Interstate Delivery of Consumer Financial Services: Credit Card Issuers Win Decisions in *Greenwood Trust* and Related Cases

*by Darrell L. Dreher and Michael C. Tomkies**

The United States Court of Appeals for the First Circuit, in *Greenwood Trust Co. v. Massachusetts,*[1] reversed the Massachusetts federal district court's decision that prohibited Greenwood Trust Company, a Delaware-chartered bank, from charging late fees on its credit card accounts with Massachusetts cardholders.[2] The First Circuit ruled in favor of Greenwood Trust Company on the issue of federal preemption, holding that late fees are "interest" under section 521 of the Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDMCA)[3] and thus may be charged to residents of foreign states (referred to as the "exportation" of interest and fees).[4]

The First Circuit's decision in *Greenwood Trust* agreed with two Minnesota federal district court decisions involving class action lawsuits filed in the awake of the district court decision in *Greenwood Trust.* In *Hill v. Chemical Bank,*[5] the Minnesota district court concluded that late fees, overlimit fees, and similar charges were "interest" for purposes of exportation under section 521 of the DIDMCA.[6] This decision followed the Minnesota district

*Mr. Dreher, a member of the Ohio bar, practices law with Jones, Day, Reavis & Pogue in Columbus, Ohio. He is the chairman of the Subcommittee on the Interstate Delivery of Consumer Financial Services. Mr. Tomkies, a member of the Ohio and District of Columbia bars, also practices law with Jones, Day, Reavis & Pogue in Columbus.

1. 776 F. Supp. 21 (D. Mass. 1991), *rev'd,* 971 F.2d 818 (1st Cir. 1992), *cert. denied,* 113 S. Ct. 974 (1993).

2. *See* Darrell L. Dreher & Michael C. Tomkies, *Interstate Delivery of Consumer Financial Services:* Greenwood Trust *Decision Rendered,* 47 Bus. Law. 1251 (1992) (discussing lower court decision).

3. Pub. L. No. 96-221, § 521, 94 Stat. 132, 164 (1980) (codified at 12 U.S.C. § 1831d (1988 & Supp. III 1991)) [hereinafter DIDMCA].

4. *Greenwood Trust,* 971 F.2d at 831.

5. 799 F. Supp. 948 (D. Minn. 1992). In this decision, the district court considered motions to remand from both Hill v. Chemical Bank and Fasulo v. Chemical Bank, although the cases were not formally consolidated. *Id.* at 949. *Hill* was dismissed without prejudice Aug. 10, 1992. *Fasulo* was dismissed without prejudice Aug. 7, 1992.

6. *Id.* at 952-54.

court decision in *Nelson v. Citibank (South Dakota), N.A.*[7] in which a different judge denied motions to remand, holding that late fees and overlimit charges were "interest" under sections 85 and 86 of the National Bank Act.[8]

THE GREENWOOD TRUST *APPEAL*

The First Circuit found express federal preemption of state law based on the language of section 521.[9] Because federal preemption provided a resolution of the matter, the court did not reach any of the Massachusetts law issues raised on appeal.[10]

With respect to the scope of preemption under section 521, the court found that the issue required it to consider Congress' intent by its use of the terms *interest* and *interest rates*.[11] The court rejected as unpersuasive the lower court's narrow "plain meaning" analysis of the text of section 521, noting that federal court opinions have long suggested that, in ordinary usage, "interest" may encompass late fees and kindred charges.[12]

The court concluded that the text of the statute is inconclusive and turned instead to a consideration of legislative and historical context.[13] The court determined that "[t]he historical record clearly requires a court to read the parallel provisions of [DIDMCA] and [section 85 of the National] Bank Act *in pari materia*" because Congress used the same language in both and intended to create parity between federally insured state-chartered banks and national banks.[14] The First Circuit noted that many principles inherent in section 85, including exportation authority and the most favored lender doctrine,[15] consequently are "transfused" into section 521.[16] The court opined that "[t]o the extent that a law or regulation

7. 794 F. Supp. 312 (D. Minn. 1992). In this decision, the district court considered motions to remand from both Nelson v. Citibank (South Dakota), N.A. and Tikkanen v. Citibank (South Dakota), N.A. *Id.* at 313. The ruling was followed by a decision in which the court granted the defendants' motions for summary judgment and denied the plantiffs' motions for voluntary dismissal. Tikkanen v. Citibank (South Dakota), N.S., 801 F. Supp. 270 (D. Minn. 1992). The plaintiffs did not appeal the decision.

8. *Nelson*, 794 F. Supp. at 320; *see* 12 U.S.C. §§ 85, 86 (1988 & Supp. III 1991).

9. *Greenwood Trust*, 971 F.2d at 831.

10. Greenwood Trust Co. also had challenged the lower court's rulings that Massachusetts' prohibition against late fees on credit card loans reaches out-of-state credit card issuers and that Massachusetts law evidences a fundamental public policy that overrides the contractual choice-of-law provision in the cardholder agreement choosing Delaware law. *See* Brief for Appellant Greenwood Trust Company, Greenwood Trust Co. v. Massachusetts, 971 F.2d 818 (1st Cir. 1992); Dreher & Tomkies, *supra* note 2, at 1257-58.

11. *Greenwood Trust*, 971 F.2d at 824.

12. *Id.* at 826.

13. *Id.* at 826-27.

14. *Id.* at 827.

15. The most favored lender doctrine was first expressed in Tiffany v. National Bank of Mo., 85 U.S. (18 Wall.) 409, 411 (1874).

16. *Greenwood Trust*, 971 F.2d at 827 n.8.

enacted in the borrower's home state purposes [sic] to inhibit the bank's choice of an interest term under section 521, [DIDMCA] expressly preempts the state law's operation," Massachusetts law must yield insofar as the regulation of "interest" is concerned.[17]

Because the court found the DIDMCA's text and legislative history also to be inconclusive with respect to the interpretation of the terms *interest* and *interest rates*, the court indicated that federal common law or state law must give content to these terms.[18] Although the terms are contained in a federal statute, the court noted that resort to uniquely federal definitions is not automatic if Congress intends state law to fill the interstices within a federal legislative scheme.[19] The court stated that while state law cannot be permitted to define a statutory term in a way entirely strange to ordinary usage, where there are permissible variations in the ordinary concept of the term, a court may deem state law controlling.[20] In the court's view, however, both state law and federal common law produced the same result.[21] The court therefore declined to decide which law, state or federal, was the appropriate point of reference.[22]

The court stated, however, that if state law were applicable, the court would apply the laws of the bank's home state—Delaware in this case.[23] The court said that it was bolstered in its interpretation by the recognition that section 85 "adopts the entire case law" of a bank's home state.[24] The court noted that federal common law provides the same result and observed that courts "have had little trouble in construing the term 'interest' to encompass a variety of lender-imposed fees and financial requirements which are independent of a numerical percentage rate."[25] While noting that some such cases were decided with respect to intrastate loans and not in the exportation context, the court said that it discerned no principled basis for defining *interest* differently in intrastate and interstate contexts.[26] The court rejected the lower court's reliance on section 501 of DIDMCA for the meaning of *interest* as "misplaced" because the several provisions are part of different statutes that address different categories of lenders and loans and contain "materially different preemption terms."[27]

17. *Id.* at 827.

18. *Id.* at 828.

19. *Id.*

20. *Id.* at 829.

21. *Id.*

22. *Id.*

23. *Id.*

24. *Id.* (quoting First Nat'l Bank v. Nowlin, 509 F.2d 872, 876 (8th Cir. 1975)).

25. *Id.* (citing Nelson v. Citibank (South Dakota), N.A., 794 F. Supp. 312, 318 (D. Minn. 1992)).

26. *Id.* at 830.

27. *Id.* at 830 n.10; *see* DIDMCA § 501, 12 U.S.C. § 1735f-7a (1988). Section 501 preempts state law limitations on the rate or amount of interest, discount points, finance charges, or other charges which may be charged, taken, received, or reserved with respect to certain specified types of federally related first mortgage loans. DIDMCA § 501(a)(1), 12 U.S.C. § 1735f-7a(a)(1) (1988).

The court stated that construing the terms *interest* and *interest rates* to include late fees is most consistent with the stated legislative purposes of section 521.[28] The court also found "broad support" for its construction in the administrative rulings and informal opinion letters of federal regulatory agencies, citing by way of example the Comptroller's most favored lender interpretive ruling[29] for the proposition that all of a bank's home-state laws that are "material to the determination of the interest rate" are exportable.[30] The court did not dwell on administrative interpretations because, the court said, it would have reached the same result independent of them.[31]

HILL V. CHEMICAL BANK

The Minnesota federal district court in *Hill* engaged in a two-step analysis: (i) whether section 521 completely preempted the field of usury claims against federally insured state-chartered banks, and (ii) whether the plaintiffs' claims were in fact usury claims challenging the rate of interest charged by a federally insured state-chartered bank within the meaning of section 521.[32] The court noted that section 521 establishes the maximum interest rate for federally insured state-chartered banks and creates a federal remedy.[33] The court further noted that section 86 of the National Bank Act has been construed to provide an exclusive remedy for a violation of section 85.[34] Because section 521 contains provisions nearly identical to sections 85 and 86, the district court concluded that section 521 completely preempts the field of usury claims against federally insured state-chartered banks.[35]

On the issue of whether the plaintiffs' state law claims nevertheless may fall outside the preemptive scope of section 521, the court cited the decision in *Nelson* for a "wealth of authority" in case law and agency determinations that interpreted "interest" under section 85 to include fees other than periodic interest charges.[36] The court stated that the same result must hold true under section 521 because the statutes have nearly identical

28. *Greenwood Trust*, 971 F.2d at 830.

29. 12 C.F.R. § 7.7310(a) (1992).

30. *Greenwood Trust*, 971 F.2d at 830.

31. *Id.* at 830 n.11. Because the court found that Massachusetts had opted back into federal preemption, *id.* at 813 n.4, the court did not address the effect of state opt-out under section 525 of DIDMCA, 12 U.S.C. §1730g note (1988), on the exportation authority of federally insured state-chartered banks other than to note its repeal in 1989. *Greenwood Trust*, 971 F.2d at 823 n.4.

32. Hill v. Chemical Bank, 799 F. Supp. 948, 951 (D. Minn. 1992).

33. *Id.* at 951.

34. *Id.* at 952; *see* 12 U.S.C. §§ 85-86 (1988 & Supp. III 1991).

35. *Hill*, 799 F. Supp. at 952. The court's reasoning follows that of the Eighth Circuit in M. Nahas & Co. v. First Nat'l Bank of Hot Springs, 930 F.2d 608 (8th Cir. 1991).

36. *Hill*, 799 F. Supp. at 952-53.

language and because Congress enacted section 521 to prevent discrimination against federally insured state-chartered banks.[37] Among other authorities, the *Hill* court relied on *Fisher v. First National Bank*[38] for the proposition that flat fees are "interest" under section 85 and, because of the parity intended between sections 85 and 521, under section 521 as well.[39] The court also cited a recent FDIC interpretive letter[40] confirming the agency's interpretation that section 521 authorizes federally insured state-chartered banks to export the same fees and charges on interstate loans as section 85 authorizes for national banks, including credit card late charges and overlimit fees.[41] The court specifically rejected the district court's analysis in *Greenwood Trust* with respect to the relevance and applicability of sections 501 and 525 of the DIDMCA.[42] Following the issuance of the *Hill* court's ruling on the motions for remand, the plaintiffs voluntarily dismissed their suits.

NELSON V. CITIBANK

The *Nelson* court's ruling denying remand to state court employed an analysis of the remand issue substantially similar to that later employed in *Hill*. Because the court found that under the authority of *M. Nahas*, *Fisher*, and other cases, sections 85 and 86 of the National Bank Act preempt the field of usury claims against national banks and that for purposes of Sections 85 and 86 flat fees constitute "interest," the court concluded that the plaintiffs' claims were in fact federal questions properly removable to federal court.[43]

In its subsequent decision, *Tikkanen v. Citibank (South Dakota), N.A.*,[44] the same court rejected the plaintiffs' attempts, after the defendants had filed summary judgment motions, to obtain voluntary dismissal of the cases, or stays of the actions, on grounds that the relevant law was "unsettled."[45] The court noted that the issues in *Tikkanen* arose out of two lines of cases that interpret section 85 of the National Bank Act: (i) cases interpreting the definition of *interest* under section 85, and (ii) cases interpreting the "exportation principles" of section 85.[46] With respect to the first line of cases, the court noted its earlier ruling that "interest under section 85

37. *Id.* at 953.

38. 548 F.2d 255 (8th Cir. 1977).

39. *Id.* at 254-61.

40. FDIC Letter from Douglas H. Jones, Deputy Gen. Counsel (July 8, 1992) (on file with *The Business Lawyer*, University of Maryland School of Law).

41. *Hill*, 799 F. Supp. at 953.

42. *Id.*; *see* Greenwood Trust Co. v. Massachusetts, 776 F. Supp. 21, 29-32, 35-36 (D. Mass. 1991), *rev'd*, 971 F.2d 818 (1st Cir. 1992), *cert. denied*, 113 S. Ct. 974 (1993).

43. Nelson v. Citibank (South Dakota), N.A., 794 F. Supp. 312, 314 (D. Minn. 1992).

44. 801 F. Supp. 270 (D. Minn. 1992).

45. *Id.* at 273.

46. *Id.* at 274.

could not be defined narrowly to include only periodic interest charges, but included flat fees as well." [47] With respect to the second line of cases, the court observed that the United States Supreme Court in *Marquette National Bank v. First of Omaha Service Corp.*[48] acknowledged that the exportation of interest pursuant to section 85 could impair the ability of states to enact effective usury laws.[49] While acknowledging that plaintiffs' policy arguments for preserving an individual state's authority to enforce consumer protection laws had some appeal, the court dismissed them, stating that it must apply the controlling law.[50] The court consequently turned to a consideration of the plaintiffs' attempts to limit the application of the two lines of relevant case law.

The court reiterated its earlier rejection of plaintiffs' arguments that section 85 refers only to numerical interest rates and that the broad definition of *interest* applied under the most favored lender doctrine should apply only to intrastate, and not interstate, contexts.[51] The court then explored a third argument proposed by plaintiffs, that late and overlimit fees may be characterized under the common law as penalties outside the scope of interest limitations.[52] The court ultimately rejected the penalty/interest distinction as unpersuasive, noting that the cases cited by plaintiffs did not hold that late fees may never be deemed "interest" that implicates usury laws, and that the few cases cited by plaintiffs did not necessarily reflect a universal common law approach.[53] The court observed that, indeed, the variation among state usury statutes and cases construing them was the very genesis of the actions before the court.[54]

Next, addressing the plaintiffs' attack on the exportation principle on historical grounds, the court rejected the plaintiffs' argument that the National Bank Act was created only to address intrastate problems of bank note redemption.[55] The court noted that the Supreme Court determined in *Marquette* that the National Bank Act was intended to facilitate a national banking system that included interstate loans.[56] Finally, the court addressed the plaintiffs' constitutional arguments that (i) exportation under section 85 violates principles of state sovereignty, and (ii) the incorporation of state law definitions of *interest* represents an unconstitutional delegation of Congress' legislative authority to the states.[57] In disposing of these

47. *Id.* at 275.
48. 439 U.S. 299 (1978).
49. *Id.* at 318-19.
50. *Tikkanen*, 801 F. Supp. at 276.
51. *Id.* at 276-77.
52. *Id.* at 277.
53. *Id.* at 278.
54. *Id.*
55. *Id.* at 279.
56. *Id.*
57. *Id.*

arguments, the court concluded that the impairment of state authority results from the interaction of state and federal laws, not simply conflicts between two state laws, and that such impairment results from the Supremacy Clause of the United States Constitution.[58] The court also noted that while section 85 limits the scope of an individual state's laws, the statute does not preempt state laws in their entirety.[59] Because section 85 dictates the laws governing national banks but does not affect the operation of a particular state's laws upon banks within its borders, the court concluded that section 85 does not constitute an impermissible delegation of Congressional authority.[60]

The *Tikkanen* decision addressed several issues involving exportation authority not previously addressed by the First Circuit's *Greenwood Trust* decision or the court's earlier remand ruling, such as the penalty/interest distinction and the constitutional arguments proposed by the plaintiffs. Because the district court determined the *Nelson* and *Tikkanen* cases under section 85, however, the court did not reach arguments by the defendants that the plaintiffs' state law causes of action represented impermissible state law interference with lending powers conferred on national banks under section 24 (Seventh) of the National Bank Act.[61]

THE EFFECT OF THE DECISIONS

These opinions are well reasoned, well written, and consistent and therefore are likely to be persuasive to other courts. Indeed, these decisions have been cited in two subsequent state court cases also allowing the exportation of additional fees as "interest" under federal preemption.[62]

While the court decisions to date have agreed that the meaning of *interest*, for purposes of exportation by federally-chartered or federally-insured institutions, is broader than just a numeric rate, these decisions leave unanswered the full scope of federal preemption under sections 85 and 521 and the precise controlling law (whether federal or state law definitions

58. *Id.* at 280; *see* U.S. CONST. art. VI, cl. 2.

59. *Tikkanen*, 801 F. Supp. at 280.

60. *Id.*

61. 12 U.S.C. § 24 Seventh (1988 & Supp. III 1991).

62. Sherman v. Citibank, N.A., No. L-01834-92 (Super. Ct. Camden County, N.J. Order filed Nov. 25, 1992) (court dismissed with prejudice plaintiffs' challenge of late charge provisions on grounds of failure to state a claim; court found that the meaning of *interest* under section 85 is not limited to numerical interest rates, observing that "interest" is a charge on borrowed money that can come in many forms, including (under federal case law) late fees, closing costs, prepayment charges, and "other varieties"); Mazaika v. Bank One, Columbus, N.A., No. 4058 (C.P. Philadelphia County, Pa. Dec. 17, 1992) (court sustained defendant's objection that plaintiffs had no valid cause of action under Pennsylvania law; plaintiffs had challenged annual fee, late charge, returned check charge and overlimit charge provisions; court characterized the rationale of recent federal decisions as defining *interest* to include "those fees and charges that arise out of the extension and maintenance of credit").

of *interest*). Credit card issuers impose many kinds of fees and charges that have not been addressed specifically by the courts. Whether any courts will take divergent views remains to be seen.[63] A number of class actions precipitated by the district court decision in *Greenwood Trust* are still pending in a number of states against various state-chartered and national banks.

The decisions to date also do not directly address the permissibility of exporting non-fee terms under the concept of materiality[64] that originated under the most favored lender doctrine, although the First Circuit's passing reference to the Comptroller's interpretive ruling on the most favored lender doctrine[65] and the *Nelson* and *Tikkanen* rulings that the most favored lender doctrine and exportation authority should not be divergently interpreted may portend judicial consideration and eventual adoption of a materiality concept to define the scope of *interest* under sections 85 and 521. Because the decisions to date do not demarcate the outer boundaries of the definition of *interest* and because cases are still pending within other federal circuits, debate and litigation over the scope of federal preemption of interest rates likely will continue.

63. In at least one class action challenging the exportation of late charges by a state-chartered bank into California, a court has denied a demurrer. Order Overruling Demurrer, St. John v. Greenwood Trust Co., No. 695111-5 (Super. Ct. Alameda County, Cal. Order filed Dec. 17, 1992). The court stated that it could not conclude that Congress had, in drafting section 521 (expressly preempting state statutes and constitutions), the purpose of preempting the state common law complaints of the plaintiff which included charges of violation of an implied covenant of good faith and fair dealing.

64. *See* 12 C.F.R. § 7.7310 (1992).

65. *Id.*