiaries.

In addition, the OTS concluded that the NYPLL's compliance scheme is preempted for FSBs. In support of its conclusion, the OTS indicated that the HOLA and regulations issued by the OTS occupy the field of regulation for lending activities of FSBs. The OTS again indicated that such federal regulation is "exclusive leaving no room for state regulation, conflicting or complementary." The OTS specifically cited section 560.2 of the OTS regulations in support of its conclusion. Section 560.2 sets forth specific types of state laws that are preempted, such as state laws on terms of credit, loan-related fees, disclosure, advertising, processing, origination, servicing, sale, purchase, investment, and participation in mortgages. The OTS concluded that many of the provisions of the NYPLL would fall within these areas, and thus would be preempted. The OTS stated that such preemption is necessary because subjecting FSBs to the burdens of complying with a hodgepodge of conflicting and overlapping state lending requirements would undermine the federal objective of permitting FSBs to exercise their lending powers under a single set of uniform federal laws and regulations.

IX. Preemption Impacting Multiple Types of Entities

A. The Lockyer Decision

In *American Bankers Association v. Lockyer*⁴¹ the California federal district court invalidated on federal preemption grounds the entire California minimum payment periodic statement disclosure law (Civil Code section 1748.13) with

respect to national banks, federal savings associations or savings banks, and federal credit unions. The court, however, did note that a California law that merely required a simple warning on a periodic statement that "Making the minimum payment will increase the interest you pay and the time it takes to repay the balance" (a disclosure required under the law at issue) likely would not be preempted as to national banks. Moreover, the court declared that, more generally, states could impose some consumer protection regulation on national banks in the areas of "contracts, debt collection, acquisition and transfer of property, and taxation, zoning, criminal, and tort law" as long as such regulation would not "prevent or significantly interfere with" national banks' federally-granted powers.

The *Lockyer* court also held that even a limited disclosure such as the above-quoted one is preempted as to federal savings associations under the HOLA and OTS regulations at 12 C.F.R. section 560.2(b)(9). The court granted a permanent injunction prohibiting enforcement of the statute against federally chartered credit card issuers. A stipulation extending the permanent injunction in *Lockyer* was signed on Monday, January 13, 2003. The stipulation stated that the permanent injunction issued by the court on December 23, 2002 now applies as well to all non-federally chartered card issuers. However, there may be a serious issue with regard to the validity and/or constitutionality of the order insofar as it covers non-parties to the case.

B. Ninth Circuit Decision

In *Bank of America v. City and County of San Francisco*⁴² the U.S. Court of Appeals for the Ninth Circuit held that national banks and federal savings associations need not comply with ordinances limiting automated teller machine (ATM) fees enacted by the cities of San Francisco and Santa Monica, due to fed-

eral preemption. The case involved the cities of San Francisco and Santa Monica, California each of which in 1999 enacted identical ordinances barring financial institutions (defined to include banks, savings associations, savings banks, credit unions and industrial loan companies) from charging nondepositors a fee for using their ATMs. Bank of America and Wells Fargo Bank, both national banks, and the California Bankers Association filed suit challenging the validity of the ordinances. California Federal Bank, a federal savings bank, was subsequently added as a plaintiff. The Ninth Circuit held that the ordinances are preempted by (1) the HOLA and OTS regulations (with respect to federal savings associations) and (2) the NBA and OCC regulations (with respect to national banks). The regulation of federal savings associations by the OTS is so pervasive, said the Ninth Circuit, as to leave no room for state regulatory control. Therefore, state limitations on the authority of federal savings associations to collect ATM fees are invalid under the Supremacy Clause of the U.S. Constitution. The court also held the ordinances invalid with respect to national banks, specifically rejecting the cities' contention that charging ATM fees to nondepositors exceeds the incidental powers granted to national banks under section 24 (Seventh) of the NBA.

Finally, in response to the cities' argument that the Electronic Funds Transfer Act (EFTA)⁴³ authorizes states to regulate ATM fees as a consumer protection measure, the court opined that the EFTA does not save the ordinances from preemption for two reasons. First, the regulation of ATM fees is not the type of consumer protection measure contemplated by the EFTA and, second, the EFTA anti-preemption provision (which saves state laws affording greater protection to consumers than the EFTA from preemption by the EFTA) does not preclude preemption by other statutes, such as the HOLA and the NBA. Accordingly,

41. 239 F.Supp. 2d 1000 (E.D. Cal. 2002).

42. 309 F.3d 551 (9th Cir. 2002), cert. denied, 123 S. Ct. 155 (2003). See also *supra* this text at note 23.

43. 15 U.S.C. §§ 1693-1693r.

the Ninth Circuit affirmed the district court's grant of summary judgment to the banks as well as the permanent injunction prohibiting the cities from enforcing the ordinances.

X. Arkansas Usury Preemption Under the GLB Act

The Eighth Circuit U.S. Court of Appeals held that a federally-insured Arkansas-chartered bank could, under the Gramm-Leach-Bliley Act (GLB Act),⁴⁴ charge interest to a Texas resident at the same rate as the Arkansas branch of an Alabama-chartered bank.⁴⁵ A Texas resident argued that the 18.5 percent interest rate imposed on his credit card by the Arkansas bank was in violation of Arkansas and Texas usury laws. Under a special provision, the GLB Act allows federally-insured Arkansas banks to charge interest at a rate allowed by the state of any out-of-state bank with a branch office in Arkansas, except when the Arkansas bank has "made" the loan in any state other than Arkansas.

The Eighth Circuit found that the loan in question was "made" in Arkansas and so the rate authorized by the GLB Act could be imposed without regard to the location of the borrower.⁴⁶ The court relied on prior OCC letters involving branches to conclude that a loan is "made" for GLB Act purposes at the location where the lender approves the loan, extends the credit, and disburses the funds.⁴⁷ In this case, the court concluded that all such functions occurred in Arkansas.

XI. Insurance Preemption

A. Fourth Circuit Decision

In *Cline v. Hawke*,⁴⁸ an unpublished opinion of a three-judge panel of the United States Court of Appeals for the Fourth Circuit, the court upheld an OCC opinion that concluded that section 104 of the GLB Act preempts certain portions of the West Virginia Insurance Sales Consumer Protection Act (CPA). The case involved a petition by the Insurance Commissioner of the State of West Virginia and the State of West Virginia for review of the 2001 OCC preemption opinion. The OCC's 2001 opinion considered certain provisions of the West Virginia CPA, which sets forth numerous requirements regarding insurance sales, solicitation, and crossmarketing activities of financial institutions, including national banks. In reviewing seven sections of the CPA, the OCC determined that under the preemption standards of the GLB Act, three were preempted and one was preempted in part. The OCC opinion also considered one additional section of the CPA, which it determined to be preempted by the federal Fair Credit Reporting Act.

In reviewing the OCC's 2001 opinion, the *Cline* court considered whether the OCC had authority to interpret the GLB Act and, if so, whether the OCC properly exercised such authority. The court also considered what deference to give to the OCC's interpretation. The court found that the language of the GLB Act clearly gave the OCC interpretive authority as to the GLB Act. Additionally, the *Cline* court found that the GLB Act entitled the OCC to some level of deference with respect to its interpretations and that such deference is to be governed by the standards set forth in *Skidmore v. Swift & Co.*⁴⁹ (i.e., the OCC's interpretation is entitled to deference to the extent such interpretation has the "power to persuade"). Finding that the OCC had been

thorough in its review of the provisions of the CPA (e.g., the OCC had considered public comments prior to its preemption determination) and that it had used valid reasoning in its decision, the *Cline* court dismissed the petition for review.

B. First Circuit Decision

The U.S. Court of Appeals for the First Circuit dismissed a petition filed by the Commonwealth of Massachusetts and its Commissioners of Insurance and Banks in which they sought to vacate an opinion of the OCC.⁵⁰ The informal opinion letter of the OCC had indicated that the GLB Act preempts certain provisions of Massachusetts law that regulate the sales, solicitation, and cross-marketing activities of national banks within Massachusetts.

The petitioners claimed that the OCC opinion letter created a regulatory conflict between a Massachusetts insurance regulator and the OCC regarding insurance issues, and therefore argued that judicial review of the opinion was permissible under section 304(a) of the GLB Act. Section 304(a) of the GLB Act provides that in the case of a regulatory conflict between a state insurance regulator and a federal regulator regarding insurance issues (including preemption issues), either regulator may seek expedited judicial review of such determination in the United States Court of Appeals for the circuit in which the state is located or in the United States Court of Appeals for the District of Columbia Circuit by filing a petition for review in such court.⁵¹

In *Bowler*, however, the First Circuit disagreed with the petitioners. According to the court of appeals, the OCC opinion letter constituted no more than informal agency guidance, which (1) could not constrain the petitioners in any meaningful way from enforcing the provisions of Massachusetts law, and (2) did

44. Pub. L. No. 102-106 (1999). See generally, *Symposium on Privacy*, 55 Consumer Fin. L. Q. Rep. 4 (2001).

45. *Jessup v. Pulaski*, 327 F.3d 682 (8th Cir. 2003), citing 12 U.S.C. § 1831u(f)(2).

46. *Jessup*, 327 F.3d at 684-85.

47. *Id.*

48. 2002 WL 31557392 (4th Cir. Nov. 19, 2002), cert. denied, 124 S. Ct. 63 (2003).

49. 323 U.S. 134 (1944).

50. *Bowler v. Hawke*, 320 F.3d 59 (1st Cir. 2003).

51. 15 U.S.C. § 6714(a).

not authorize third parties to engage in conduct forbidden by the preempted law. For these reasons, the First Circuit found that there was no case or controversy between the petitioners and the OCC that would constitute a regulatory conflict subject to judicial review under section 304(a) of the GLB Act, and consequently, the petition was dismissed.

XII. Alternative Mortgage Transactions

A. District of Columbia Decision

The United States District Court for the District of Columbia held that the OTS's interpretation as to the scope of preemption under the Alternative Mortgage Transaction Parity Act (AMTPA) was entitled to deference and the amended OTS AMTPA rule was not arbitrary and capricious.⁵² The OTS had determined that the regulations governing prepayment penalties and late fees would no longer apply to state housing creditors (as defined in AMTPA). Therefore, such creditors would be required to comply with state law requirements on prepayment penalties and late fees. The *National Home Equity* court found that the AMTPA gives the OTS the authority to identify the scope of regulation applicable to state housing creditors, and therefore the OTS interpretation was entitled to deference. The court found that the OTS's amended rule, concluding that federal regulations on prepayment penalties and late fees restrictions were not essential or intrinsic to state housing creditors' ability to offer alternative mortgages, was not arbitrary and capricious.

B. New Jersey Decision

The Superior Court of New Jersey found that the OTS exceeded its authority in preempting prepayment penalties

under the AMTPA regulations.⁵³ Thus, the court permitted the mortgagor to assert claims that the prepayment penalty violated state law on an alternative mortgage transaction. The court found that the OTS acted arbitrarily and exceeded the authority delegated by Congress under the AMTPA in adopting 12 C.F.R. section 560.220. The court referred to the recent amendment of the AMTPA regulations that removed the reference to prepayment penalties as recognition by the OTS that state law limitations on prepayment penalties do not interfere with alternative mortgage transactions.

C. Seventh Circuit Decision

The U.S. Court of Appeals for the Seventh Circuit held that the Home Ownership and Equity Protection Act of 1994 (HOEPA) does not repeal the AMTPA.⁵⁴ The court held that as the two statutes are not irreconcilable and the later statute contains no express repeal, there is no repeal. The suit was brought by mortgage lenders and brokers seeking a declaratory judgment that anti-predatory lending regulations were preempted by section 3803(c) of the AMTPA as to state-chartered lenders.

The Seventh Circuit held that state regulations are preempted under section 3803(c) to the extent that the state regulation blocks state lenders from extending credit on terms permitted under federal regulations, when the lenders actually comply with the federal regulations. The court remanded the case to the district court to determine which provisions of the state regulations are incompatible with the federal regulations.

XIII. Governing Law Provisions

Lenders relying on federal preemption need to review their governing law provisions to ensure that they are not adopting by contract more home state law

than they intend. Federal preemption is a matter of federal law and a specific statement in a contract is not required for a lender to rely on federal preemption. However, it is possible for a lender and a borrower to agree by contract to terms that are more restrictive than those that the lender is otherwise required to comply with under federal law.

In *Wells v. Chevy Chase Bank, FSB*,⁵⁵ credit cardholders brought an action against an issuing federal savings bank alleging that the bank violated a provision of the credit card agreement when it raised fees without giving the notice required by Maryland Subtitle 9. The cardholder agreement stated: "We may amend the terms of this Agreement in accordance with applicable law at any time." The cardholder agreement also contained a choice of law provision reading:

This Agreement is made in Maryland. It is governed by Subtitle 9 ["Credit Grantor Revolving Credit Provisions"] of Title 12 ["Credit Regulations"] of the Commercial Law Article of the Maryland Annotated Code and applicable federal laws.

The cardholders sued the lender on a breach of contract theory. The court stated that Subtitle 9 is a state law that falls within the category of state imposed obligations that 12 C.F.R. section 560.2 preempts. Thus, the court and the parties agreed that the bank was not required to comply with Subtitle 9 by statute. The court, however, also recognized that section 560.2 expressly exempts from preemption certain contract laws and thus a federal savings bank's contractual undertakings are not preempted. The court concluded that Subtitle 9 was relevant to the case because the agreement between the parties referred to it. The court remanded the case to the lower court to apply state law contract interpretation to determine the parties' rights and obligations under the agreement.

53. *Glukowsky v. Equity One, Inc.*, 360 N.J. Super. 1 (2003), cert. granted, 177 N.J. 575 (2003).

52. *National Home Equity Mortgage Ass'n v. Office of Thrift Supervision*, 271 F.Supp. 2d 264 (D.D.C. 2003).

54. *Illinois Ass'n of Mortgage Brokers v. Office of Banks and Real Estate*, 308 F.3d 762 (7th Cir. 2002).

55. 377 Md. 197 (2003), cert. denied, 124 S.Ct. 1875 (2004).