A "Smiley" Conclusion to the Fee Exportation Saga: Certain Implications of *Smiley v. Citibank*

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In the most important interstate lending court decision since *Marquette National Bank v. First of Omaha Service Corp.*[1] in 1978, the United States Supreme Court upheld the authority of national banks to "export" loan fees deemed by an Interpretive Ruling of the Office of the Comptroller of the Currency (OCC)[2] to constitute "interest" under section 30 of the National Bank Act (NBA) (12 U.S.C. section 85 or section 85)[3] in *Smiley v. Citibank (South Dakota), N.A.*[4] The Court's decision in *Smiley* culminated nearly a decade[5] of litigation concerning whether and to what extent national banks and other federally-chartered or federally-insured financial institutions may impose fees allowed by the laws of the state where the institution is "located" as "interest" on loans to borrowers residing in other states.

This article will delineate the issues resolved by the *Smiley* decision and some of the key issues yet to be resolved. Despite the apparent breadth of the Supreme Court's opinion, a number of important interstate lending and bank administrative law issues were either created or left unresolved by the decision. This article will suggest means of resolving certain but not all of these unresolved issues.

I. Issues Resolved by *Smiley*

A. Fees That Constitute "Interest" Under Federal Law May be Exported by National Banks

Smiley conclusively resolves that national banks have the authority to export fees that are deemed "interest"[6] under OCC Interpretive Rule 7.4001 (the OCC Ruling), including the credit card late fees at issue in the case,[7] if the law of the state where the bank is located permits its most favored lender to charge the fees.[8] The

1. 439 U.S. 299 (1978).

2. 61 Fed. Reg. 4849, 4869 (1996) (to be codified at 12 CFR § 7.4001(a)).

3. 12 U.S.C. § 85 (1994). 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.

4. 116 S. Ct. 1730 (1996).

5. Iowa ex rel. Miller v. First Nat'l Bank, Civ. No. 88-20 (D. Del., filed Jan. 19, 1988, dismissed Apr. 15, 1988), was the first such suit filed.

6. The OCC Ruling provides in pertinent part:

> (a) *Definition.* The term "interest" as used in 12 U.S.C. 85 includes any payment compensating a creditor or prospective creditor for an extension of credit, making available of a line of credit, or any default or breach by a borrower of a condition upon which credit was extended. It includes, among other things, the following fees connected with credit extension or availability: numerical periodic rates, late fees, not sufficient funds (NSF) fees, overlimit fees, annual fees, cash advance fees, and membership fees. It does not ordinarily include appraisal fees, premiums and commissions attributable to insurance guaranteeing repayment of any extension of credit, finders' fees, fees for document preparation or notarization, or fees incurred to obtain credit reports.

61 Fed. Reg. 4849, 4869 (1996) (to be codified at 12 CFR § 7.4001(a)).

7. 116 S. Ct. at 1732.

8. The OCC Ruling further provides:

> (b) *Authority.* A national bank located in a state may charge interest at the maximum rate permitted to any state-chartered or licensed lending institution by the law of that state. If state law permits different interest charges on specified classes of loans, a national bank making such loans is subject only to the provisions of state law relating to that class of loans that are material to the determination of the permitted interest. For example, a national bank may lawfully

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Supreme Court endorsed as "reasonable" the OCC's interpretation of the term "interest" in section 85.[9] This principle applies to all types of loans, consumer or commercial,[10] closed-end or open-end, secured or unsecured, made by national banks.

A contentious issue throughout the fee exportation litigation was whether the term "interest" in section 85 is defined by federal law or the law of the state where the bank is located. The Supreme Court's deference to the OCC's definition also establishes that federal law controls in this instance. Accordingly, "interest" under section 85 includes "any payment compensating a creditor or prospective creditor for an extension of credit, making available of a line of credit, or any default or breach by a borrower of a condition upon which credit was extended," including without limitation "numerical periodic rates, late fees, not sufficient funds (NSF) fees, overlimit fees, annual fees, cash advance fees, and membership fees.[11] The term, however, "does not ordinarily include appraisal fees, premiums and commissions attributable to insurance guaranteeing repayment of any extension of credit, finders' fees, fees for document preparation or notarization, or fees incurred to obtain credit reports."[12] The Supreme Court characterized non-"interest" charges as encompassing "reimbursement for the lender's costs in processing the application, insuring the loan, and appraising the collateral."[13] The Court distinguished non-"interest" charges—"those charges that are specifically assigned to" the lender's expenses listed above—from "interest" charges—"those that are assessed for simply making the loan, or for the borrower's default."[14]

Although this federal definition of "interest" is broad, it is not as expansive as the definition propounded by many of the states to which bank credit card operations have migrated since the early 1980s. For instance, in addition to a number of other specifically enumerated fees, the Bank Revolving Credit subchapter of the Delaware Banking Code treats as "interest":

> [r]easonable fees for services rendered or for reimbursement of expenses incurred in good faith by the bank or its agents in connection with the plan, or other reasonable fees incident to the application for and the opening, administration and termination of a plan including, without limitation, commitment, application and processing fees, official fees and taxes, costs incurred by reason of examination of title, inspection, appraisal, recording, mortgage satisfaction or other formal acts necessary or appropriate to the security for the plan, and filing fees.[15]

Similarly, the Illinois Financial Services Development Act, which governs "revolving credit plans"[16] by, *inter alia*, in-state banks,[17] authorizes as "interest," among other fees, "fees for services rendered."[18] The Nevada Debt Evidenced by Credit Card statute defines "interest" to include "[a]ny other charge or fee [besides those specifically listed] to which the issuer and cardholder agree."[19] Moreover, the Ohio Banking statute authorizes a "bank"[20] to charge, collect, and receive as "interest," in addition to periodic interest, "other fees and charges that are agreed upon by the bank and the borrower."[21] Finally, the South Dakota Banking statutes permit a "bank"[22] to contract for and collect as "interest," in addition to certain enumerated charges, "[o]ther charges made in connection with the revolving loan or charge account arrangement."[23] Thus, national banks located in these and other states having similarly expansive definitions of "interest" seemingly would have preferred a home state definition of "interest" to that provided in the OCC Ruling.

In any event, the OCC Ruling incorporates a national bank's home state's law to determine the rate and amount of "interest" that the bank may impose (and export on its interstate loans). The OCC Ruling provides that (i) "[a] national bank located in a state may charge interest at the maximum rate permitted to any state-chartered or licensed lending institution by the law of that state"[24] and (ii) if the most favored lender in a state where a national bank is located may charge a fee that is "interest" under the OCC Ruling, the bank may charge the fee to its interstate customers whether or not the

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> charge the highest rate permitted to be charged by a state-licensed small loan company, without being so licensed, but subject to state law limitations on the size of loans made by small loan companies.
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> (c) *Effect on state definitions of interest.* The Federal definition of the term "interest" in paragraph (a) of this section does not change how interest is defined by the individual states (nor how the state definition of interest is used) solely for purposes of state law. For example, if late fees are not "interest" under state law where a national bank is located but state law permits its most favored lender to charge late fees, then a national bank located in that state may charge late fees to its intrastate customers. The national bank may also charge late fees to its interstate customers because the fees are interest under the Federal definition of interest and an allowable charge under state law where the national bank is located. However, the late fees would not be treated as interest for purposes of evaluating compliance with state usury limitations because state law excludes late fees when calculating the maximum interest that lending institutions may charge under those limitations.

61 Fed. Reg. 4849, 4869 (1996) (to be codified at 12 CFR §§ 7.4001(b), (c)).

9. 116 S. Ct. at 1735.

10. Subsection (d) of the OCC Ruling provides that "[a] national bank located in a state the law of which denies the defense of usury to a corporate borrower may charge a corporate borrower any rate of interest agreed upon by a corporate borrower." 61 Fed. Reg. 4849, 4869 (1996) (to be codified at 12 CFR § 7.4001(d)).

11. *Id.* (to be codified at 12 CFR § 7.4001(a).

12. *Id.*

13. 116 S. Ct. at 1734.

14. *Id.*

15. Del. Code Ann. tit. 5, § 945(a)(4), *redesignated by* 1996 Del. Laws ch. 327, § 26 (effective May 2, 1996).

16. 205 ILCS 675/3(b) (Supp. 1996).

17. *Id.* 675/3(a).

18. *Id.* 675/6 (1993).

19. Nev. Rev. Stat. Ann. § 97A.090(2)(e) (Michie Cum. Supp. 1995).

20. Ohio Rev. Code Ann. § 1101.01(B), *as amended by* 1995 Ohio Am. Sub. H.B. 538, § 1 (effective Jan. 1, 1997).

21. 1995 Ohio Am. Sub. H.B. 538, § 1 (to be codified at Ohio Rev. Code § 1109.20) (effective Jan. 1, 1997).

22. S.D. Codified Laws Ann. § 51A-1-2(1) (Supp. 1996).

23. *Id.* § 51A-12-13 (1990).

24. 61 Fed. Reg. 4849, 4869 (1996) (to be codified at 12 CFR § 7.4001(b)).

fee is "interest" under state law, because the fee is "interest" under the federal definition.[25] Consequently, if the law of the state where a national bank is located permits a fee that is "interest" under the OCC Ruling, the bank may export the fee in an amount permitted under that state's law. While this principle is clear, as discussed in Part II.C of this article, the scope of the incorporation of home state law in section 85 remains unresolved to a significant extent.

B. The Supreme Court Will Defer to the OCC's Interpretations of Ambiguous Provisions of the National Bank Act, If the OCC's Interpretation is Formal, "Reasonable," and Directed to National Banks Generally

In an important reaffirmation of the principle of judicial deference to administrative agency interpretations of statutes that they are charged with administering, the *Smiley* Court deferred to the OCC's interpretation of the meaning of the term "interest" in section 85.[26] Following upon the heels of the Supreme Court's decision in *NationsBank of North Carolina, N.A. v. Variable Annuity Life Insurance Co.*[27] deferring to the Comptroller of the Currency's (Comptroller) determinations that national banks may serve as agents in the sale of annuities and that annuities are properly classified as investments, not "insurance" within the meaning of 12 U.S.C. section 92,[28] *Smiley* signifies that the Court will defer to the OCC's or the Comptroller's formal interpretations of the NBA, as long as those interpretations are reasonable.[29] Moreover, the Court clarified that a "reasonable" agency interpretation of a statute need not be the best interpretation.[30]

The Court in *Smiley* nonetheless appears to have limited the types of OCC or Comptroller interpretations to which courts should accord deference. In rejecting the cardholder's argument that the OCC Ruling was inconsistent with past Comptroller positions and therefore not entitled to deference, the Supreme Court characterized as insufficient "to establish a binding agency policy" (i) a 1964 Comptroller letter to the President's Committee on Consumer Interests because it was "too informal" and (ii) a 1988 opinion letter from the Deputy Chief Counsel of the OCC, because it only purported to represent the Deputy Chief Counsel's position "in response to an inquiry concerning particular banks."[31] As many, if not most, OCC interpretive letters are issued in response to inquiries concerning particular banks, the Court has left in question the extent to which national banks—indeed all federally-regulated financial institutions—may rely upon such narrowly-directed interpretations by their federal supervisory agency. After *Smiley*, in order to ensure deference to their interpretations, the OCC and the other federal bank regulatory agencies may be required to address interpretive letters or any other interpretations in the name of the agency or its chief official and to all institutions that it regulates.

In this regard, before issuing any opinion letter or interpretive rule (such as the OCC Ruling), in response to a request or upon the agency's own motion, that concludes that federal law preempts the application to a national bank of any state law regarding, *inter alia*, consumer protection, the OCC is required to (i) publish in the Federal Register notice of the preemption issue that the OCC is considering (including a description of each state law at issue); (ii) give interested parties not less than 30 days in which to submit written comments; and (iii) in developing its final opinion letter or interpretive rule, consider any comments received.[32] This provision, however, does not apply with respect to any opinion letter or interpretive rule that (i) raises issues of federal preemption that are essentially identical to those previously resolved by the courts or on which the agency has previously issued an opinion letter or interpretive rule; or (ii) responds to a request that contains no significant legal basis on which to make a preemption determination.[33] The OCC followed neither all of the above requirements before issuing the OCC Ruling[34] nor any of these requirements before its Chief Counsel issued an interpretive letter in 1995 regarding the scope of the term "interest" under section 85.[35] The basis for this approach in the case of the OCC 1995 interpretive letter was that the question concerned whether the charges at issue constituted "interest" under section 85 and was not a determination that federal law preempts the application of state law to a national bank.[36] The foundation for this approach in the case of the OCC Ruling arguably was that, as in the case of the OCC 1995 interpretive letter, only the definition of "interest" and the most favored lender status of national banks under section 85, not preemption of state law, was at issue.

The Supreme Court, in deferring to the OCC Ruling, adopted this distinction between the meaning of the term "interest" under and the preemptive scope of section 85. The cardholder contended that no Comptroller interpretation of section 85 is entitled to deference because section 85 itself preempts state law. The Court disagreed, declaring that under *Marquette*, section 85 clearly preempts

25. *Id.* (to be codified at 12 CFR § 7.4001(c)).

26. 116 S. Ct. at 1733, 1735.

27. 115 S. Ct. 810 (1995).

28. *Id.* at 815-17.

29. *See* 116 S. Ct. at 1733, 1735.

30. *Id.* at 1735.

31. *Id.* at 1734.

32. 12 U.S.C. § 43(a) (Supp. I 1995), *as added by* Riegle-Neal Interstate Banking and Branching Act of 1994, Pub. L. No. 103-328, § 114 (1994).

33. *Id.* § 43(c)(1).

34. *See* OCC Proposed Rule, Interpretive Rulings, 60 Fed. Reg. 11,925, 11,929 (1995).

35. OCC Interpretive Letter No. 670 from Julie L. Williams, Chief Counsel (Feb. 17, 1995), *reprinted in* [1994-1995 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,618 ("Williams 1995 OCC Letter").

36. *Id.* n.1.

state law, but that only the definition of "interest," which term "does not...deal with pre-emption," was at issue.[37] The effect of the Court's distinction is to elevate deference to an agency's interpretation of the substantive meaning of a statute above the "presumption against preemption" announced in *Cipollone v. Liggett Group, Inc.*[38] This is the case because in *Smiley*, the preemption clause of section 85, *i.e.*, the phrase "the rate allowed by the laws of the State...where the bank is located," was not at issue, already having been found to preempt state law in *Marquette*.[39] Nonetheless, the Court's decision to defer to the OCC Ruling has the effect of significantly expanding the preemptive scope of section 85. Thus, where a federal agency interpretation of ambiguous statutory language not including the preemption clause is reasonable, the Court indicates in *Smiley* that it will defer to the agency's interpretation, even if deference will greatly extend the preemptive reach of the statute.

II. Certain Issues Not Resolved by *Smiley*

A. Scope of Fee Exportation by State-Chartered Banks and Federally and State-Chartered Savings Associations

Given that the *Smiley* decision is based upon the Supreme Court's deference to the OCC's interpretation of section 85, it is not dispositive as to whether federally-insured state-chartered banks and federally-chartered and federally-insured state-chartered savings associations may export late fees and other loan fees. There are nonetheless several grounds for concluding that the fee exportation rights of these institutions should be equivalent to those of national banks. First, one week after its decision in *Smiley*, the Supreme Court vacated the New Jersey Supreme Court's decision in *Hunter v. Greenwood Trust Co.*[40] holding that section 521 of the Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDA)[41] did not preempt New Jersey's credit card late fee limitations in the case of federally-insured state banks. Upon remand for reconsideration in light of *Smiley*, the New Jersey Supreme Court reinstated the decision of the state's Appellate Division upholding preemption of the New Jersey limitations.[42] Thus, the only lower court to interpret *Smiley* has concluded that state-chartered banks possess the same fee exportation rights as national banks, at least concerning late fees.

Second, both the Federal Deposit Insurance Corporation (FDIC)[43] and the Office of Thrift Supervision (OTS)[44] have issued interpretations (the more recent OTS interpretation consists of an interpretive ruling on most favored lender usury preemption (the OTS Most Favored Lender Ruling)[45]) providing that federally-insured state banks and federally-insured savings associations, respectively, may export the same fees on credit card loans as national banks. Indeed, the OTS Most Favored Lender Ruling contains a definition of "interest"[45] under section 4(g) of the Home Owners' Loan Act of 1993[46] that is iden-

37. 116 S. Ct. at 1735.

38. 505 U.S. 504, 518 (1992).

39. 439 U.S. at 313-19.

40. 143 N.J. 97, 668 A.2d 1067 (1995), *vacated and remanded*, 116 S. Ct. 2493 (1996), *rev'd on remand*, 146 N.J. 65, 679 A.2d 653 (1996).

41. Pub. L. No. 96-221, § 521 (Mar. 31, 1980) (codified at 12 U.S.C. § 1831d (1994)). Section 521 of the DIDA provides in pertinent part:

> In order to prevent discrimination against State-chartered insured depository institutions, including insured 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 where the bank is located, whichever may be greater.

Id. § 1831d(a).

42. Hunter v. Greenwood Trust Co., 146 N.J. 65, 679 A.2d 653 (1996), *reinstating* 272 N.J. Super. 526, 640 A.2d 855 (1994).

43. FDIC Letter No. 92-47 from Douglas H. Jones, Dep. Gen. Counsel (July 8, 1992), *reprinted in* [1992-1993 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,534 ("Jones 1992 FDIC Letter").

44. OTS Final Rule on Most Favored Lender Usury Preemption, 61 Fed. Reg. 50,951, 50,967-68 & n.63, 50,981 (1996) (to be codified at 12 C.F.R. § 560.110) (effective Oct. 30, 1996); OTS Op. 94/CC-18 from Karen Solomon, Dep. Chief Counsel (Sept. 29, 1994), *reprinted in* [1994-1995 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 82,852 (attaching Federal Home Loan Bank Board (predecessor to OTS) Interpretive Letter from Harry W. Quillian (June 27, 1986)).

45. The OTS Most Favored Lender Ruling provides:

> (a) *Definition.* The term "interest" as used in 12 U.S.C. 1463(g) includes any payment compensating a creditor or prospective creditor for an extension of credit, making available of a line of credit, or any default or breach by a borrower of a condition upon which credit was extended. It includes, among other things, the following fees connected with credit extension or availability: numerical periodic rates, late fees, not sufficient funds (NSF) fees, overlimit fees, annual fees, cash advance fees, and membership fees. It does not ordinarily include appraisal fees, premiums and commissions attributable to insurance guaranteeing repayment of any extension of credit, finders' fees, fees for document preparation or notarization, or fees incurred to obtain credit reports.
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> (b) *Authority.* A savings association located in a state may charge interest at the maximum rate permitted to any state-chartered or licensed lending institution by the law of that state. If state law permits different interest charges on specified classes of loans, a federal savings association making such loans is subject only to the provisions of state law relating to that class of loans that are material to the determination of the permitted interest. For example, a federal savings association may lawfully charge the highest rate permitted to be charged by a state-licensed small loan company, without being so licensed, but subject to state law limitations on the size of loans made by small loan companies. Except as provided in this paragraph, the applicability of state law to Federal savings associations shall be determined in accordance with § 560.2 of this part. State supervisors determine the degree to which state-chartered savings associations must comply with state laws other than those imposing restrictions on interest, as defined in paragraph (a) of this section.
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> (c) *Effect on state definitions of interest.* The Federal definition of the term "interest" in paragraph (a) of this section does not change how interest is defined by the individual states (nor how the state definition of interest is used) solely for purposes of state law. For example, if late fees are not "interest" under state law where a savings association is located but state law permits its most favored lender to charge late fees, then a savings association located in that state may charge late fees to its intrastate customers. The savings association may also charge late fees to its interstate customers because the fees are interest under the Federal definition of interest and an allowable charge under state law where the savings association is located. However, the late fees would not be treated as interest for purposes of evaluating compliance with state usury limitations because state law excludes late fees when calculating the maximum interest that lending institutions may charge under those limitations.

61 Fed. Reg. 50,951, 50 981 (1996) (to be codified at 12 CFR § 560.110) (effective Oct. 30, 1996).

46. Pub. L. No. 101-73, § 301 (Aug. 9, 1989) (codified at 12 U.S.C. § 1463(g) (1994)). Section 4(g) of the HOLA provides in pertinent part:

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tical to that in the OCC Ruling and presumably would receive deference from the Supreme Court. Because the FDIC letter is not addressed to all institutions that the agency regulates and is issued neither by the head of the FDIC nor by the FDIC after notice and comment, however, it may not be entitled to deference under *Smiley*.[47] Conversely, because the FDIC has consistently interpreted section 521 of the DIDA to grant federally-insured state banks most favored lender status[48]—in effect, parity with national banks, deference appears more likely to be accorded than in the case of the OCC 1988 Deputy Chief Counsel opinion denied deference in *Smiley*.[49]

In any event, sections 521 and 4(g) should be interpreted to have the same meaning as section 85 with respect to the term "interest" because the operative language of all three provisions, *i.e.*, the authority to "charge interest at the rate allowed by the laws of the state where the institution is located," is virtually identical. Indeed, the Court of Appeals for the First Circuit in *Greenwood Trust Co. v. Massachusetts*[50] determined that "[t]he historical record clearly requires a court to read the parallel provisions of [the DIDA] and [section 85] *in pari materia*."[51] After *Smiley*, to heighten the likelihood of judicial deference to its position, the FDIC would be well advised to adopt an interpretive ruling concerning the definition of "interest" and most favored lender status under section 521 that is coextensive with the OCC Ruling. While the FDIC never has adopted such a formal interpretation, as noted above, the OTS has just adopted such an interpretive ruling with respect to usury preemption and most favored lender status.[52] Since *Smiley* was decided, the OTS has issued a final interpretive rule on Lending and Investment by federal savings associations[53] that provides for broader federal preemption of state "loan-related" fee limitations than that established in the OCC Ruling.[54] This greater preemption, however, is premised on section 5(a)[55] as well as section 4(g) of the HOLA. Section 5(a) of the HOLA grants the OTS plenary authority to regulate federal savings associations' lending practices,[56] an authority that has been interpreted more broadly[57] than that of the OCC under section 24(Seventh) of the NBA[58] to regulate national banks' lending activities.

B. Whether Certain Fees Are "Interest" Under the OCC Ruling

The OCC Ruling indicates that the OCC's list of fees that constitute "interest" is not intended to be exhaustive.[59] Accordingly, fees other than those listed may constitute "interest," as long as they are not among the fees not considered by the OCC to be "interest."[60] A number of credit card and other loan fees do not neatly fall into either category. For instance, attorneys' fees and collection costs are assessed because of "default or breach by a borrower of a condition upon which credit was extended," but they may not be a "payment compensating a creditor or prospective creditor" (as opposed to a third party) for nonpayment of a loan.[61] Similarly, loan application fees may compensate a creditor or prospective creditor for making a line of credit available, but the *Smiley* Court declared that charges assigned to reimbursement of the lender's costs in processing the application do not constitute "interest" under the OCC Ruling.[62] Among the other fees that may not be considered "interest" under section 85 are credit card replacement fees, copy fees, currency conversion fees, line of credit access check stop payment fees, security interest filing and release or termination fees, and other types of secured loan closing and post-closing costs and fees.

Finally, certain fees and charges that banks may have considered "interest" under sections 85, 521, and 4(g) appear not to constitute "interest" under the OCC

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> (g) Preemption of State usury laws
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> (1) Notwithstanding any State law, a savings association may charge interest on any extension of credit at a rate of not more than 1 percent in excess of the discount rate on 90-day commercial paper in effect at the Federal Reserve bank in the Federal Reserve district in which such savings association is located or at the rate allowed by the laws of the State in which such savings association is located, whichever is greater.

Id. § 1463(g)(1).

47. *Supra* note 31.

48. Jones 1992 FDIC Letter, *supra* note 43; FDIC Letter No. 83-16 from Peter M. Kravitz, Senior Att'y, to Peter D. Schellie (Oct. 20, 1983), *reprinted in* [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,013; FDIC Letter No. 81-7 from Kathy A. Johnson, Att'y, to Harvey Bock (Mar. 17, 1981), *reprinted in* [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,008.

49. *See* 116 S. Ct. at 1734-35.

50. 971 F.2d 818 (1st Cir. 1992), *cert. denied*, 506 U.S. 1052 (1993).

51. 971 F.2d at 827. Those "parallel provisions" include not only section 521 but also sections 522 (now section 4(g) of the HOLA) and 523 (regarding federally-chartered and federally-insured state-chartered credit unions). *See* 12 U.S.C. §§ 1463(g), 1785(g), 1831d (1994). *See also* Part II.D of this article *infra* (regarding applicability of opt-out provision of DIDA).

52. 61 Fed. Reg. 50,951, 50,981 (1995) (to be codified at 12 CFR § 560.110) (effective Oct. 30, 1996).

53. 61 Fed. Reg. 50,951 (1996) (effective Oct. 30, 1996).

54. *Id.* at 50,972 (to be codified at 12 CFR § 560.2(b)) (effective Oct. 30, 1996). The rule also preempts state law limitations or requirements concerning disclosures, disbursements and repayments, and usury and interest rate ceilings to the extent provided in 12 U.S.C. § 1735f-7(a) and 12 CFR Part 590 (regarding first lien real estate loans) and 12 U.S.C. § 1463(g) and newly-promulgated 12 CFR § 560.110 (regarding exportation and most favored lender rights). 61 Fed. Reg. 50,951, 50,972 (to be codified at 12 CFR § 560.2(b)) (effective Oct. 30, 1996).

55. 12 U.S.C. § 1464(a) (1994).

56. *Id.*; *see* Fidelity Fed. Sav. & Loan Ass'n v. de la Cuesta, 458 U.S. 141 (1982).

57. *See id.*; OTS Final Rule, 61 Fed. Reg. 50,951, 50,965-67 (1996).

58. 12 U.S.C. § 24(Seventh) (1994).

59. The OCC Ruling provides that "interest" under section 85 includes, "among other things," certain enumerated fees. 61 Fed. Reg. 4849, 4869 (1996) (to be codified at 12 CFR § 7.4001(a)). The OTS Most Favored Lender Ruling contains identical language. *See supra* note 45.

60. *Supra* text accompanying note 12. Since the *Smiley* decision, the OCC has opined in an interpretive letter that prepayment fees or penalties levied by a national bank on home equity loans constitute "interest" under 12 U.S.C. § 85 because, *inter alia*, the fees represent "compensation to the bank, in the form of an alternative to higher finance charges, for the risk that an extension of credit will be repaid prior to the maturity date on which the interest rate was predicated." OCC Interpretive Letter from Julie L. Williams, Chief Counsel (Aug. 21, 1996).

61. *See* OCC Ruling, 61 Fed. Reg. 4849, 4869 (1996) (to be codified at 12 CFR § 7.4001(a)).

62. 116 S. Ct. at 1734.

Ruling. These charges fall into two categories. First, because "premiums and commissions attributable to insurance guaranteeing repayment of any extension of credit" are not "interest" in the OCC's view,[63] credit insurance charges, real estate mortgage insurance premiums, and other fees paid to third parties who guarantee or insure repayment of loans if the borrower should default likely are not "interest" under section 85. Second, "finders' fees" also do not constitute "interest" under the OCC Ruling.[64] Consequently, mortgage broker and other loan broker fees denominated as such likely are not "interest" under section 85. The effect of classifying these two types of charges as non-"interest" charges may be to encourage banks to impose larger loan origination or cash advance fees (which are likely or certain, respectively, to be characterized as "interest" under section 85) or higher periodic interest rates in lieu of such non-"interest" charges.

C. Scope of Incorporation of a National Bank's Home State's Law in Section 85: What Provisions Are "Material to the Determination of the Permitted Interest" and Are Those Provisions Exportable?

The courts and the OCC staff have differed as to whether the state law incorporated in section 85 encompasses only the numerical "rate" of interest,[65] the method of calculating the rate as well,[66] or even the entire case law interpreting limitations on usury,[67] including common law conflict of laws rules.[68] Even the Supreme Court has been unable to agree on the scope of incorporation of a national bank's home state's law in section 85.[69] Unfortunately, the OCC Ruling does not resolve the extent of this incorporation, merely providing that home state law determines the "rate" and amount of interest that a national bank may impose, and federal law determines what constitutes "interest."[70]

The courts and the OCC staff have determined on numerous occasions that laws of a national bank's home state that establish the manner in which the rate of interest is calculated apply under section 85 in intrastate loans.[71] In effect, these cases or interpretive letters have concluded that, in the language of the OCC Ruling, these statutory provisions are "material to the determination of the permitted interest."[72] Among the provisions that have been found to be "material" are prohibitions or restrictions against compounding interest,[73] authorizations to vary and restrictions on the variation of the rate,[74] and restrictions on day-count methods.[75] Neither the courts nor the OCC, however, have addressed whether other provisions that restrict the amount or the timing of collection of interest are "material." Thus, there is no guidance regarding the "materiality" of such terms as balance calculation methods, the grace period for repayment of account balances, grace periods and notice requirements for assessment of late fees and returned check fees, and (except insofar as the OCC staff letters on variable rate authority are deemed applicable to changes in fixed "interest" terms) restrictions on the timing (*e.g.*, effective dates and retroactive effect) of changes in terms.

Because national banks—and other financial institutions with fee exportation rights—may in the wake of *Smiley* seek to increase the dollar or percentage amounts of fees that they have been imposing or impose new fees, the question of whether and to what extent they must comply with state change-of-terms notice requirements and restrictions has become particularly important. If such an institution has included a governing law provision in its open-end credit agreements selecting its home state's law (and federal law) or if change-of-terms requirements are "material,"[76] then the institution must comply with any such home

63. *See supra* note 61.

64. *Id.*

65. Evans v. Nat'l Bank, 251 U.S. 108, 111 (1919). *See* Nat'l Bank v. Johnson, 104 U.S. 271, 277-78 (1881); Farmers' & Mechanics' Nat'l Bank v. Dearing, 91 U.S. 29, 34 (1875).

66. This includes all prohibitions on enlarging the rate, even if the resulting charge is within the 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).

67. First Nat'l Bank v. Nowlin, 509 F.2d 872, 876 (8th Cir. 1975). *See* Union Nat'l Bank v. Louisville, N.A. & C. Ry., 163 U.S. 325, 331 (1896); OCC Interpretive Letter No. 452 from Robert B. Serino, Dep. Chief Counsel (Policy) (Aug. 11, 1988), *reprinted in* [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,676 ("Serino 1988 OCC Letter").

68. OCC Interpretive Letter No. 325 from Peter Liebesman, Asst. Dir., Legal Advisory Servs. Div. (Jan. 22, 1985), *reprinted in* [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,495, at 77,754. *See* Hershel Shanks, *Special Usury Problems Applicable to National Banks*, 87 Banking L.J. 483, 489-91 (1970). *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).

69. *See supra* notes 65-67.

70. *See supra* text accompanying notes 24-25; *supra* note 8; Williams 1995 OCC Letter, *supra* note 35, at 71,834 n.3.

71. *See* Jeffrey I. Langer and Jeffrey B. Wood, *A Comparison of the Most Favored Lender and Exportation Rights of National Banks, FSLIC-Insured Savings Institutions, and FDIC-Insured State Banks*, 42 Consumer Fin. L.Q. Rep. 4, 12 (1988) ("*Langer and Wood*"). *See generally* OCC Interpretive Letter from Peter C. Liebesman, Asst. Dir., Legal Advisory Servs. Div. (Feb. 4, 1983), 1983 WL 145788 (O.C.C.) ("Liebesman 1983 OCC Letter").

72. 61 Fed. Reg. 4849, 4869 (1996) (to be codified at 12 CFR § 7.4001(b)).

73. *Donnell*, 195 U.S. at 373-74; Haas v. Pittsburgh Nat'l Bank, 526 F.2d 1083, 1094-95 (3d Cir. 1975); Acker v. Provident Nat'l Bank, 512 F.2d 729, 740-42 (3d Cir. 1975); Partain v. First Nat'l Bank, 467 F.2d 167, 173-78 (5th Cir. 1972). *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).

74. OCC Interpretive Letter No. 354 from Roberta W. Boylan, Dir., Legal Advisory Servs. Div. (Nov. 18, 1985), *reprinted in* [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,524 ("Boylan 1985 OCC Letter") (equates variable rate lending authority with absence of restrictions on frequency of rate changes, but locates "no judicial pronouncements on point"); OCC Interpretive Letter No. 333 from Charles F. Byrd, Asst. Dir., Legal Advisory Servs. Div. (Mar. 20, 1985) *reprinted in* [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,503, at 77,785 ("Byrd 1985 OCC Letter") ("material" restrictions include annual and life-of-loan interest rate caps, restrictions on frequency of interest rate changes, and restrictions on permissible index).

75. American Timber & Trading Co. v. First Nat'l Bank, 511 F.2d 980, 983-85 (7th Cir. 1973), *cert. denied*, 421 U.S. 921 (1974); Voitier v. First Nat'l Bank, 514 F. Supp. 585, 594 (E.D. La. 1981).

76. The OTS Most Favored Lender Ruling adopts the OCC Ruling's "materiality" test with respect to federal savings associations. In the case of state-chartered savings associations, this ruling provides that "[s]tate supervisors determine the degree to which [such] associations must comply with state laws other than those imposing restrictions on interest, as defined in [the ruling]." 61 Fed. Reg. 50,951, 50,981 (1996) (to be codified at 12 CFR § 560.110(b)) (effective Oct. 30, 1996). With respect to national banks, the "federal instrumentality" doctrine also may make home state law applicable. *See infra* text accompanying notes 84-85. With respect to federally-insured state banks, the "materiality" test has been applied. *See, e.g., Equitable Trust*, 294 Md. 385, 450 A.2d 1273.

state requirements. Moreover, the loan agreement may impose restrictions on the institution's authority to change terms. To the extent that the borrower's state's law impedes the bank's or thrift's ability to charge "interest" under federal law to a greater extent than either the contractual governing law or the contractual change-of-terms provision, it can be argued that the borrower state change-of-terms restriction should be preempted. Of course, if the contract allows unilateral changes of terms without restriction, under common law principles, there is no enforceable agreement either at inception or for the new terms.[77] National banks and other "exporting" lenders should review their loan contracts and manner of changing terms to assess the enforceability and preemptive scope of their change-of-terms structures.

In its recently-promulgated interpretive rulings that included the OCC Ruling, the OCC has delineated a final set of terms that may be "material to the determination of the permitted interest": non-"interest" charges and fees.[78] OCC Interpretive Rule 7.4002 declares that "[a] national bank may charge its customers non-interest charges and fees, including...reasonable fees for credit reports or investigations with respect to a borrower's credit."[79] These fees may be merely illustrative of non-"interest" fees that a national bank may impose; accordingly, all non-"interest" fees may be subject to Interpretive Rule 7.4002. This rule requires that such fees (i) "be arrived at by each bank on a competitive basis and not on the basis of any agreement, arrangement, undertaking, understanding, or discussion with other banks"[80] and (ii) be reasonably established.[81] To "reasonably establish" such fees, a national bank must consider these factors, among others: (a) the cost incurred by the bank, plus a profit margin, in providing the service; (b) the deterrence of misuse by customers of banking services; (c) the enhancement of the bank's competitive position in accordance with its marketing strategy; and (d) the maintenance of the bank's safety and soundness.[82]

These fees may be "material" on the bases that they are permitted by a national bank's home state's law and the legislature presumably considered the amounts of such fees when it determined permissible "interest" charges. Even if non-"interest" fees are not "material," Interpretive Rule 7.4002 provides that the OCC may preempt contrary state law limitations on such fees on a case-by-case basis. In making such determinations, the OCC is to apply "preemption principles derived from the Supremacy Clause ofthe United States Constitution and applicable judicial precedent."[83] In the case of national banks, one of these principles consists of the "federal instrumentality" doctrine: national banks are subject to state law except to the extent that such law conflicts with or frustrates the purpose of federal legislation (*i.e.*, the NBA) or disrupts the banks in the performance of their duties as federal instrumentalities.[84] The federal instrumentality doctrine appears to operate independently of the OCC Ruling's "materiality" standard to make national banks subject to additional non-"material" provisions of home state *and* borrower state laws.[85] If the bank's loan agreements select its home state's law as the governing law, the bank in any case will have to comply with all applicable provisions of such law.

There are several provisions of state law that have been found not to be material to the determination of the rate of interest that a national bank may impose. In the leading case on "materiality," *Attorney General v. Equitable Trust Co.*,[86] Maryland's highest court[87] ruled that a provision that subjected the lender to the borrower's claims and defenses against a seller of goods was not "material." Additionally, on two occasions the OCC staff has concluded that state disclosure requirements are not "material."[88]

The OCC Ruling also fails to state whether or not "material" terms are exportable in addition to "interest." Construing former OCC Interpretive Rule

77. *See* RESTATEMENT (SECOND) OF CONTRACTS §§ 1, 22, 33-34 (1979).

78. 61 Fed. Reg. 4849, 4869-70 (1996) (to be codified at 12 CFR § 7.4002) provides in pertinent part:

> (a) *Customer charges and fees.* A national bank may charge its customers non-interest charges and fees, including deposit account service charges. For example, a national bank may impose deposit account service charges that its board of directors determines to be reasonable on dormant accounts. A national bank may also charge a borrower reasonable fees for credit reports or investigations with respect to a borrower's credit. All charges and fees should be arrived at by each bank on a competitive basis and not on the basis of any agreement, arrangement, undertaking, understanding, or discussion with other banks or their officers.
>
> (b) *Considerations.* The establishment of non-interest charges and fees, and the amounts thereof, is a business decision to be made by each bank, in its discretion, according to sound banking judgment and safe and sound banking principles. A bank reasonably establishes non-interest charges and fees if the bank considers the following factors, among others:
>
> (1) The cost incurred by the bank, plus a profit margin, in providing the service;
>
> (2) The deterrence of misuse by customers of banking services;
>
> (3) The enhancement of the competitive position of the bank in accordance with the bank's marketing strategy; and
>
> *(Continued in next column)*

78. *(Continued from previous column)*

> (4) The maintenance of the safety and soundness of the institution.
>
> (c) *Interest.* Charges and fees that are "interest" within the meaning of 12 U.S.C. § 85 are governed by § 7.4001 and not by this section.
>
> (d) *State law.* The OCC evaluates on a case-by-case basis whether a national bank may establish non-interest charges or fees pursuant to paragraphs (a) and (b) of this section notwithstanding a contrary state law that purports to limit or prohibit such charges or fees. In issuing an opinion on whether such state laws are preempted, the OCC applies preemption principles derived from the Supremacy Clause of the United States Constitution and applicable judicial precedent.

Id. (to be codified at 12 CFR § 7.4002(a)-(d)).

79. *Id.* (to be codified at 12 CFR § 7.4002(a)).

80. *Id.*

81. *Id.* (to be codified at 12 CFR § 7.4002(b)).

82. *Id.*

83. *Id.* (to be codified at 12 C.F.R. § 7.4002(d)).

84. *See* Anderson Nat'l Bank v. Luckett, 321 U.S. 288 (1944); First Nat'l Bank v. Missouri, 263 U.S. 640, 656 (1924); Davis v. Elmira Savings Bank, 161 U.S. 275 (1896).

85. *See Langer and Wood*, *supra* note 71, at 9.

86. 294 Md. 385, 450 A.2d 1273 (1982).

87. The Court of Appeals.

88. Byrd 1985 OCC Letter, *supra* note 74 (notes that, based on federal instrumentality doctrine, in absence of federal statute or regulation, national banks remain subject to law applicable to them, including disclosure requirements); OCC Interpretive Letter No. 178 from Richard V. Fitzgerald, Dir., Legal Advisory Servs. Div. (Jan. 12, 1981), *reprinted in* [1981-1982 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,259.

7.7310,[89] the interpretive rule on most favored lender status supplanted by the OCC Ruling, the OCC staff declared in several interpretive letters that "material" provisions are exportable.[90] A strong argument can be made that at least those provisions of a national bank's home state's law that determine the "rate" or amount of "interest" that the bank may impose should be exportable. The courts should consider the calculation of the permitted interest to be so intimately bound up with the "rate" of "interest" as to be exportable with the "rate" itself.

D. Effect of Opt-Out Under Section 525 of DIDA on Exportation by State-Chartered Banks and Federally and State-Chartered Savings Associations

When Congress enacted sections 521 and 522 (now section 4(g) of the HOLA) of the DIDA, it also enacted section 525 permitting the voters or legislature of any state to determine explicitly that DIDA's usury preemption provisions would not apply "with respect to loans made in such" state.[91] No such opt-out provision exists with respect to national banks. Seven states and Puerto Rico opted out of DIDA section 521 and 522 preemption, but five states have since repealed their opt-out provisions, leaving Iowa and Wisconsin, along with Puerto Rico, as the only remaining opt-out states.[92] Moreover, Wisconsin recently enacted legislation, *inter alia*, (i) repealing the provisions of its Consumer Act limiting the rate of finance charge on open-end credit plans; (ii) authorizing the parties to agree to the customer's payment of a finance charge on such plans at any periodic rate; (iii) effective February 1, 1997, repealing limitations on minimum finance charges, delinquency charges, cash advance fees, overlimit fees, and dishonored instrument charges under such plans; and (iv) effective February 1, 1997, authorizing a creditor to impose other fees in addition to finance charges, including periodic membership fees, late payment fees, cash advance fees, dishonored instrument charges, and document charges, as agreed upon by the creditor and customer.[93] Iowa and Puerto Rico thus represent the only remaining jurisdictions where an opt-out provision may actually limit interest rates and frequently-imposed fees on open-end credit plans. In this regard, Iowa's Consumer Credit Code purports to have extraterritorial effect, providing that an open-end credit transaction is "entered into in" Iowa if the debtor is a resident of Iowa at the time the debtor gives to the creditor a written or oral communication of his intention to establish the transaction.[94]

Congress in any case may have repealed section 525 of the DIDA, at least with respect to federally-insured savings associations. Section 522 was enacted as section 414 of the National Housing Act (NHA).[95] In section 407 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA), Congress repealed Title 4 of the NHA, including section 414.[96] While section 522 essentially was re-enacted in section 301 of the FIRREA as section 4(g) of the HOLA, no provision of the FIRREA replaced the reference in section 525 to section 522 with a reference to section 4(g). Accordingly, insured savings associations may assert that effective upon the enactment of the FIRREA on August 9, 1989, state opt-out authority under section 525 no longer applies to their extensions of credit.[97]

Additionally, in a case involving an FDIC-insured state-chartered bank, a Colorado court of appeals determined that on the FIRREA's effective date, Congress repealed section 525.[98] Moreover, even if Colorado's repealed opt-out provision remained in effect, the court concluded that such opt-out was ineffective with respect to the loans at issue because Colorado could only opt out as to loans "made in" Colorado and the bank involved was located in Delaware.[99] Although the court did not examine the issue, the Colorado Consumer Credit Code does not consider credit card loans made by out-of-state lenders to Colorado residents to be "made in" Colorado.[100]

In sum, pending more definitive analysis by the courts, it is uncertain (i) whether and to what extent Congress repealed section 525 and (ii) whether a borrower's state's opt-out provision overrides an out-of-state bank's ability to export "interest" on loans to opt-out state residents.

89. 12 CFR § 7.7310(1996), *repealed and replaced by* 61 Fed. Reg. 4849, 4869 (1996) (to be codified at 12 CFR § 7.4001).

90. *See, e.g.*, Serino 1988 OCC Letter, *supra* note 67; Boylan 1985 OCC Letter, *supra* note 74; Liebesman 1983 OCC Letter, *supra* note 71.

91. Section 525 of the DIDA provides:

> The amendments made by section [sic] 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. No. 96-221, § 525 (Mar. 31, 1980) (codified at 12 U.S.C. § 1831d note (1994)).

92. The opt-out states and actions repealing those opt outs are as follows: Colorado (Colo. Rev. Stat. § 5-13-104 (1992); repealed in 1994 Colo. Sess. Laws ch. 272, § 12); Iowa (1980 Iowa Acts ch. 1156, § 32 (not codified)); Maine (Me. Rev. Stat. Ann. tit. 9-A, § 1-110 (West 1994 Supp.); repealed in 1995 Me. Laws ch. 137, §§ 1, 3); Massachusetts (1981 Mass. Acts ch. 231, § 2 (codified at Mass. Gen. Laws Ann. ch. 183, § 63); repealed in 1986 Mass. Acts ch. 177); Nebraska (Neb. Rev. Stat. § 45-1,104 (1987); repealed by amendment in 1988 Neb. Laws 913); North Carolina (N.C. Gen. Stat. § 24-2.3 (1986); repealed in 1995 N.C. Sess. Laws ch. 387, § 1); Wisconsin (1981 Wis. Laws ch. 45, § 50 (not codified)); Puerto Rico (P.R. Laws Ann. tit. 10, § 9981(c) (Michie 1976)).

93. 1996 Wis. Laws 328, §§ 3-7s (effective May 17, 1996) (to be codified at Wis. Stat. Ann. §§ 421.201(10s), 422.202(2m)(a), (b)(intro.), (c)).

94. Iowa Code § 537.1201(2)(b)(1) (West 1987).

95. *See* Pub. L. No. 96-221, § 522 (Mar. 31, 1980).

96. Pub. L. No. 101-73, § 407 (Aug. 9, 1989).

97. *See* Jeffrey I. Langer, *FIRREA Removes Opt-Out Limitation on Interest Rate Exportation by Insured Savings Associations*, 44 Consumer Fin. L.Q. Rep. 213, 214 (1990).

98. Stoorman v. Greenwood Trust Co., 888 P.2d 289 (Colo. App. 1994), *aff'd on other grounds*, 908 P.2d 133 (Colo. 1995), *cert. denied*, 116 S. Ct. 2498 (1996).

99. *Id.*

100. *See* Colo. Rev. Stat. § 5-1-201(3), (11) (West 1996).

E. "Location" of an Exporting Institution When the Institution Has Contacts with or Branches in a State Where It is Not Chartered

Section 85 and the other federal usury preemption provisions permit national banks and other federally-insured financial institutions to charge "interest" at the "rate allowed by the laws of the state [where the institution] is *located*."[101] The location of such an institution therefore serves as an important factor in determining the scope of its exportation authority. *Smiley* did not address the location of the exporting bank in the case.

In the absence of definitive guidance from the Supreme Court,[102] it remains uncertain as to where a federally-insured financial institution is "located" for purposes of the relevant federal usury preemption provision in certain circumstances. In *Marquette*, the Supreme Court initially found that a national bank's address set forth in its charter or organization certificate determined its "location" under section 85 because at that time a national bank was not permitted to extend credit from any location other than its charter address or a legal branch in the charter state.[102] The petitioner contended that despite the respondent bank's charter address in Nebraska, the bank was located in Minnesota because of various contacts with that state.[103] While the Court rejected a transaction-oriented analysis of where the bank and its credit card program were located, the Court did engage in a detailed analysis of the bank's and the program's contacts with each state, ultimately reiterating that the bank and the program were located in the charter state.[104] In its analysis, the Court focused on the following contacts, all of which occurred in the charter state: (i) where credit assessments were made; (ii) where credit cards were issued; (iii) where credit was extended by the honoring of sales drafts; (iv) where finance charges were assessed; and (v) where payments were received.[105] The Court did not consider the effect of such contacts occurring or authorized bank branches being established in multiple states.

Thus, when a national bank or other "exporting" institution has contacts with or branches in a state other than its charter state, the *Marquette* analysis is not controlling. The leading case concerning the "location" of a national bank under a loan program that has contacts with more than one state is *Cades v. H & R Block, Inc.*[106] In *Cades*, the Court of Appeals for the Fourth Circuit held that a national bank with offices only in Delaware was "located" in that state for section 85 purposes and could export Delaware-authorized interest rates despite the fact that an unaffiliated agent of the bank in South Carolina solicited, took, and processed the credit application and distributed the loan proceeds check to the borrower and the borrower signed the application and the loan agreement in South Carolina.[107] In *Wiseman v. State Bank & Trust, N.A.*,[108] Arkansas residents purchased a car at an Arkansas dealership where the salesman arranged for financing from an Oklahoma national bank. Rejecting the purchasers' usury claim, the Arkansas Supreme Court held that the bank was located in Oklahoma, not Arkansas.[109] The Court relied on the bank's Oklahoma charter address in the face of the plaintiffs' assertion that the ownership of a majority of the bank's stock by an Arkansas bank holding company mandated that the bank be deemed "located" in Arkansas.[110] These courts declined to deny national banks the benefit of their charter state's location, but none of the *Marquette* factors were implicated in the two cases.

The OCC staff also has concluded that a national bank remains "located" in its charter state where all of its offices are established, even when such lending bank's state-chartered bank affiliates in other states engage in the following loan origination and closing activities on its behalf: (i) soliciting, providing, assisting individuals in completing, accepting, and transmitting applications; and (ii) scheduling closing dates, preparing documents, obtaining necessary signatures, and delivering to borrowers line of credit access checks or other access devices on lines of credit.[111] The OCC's position is consistent with *Cades* and *Wiseman*, although there are two factual differences that could have led to a different result. Under the OCC letter, the agents were affiliated banks rather than unaffiliated sellers, and one of the *Marquette* contacts, issuance of access devices, was present.

Finally, the OCC and the OTS have addressed the location of an "exporting" institution when its main office and branch offices are situated in more than one state. The OCC's Chief Counsel recently opined that in determining the "location" of such a multistate national bank, the crucial element is the nexus between the loan and a branch in the state whose interest rates are being imposed.[112] The nexus, according to the Chief Counsel, consists of the place where application, loan closing, disbursement or initiation of disbursement of loan proceeds, and "booking" of the loan occur.[113] In the scenarios addressed in the letter, all of these

101. *See* 12 U.S.C. §§ 85, 1463(g)(1), 1831d(a) (1994) (emphasis added).

102. 439 U.S. at 309.

103. *Id.* at 310.

104. *Id.* at 310-13.

105. *Id.* at 311-12.

106. 43 F.3d 869 (4th Cir. 1994), *cert. denied*, 115 S. Ct. 2247 (1995).

107. 43 F.3d at 873-74.

108. 313 Ark. 289, 854 S.W.2d 725 (1993).

109. 313 Ark. at 291-94, 854 S.W.2d at 726-28.

110. 313 Ark. at 292-94, 854 S.W.2d at 727-28.

111. OCC Interpretive Letter No. 721 from Eric Thompson, Dir., Bank Activities and Structure Div. (Mar. 6, 1996), *reprinted in* [Current] Fed. Banking L. Rep. (CCH) ¶ 81-036.

112. OCC Interpretive Letter No. 707 from Julie L. Williams, Chief Counsel (Jan. 31, 1996), *reprinted in* [Current] Fed. Banking L. Rep. (CCH) ¶ 81-022 ("OCC Letter No. 707"). *See* OCC Interpretive Letter No. 686 from Julie L. Williams, Chief Counsel (Sept. 11, 1995), *reprinted in* [Current] Fed. Banking L. Rep. (CCH) ¶ 81-001 (national bank with Pennsylvania charter address and New Jersey branches may charge New Jersey borrowers the interest rates authorized for the "most favored lender" under New Jersey law, because (i) the loans would be originated and booked at New Jersey branches, (ii) the loan proceeds would be disbursed from the New Jersey branches, and (iii) most borrowers would be New Jersey residents).

113. *Id.*

contacts occurred in one state,[114] so the result is uncertain if contacts are present in two or more states. In 1992, the OTS's General Counsel concluded that a federal savings association is "located" in the state where its home office is situated, as well as any state where the association maintains a branch office.[115] In the case of loans originated from a branch, the General Counsel opined that the association may apply the most favored lender rates of either its home state, which always may be applied, or the state in which the branch is situated.[116] The OTS consequently has propounded a more expansive interpretation of a multistate insured institution's exportation rights than the OCC.

III. Conclusion

Smiley represents an important victory for national banks and other federally-insured financial institutions in their quest to establish uniform nationwide lending programs. Nonetheless, there remain numerous unanswered questions regarding the scope of these institutions' exportation and most favored lender rights and the extent to which they can rely on informal federal banking agency interpretations of the laws that these agencies are charged with enforcing.

114. OCC Letter No. 707, *supra* note 112.

115. OTS Gen. Counsel Op. 92/CC-59 (Dec. 24, 1992), *reprinted in* [1992-1993 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 82,645, at 62,006.

116. *Id.* at 62,007.

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be mounting. As noted *infra* there is evidence that overall portfolio losses for mortgage lenders have averaged nearly 10% during previous periods of economic stress. Obviously, overall losses of this magnitude would sink most banks and mortgage lenders, even with enhanced capital standards and levels.

All in all, 1997 appears likely to be an unusually interesting year. And if the past is prologue, it may be relevant to consider the comments of speakers describing the events of the past year at the 1996 Banking Law Institute.

Introducing John Podvin Jr., your author asserted that many in banking believe that 1996 was a quiet year for banking law and regulation. Mr. Podvin responded by describing more than 40 major 1996 legislative and regulatory developments, not counting EGRPRA, belying any perception that 1996 was, in fact, an uneventful year. Among other things, he noted the importance of understanding and properly using the new "Suspicious Activity Report" in lieu of the old criminal referral form.[6]

Michael K. O'Neal then described the current regulatory enforcement powers of the federal banking agencies. He noted that these powers are triggered generally by any "unsafe and unsound banking practice," an ill-defined concept that may cover actions that are otherwise in compliance with agency guidelines and regulations.[7] Mr. O'Neal noted that after a lull, agency enforcement actions appear again to be on the rise. He noted that the new safety and soundness enforcement powers[8] provide the agencies great flexibility to issue enforcement orders to institutions that are well capitalized and profitable, on grounds of largely discretionary standards.[9] He also noted that the agency enforcement powers are not subject to the new agency appeals processes (although in some cases a basis for an enforcement action may be subject to appeal).

Stephanie C. Bluher spoke on the SAIF-BIF deposit insurance premium disparity, the FICO bonds shortfall, and efforts to merge the deposit insurance funds. At the time of the Institute, the SAIF fund was at .51% of insured deposits, compared to the 1.25% target or required level. The BIF fund is in surplus to the required level. As a result the SAIF deposit insurance premium rate has been .23%–.31% compared to an effective zero rate for most banks; a single large thrift was paying more in deposit insurance premiums than the entire banking industry. She also noted predictions that projected declines in the SAIF-insured deposit level (due to deposit "migration" to BIF deposits) were expected to impair the income stream dedicated to payment of the FICO bonds, so as to cause a 1997 default on the bonds unless a solution was found. As described elsewhere in this issue, EGRPRA addressed this in part by recapitalizing SAIF, apportioning the FICO obligation among thrifts and banks, and prohibiting deposit migration.

Dwight Smith, Deputy Chief Counsel for Business Transactions at the Office of Thrift Supervision (OTS), discussed regulatory reform at the agency level, noting that the OTS now regulates just under 1,400 institutions, with a stable asset base, currently earning record profits and a return on assets of .99 basis points. Equity capital for the industry is over 8% and virtually all thrifts are well capitalized. He reported that the threats to SAIF-insured thrifts are now largely external rather than internal.

Mr. Smith noted several thrift-industry trends and developments, including: (1) rising interest in the use of thrift charters in innovative ways;[10] (2) increased use of subprime lending programs including secured credit card lending; (3) OTS Chief Counsel Carolyn Buck's Institute program materials advocating a new community bank charter to combine the best elements of thrift and community banks;[11] (4) the current regulatory focus on

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6. 61 Fed. Reg. 4325 (Feb. 5, 1996), 31 CFR Pt. 103.

7. The general view of the courts and agencies is that an unsafe and unsound practice is "conduct deemed contrary to accepted standards of banking operations which might result in abnormal risk of loss to a banking institution or shareholder." *See,*

(Continued in next column)

7. *(Continued from previous column)*

e.g., First Nat'l. Bank v. O.C.C., 568 F.2d 610, 611 n.2 (8th Cir. 1978). *But see infra* this text at notes 8 and 9. *See also* F. John Podvin, Jr., *Overview of Recent Legislative and Regulatory Developments*, in this issue, at 141.

8. 12 CFR Pt. 364 app. A (FDIC); 12 CFR Pt. 208 app. D (FRB); 12 CFR Pt. 30 (OCC); 12 CFR Pt. 570 app. A (OTS). *See* 60 Fed. Reg. 35674 (July 10, 1995).

9. *See supra* notes 4, 5, 7, and 8; Jonathan D. Esptein, *Liability Scaring Off Directors, Survey Finds*, Am.Bank., Oct. 25, 1996, at 6, noting that excessive regulatory enforcement powers continue to "plague the industry" and scare off potential board members.

10. *See, e.g.*, Michael Roster, Erick Newell and Gregory Trimarche, *Commercial Banks v. Thrift Institutions: A Legal Analysis*, 45 Consumer Fin. L.Q. Rep. 353 (1991); Mark E. Wohar, *The Value of a Thrift Charter: an Economic Comparison of Bank and Thrift Powers*, 45 Consumer Fin. L.Q. Rep. 358 (1991).

11. *See* Carolyn J. Buck, *Freeing Thrifts and Banks to Meet the Needs of America's Communities—Options for Financial Mod-*

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