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DODD-FRANK ACT AND NATIONAL BANK PREEMPTION: MUCH ADO ABOUT NOTHING

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ABSTRACT

In 1863, the National Bank Act (NBA) established the national bank system, with the expectation that national banks would supersede state banks. Efforts by the states to prevent this result and to impose state laws on national banks have led to a debate over the preemptive effect of the National Bank Act that exists even today.

This debate was invigorated by the financial crisis that began in 2007, following a sharp decline in housing prices and massive defaults on subprime loans. Much of the blame for the crisis was placed on banking institutions for making risky mortgages, and states' rights advocates asserted that the preemption of state anti-predatory lending laws contributed significantly to the development and origination of risky subprime mortgages.

This article finds that this hypothesis is without foundation, and conflates *predatory lending* with *subprime lending*. During the lead up to the financial crisis, non-predatory subprime mortgage lending was encouraged by both the states and Federal Government as a means of increasing home ownership. Unfortunately, once housing prices began to collapse, these subprime loans began to massively default. Preemption was not a significant factor in the origination of subprime loans, and the overwhelming majority of these loans were originated by entities not subject to NBA preemption. In fact, financial holding companies that had national bank subsidiaries often used state regulated companies to originate subprime loans in order to avoid the more stringent underwriting standards imposed by the federal regulator.

In 2010, the Dodd-Frank Act amended the NBA with respect to preemption. Some commentators argue that this law changed the standard used to determine if a state law is preempted. They argue that state law is only preempted if the law "actually prevents or significantly interferes" with a national bank power. This article reviews the statutory language and legislative history of the Dodd-Frank Act, and concludes that the legislation did not make any material change in the traditional and long-standing conflict preemption standard applicable to national banks as described by the Supreme Court in the case of *Barnett Bank v. Nelson*. The other changes made by the Dodd-Frank Act relating to preemption are relatively minor.

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In short, the Dodd-Frank Act preemption amendments effect relatively minor changes in the preemption area, and the concerns that the Act made significant changes to the preemption standard are, in reality, "much ado about nothing."

I. INTRODUCTION

THE relationship between federal and state law in the regulation of financial institutions has been contentious since the earliest days of the Nation.[1] This dispute intensified after the passage of the National Bank Act (NBA) in 1863,[2] which established a system of federally chartered banks in direct competition with state chartered banks.[3] One of the primary goals of the NBA was to wrest control of the supply of paper currency in the United States from state banks and give that function to national banks, under the supervision of a bureau within the U.S. Treasury, the "Office of the Comptroller of the Currency" (OCC).[4] The intent of the NBA was to force state banks to convert to national charters, and essentially eliminate the system of state chartered banks as then existed in the United States.[5]

Following passage of the NBA, litigation over the extent of a state's ability to regulate federally chartered banks arose almost immediately,[6] and

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1 *See* McCulloch v. Maryland, 17 U.S. 316, 356, 436 (1819) (resolving the constitutional authority of the Congress to create a federally chartered bank and holding that the Supremacy Clause limits the ability of a state to regulate such an entity).

2 National Currency Act of 1863, ch. 58, 12 Stat. 665 (1863); National Bank Act of 1864, ch. 106, 13 Stat. 99 (1864) (creating a national bank system with banks chartered by the Federal Government and required to hold U.S. Treasury bonds to back their notes). In 1864, the National Currency Act was revised by the National Bank Act. In this article we will refer to both the 1863 and 1864 legislation as the National Bank Act. For a more complete discussion of the history of the National Bank Act, *see infra* Section II.A.

3 BRAY HAMMOND, BANKS AND POLITICS IN AMERICA: FROM THE REVOLUTION TO THE CIVIL WAR, 724-27 (Princeton University Press 1991).

4 *Id.*

5 *See, e.g.*, President Abraham Lincoln, Annual Message to Cong., SENATE JOURNAL, 38th Cong., 2d Sess. 10 (Dec. 6, 1864) ("Changes from State systems to the national system are rapidly taking place, and it is hoped that, very soon, there will be in the United States no banks of issue not authorized by Congress . . . .").

6 *See, e.g.*, National Exch. Bank v. Moore, 17 F. Cas. 1211, 1211-12 (S.D. Ohio 1868) (discussing a state law that voids usurious contracts preempted by NBA); National Bank v. Commonwealth, 76 U.S. 353, 359 (1869) (holding that a state may tax shareholders of a national bank based on shares owned, but may not impose a tax on the capital of a national bank).

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has continued to the present.[7] Over the next 150 years, the states attempted numerous times to enact laws that would regulate the powers of national banks. The OCC took the opposite approach and established uniform rules with preemptive effect. This approach gave national banks with interstate operations a competitive edge over state banks that are potentially subject to different requirements in every state. According to the OCC and others, it also provides for the more efficient provision of financial services on an interstate basis, for example, by facilitating the use of uniform forms, agreements and disclosure documents.[8]

Recently, the debate over preemption reached a high level of intensity when those opposed to preemption charged that the OCC's preemption policies contributed significantly to the risky subprime mortgage lending practices that led to the financial crisis beginning in 2007.[9] The attack on national bank preemption was related to legislation that many states, and even localities, enacted in the late 1990s to prevent "predatory" mortgage lending. The argument against preemption asserts that the OCC, as part of a campaign to entice state banks to switch to a national bank charter, issued a number of preemption determinations and eventually a regulation that exempted national banks from these state laws.[10] Critics of the OCC charge that as a result of these actions, the ability of the states to prevent abusive mortgage lending was significantly diminished, and since the OCC did not adopt meaningful regulations to prevent abusive mortgage loans, consumers were left defenseless.[11] When the housing bubble eventually burst, millions of these

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7 Keith Fisher, *Toward a Basal Tenth Amendment: A Riposte to National Bank Preemption of State Consumer Protection Laws*, 29 HARV. J.L. & PUB. POL'Y 981, 984-86 (2006).

8 *See, e.g.*, Joseph R. Mason, Robert Kulick & Hal J. Singer, *The Economic Impact of Eliminating Preemption of State Consumer Protection Laws*, 12 U. PA. J. BUS. L. 781, 792 (2009) ("[P]reemption generates three primary benefits for banking customers: (1) it prevents states from imposing protectionist measures, (2) it increases the availability and reduces the price of credit, and (3) it creates a uniform regulatory climate for multi-state banks, allowing them to operate more efficiently.").

9 *See, e.g.*, Arthur E. Wilmarth, Jr., *The Dodd-Frank Act's Expansion of State Authority to Protect Consumers of Financial Services*, 36 J. CORP. L. 893, 909-19 (2011) [hereinafter Wilmarth 2011]; CENTER FOR COMMUNITY CAPITAL, UNIVERSITY OF NORTH CAROLINA AT CHAPEL HILL, THE IMPACT OF FEDERAL PREEMPTION OF STATE ANTI-PREDATORY LENDING LAWS ON THE FORECLOSURE CRISIS 2-6 (2010) [hereinafter CENTER FOR COMMUNITY CAPITAL].

10 Wilmarth 2011, *supra* note 9, at 910-12; CENTER FOR COMMUNITY CAPITAL, *supra* note 9, at 2.

11 *E.g.*, NATIONAL CONSUMER LOAN CENTER, PREEMPTION AND REGULATORY REFORM: RESTORE THE STATES' TRADITIONAL ROLE AS FIRST RESPONDER, 10-12 (2009).

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consumers defaulted on their mortgages, and the nation went into a severe recession.

This narrative soon became accepted by many as "conventional wisdom," and the legal authority of the OCC to preempt state consumer law became a subject of heated debate in Congress, among academic experts, and in the popular press.[12] Eventually, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act) amended the National Bank Act with respect to preemption.[13] These amendments prescribe new procedural requirements that the OCC must use when it seeks to issue a preemption determination.[14] The Dodd-Frank Act amendments also state that national bank preemption does not apply to subsidiaries, affiliates or agents of a national bank.[15] Some argue that the Dodd-Frank Act went further, and changed the underlying standard used to determine if a state law is preempted.[16] Focusing on a phrase used in the Dodd-Frank Act, they argue that a state law is only preempted under the NBA if the law "prevents or significantly interferes" with a national bank power, a much more stringent standard than the standard used in prior OCC precedents.[17]

This paper takes a critical look at the assertion that led to the inclusion of preemption provisions in the Dodd-Frank Act: that national bank preemption played a significant role in the housing crisis. We find that the objective evidence does not support this allegation, and that the argument linking national bank preemption and predatory lending cannot be sustained.

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12 *See, e.g.*, Kate Davidson, *Post Dodd-Frank, Preemption Fight Still Favoring Banks*, AM. BANKER, Sept. 28, 2011; Kevin Wack, *Comptroller Pick Gives Few Hints on Preemption*, AM. BANKER, July 20, 2011; Letter from Barney Frank, Carolyn Maloney, Luis Gutierrez, Mel Watt and Brad Miller, Members, U.S. House of Representatives, to John Walsh, Acting Comptroller, Office of the Comptroller of the Currency (July 1, 2011), http://democrats.financialservices.house.gov/press/PRArticle.aspx?NewsID=1428; Letter from George Madison, General Counsel, U.S. Department of the Treasury, to John Walsh, Acting Comptroller, Office of the Comptroller of the Currency (June 27, 2011), http://cdn.americanbanker.com/media/pdfs/TreasuryOCC_062811.pdf [hereinafter Madison Letter].

13 Dodd-Frank Wall Street Reform and Consumer Protection Act §§ 1044-45,12 U.S.C. § 25b (2010).

14 *Id.* § 1044, 12 U.S.C. § 25b(a)-(g) (2010).

15 *Id.* §§ 1044-1045, 12 U.S.C. § 25b (2010).

16 *See, e.g.*, Wilmarth 2011, *supra* note 9, at 925-26; Madison Letter, *supra* note 12.

17 *See, e.g.*, Wilmarth 2011, *supra* note 9, at 929; J. Elosta, *Recent Development: Dynamic Federalism and Consumer Financial Protection: How the Dodd-Frank Act Changes the Preemption Debate*, 89 N.C.L.R. 1273, 1299 (2011) ("Dodd-Frank requires significant interference, whereas the OCC's 2004 formulation merely required obstruction or impairment.").

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We then undertake an in-depth analysis of the Dodd-Frank Act, examining the statutory language, legislative history, applicable rules of statutory construction, and relevant recent case law. We conclude that the Dodd-Frank Act does not change the traditional preemption standard that has been applied with respect to national banks by both the courts and the OCC. Finally, we look at the other changes made by the Dodd-Frank Act relating to the procedures mandated for the OCC, the elimination of preemption for subsidiaries and agents of a national bank, the deference a court is to give OCC preemption determinations, and the elimination of "field preemption" as a basis for preemption under the National Bank Act. We conclude that these modifications are relatively minor, and will have little practical impact on national bank preemption, unless the OCC decides for policy reasons to change course. The last section of the paper reviews the recent changes to the OCC preemption regulation.

In order to put this analysis into proper perspective, we will begin in Part II by providing the reader with a short overview of the preemption doctrine. Under relevant Supreme Court rulings, the first step in any preemption analysis is to determine whether Congress intended the federal law in question to have preemptive effect. In Part III we review the legislative history of the NBA, and demonstrate that it was intended to broadly preempt state law.

Having laid the groundwork, we discuss in Part IV the actions the OCC took to preempt state anti-predatory lending laws before the crisis that form the basis for the current attacks on OCC preemption authority. Part V then examines the charge that the OCC's actions played a significant role in the origination of predatory mortgage loans, and the resulting financial calamity. This allegation still remains the "conventional wisdom" and could well influence the outcome of future court interpretations of the Dodd-Frank Act. It is therefore critical to look at its validity, which as we will explain, is not substantiated by the facts.

In Part VI we undertake an in-depth analysis of the Dodd-Frank Act preemption amendment to the National Bank Act. We carefully review the statutory language, the legislative history of these provisions, internal inconsistencies in the statute, and finally the recent case law. We conclude that the Dodd-Frank Act did not change the traditional and well-established "conflict" standard for determining if the National Bank Act preempts a state law. Part VII discusses other aspects of the Dodd-Frank Act preemption provisions, finding that these have only a minor impact on the Comptroller of the Currency or national bank authority. Part VIII explores another aspect of

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the Dodd-Frank Act relating to the deference that a court will give to an OCC preemption interpretation. Finally, Part IX brings the reader up to date regarding the latest amendments to the OCC's preemption rule. We conclude the paper by finding that with respect to preemption, the Dodd-Frank Act really is "much ado about nothing."

II. AN OVERVIEW OF FEDERAL PREEMPTION

A. The Supremacy Clause

The foundation for the doctrine that federal law supersedes conflicting state law is found in the "Supremacy Clause" of the U.S. Constitution.[18] In 1819, in the landmark case *McCulloch v. Maryland*, the Supreme Court held that a Maryland law imposing a tax on a branch of the Second Bank of the United States was preempted.[19] The Court explained that under the Supremacy Clause, the states have "no power, by taxation or otherwise, to retard, impede, burden, or in any manner control, the operations of the constitutional laws enacted by Congress."[20]

B. Express, Field and Conflict Preemption

The case law that followed the Court's decision in *McCulloch* has established three ways in which a federal law may preempt state law. First, Congress may preempt state law by so stating in express terms.[21] Second,

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18 U.S. CONST. art. VI, cl. 2 ("This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.").

19 McCulloch v. Maryland, 17 U.S. 316, 402-03 (1819). The First Bank of the United States was created by Congress in 1791 to handle the national debt that remained from the Revolutionary War, and establish financial order and credit for the United States. In 1811, the Bank's charter expired. The Second Bank of the United States was chartered in 1816, to help the nation recover from the debt and credit crisis following the War of 1812.

20 *Id.* at 436.

21 *E.g.*, Jones v. Rath Packing Co., 430 U.S. 519, 523-24 (1977); Island Park, LLC v. CSX Transp., 559 F.3d 96, 101 (2d Cir. 2009) (holding that express preemption arises when a federal statute expressly directs that state law be ousted); Chamber of Commerce v. Whitting, 131 S.Ct. 1968, 1977 (2011) ("When a federal law contains an express preemption clause, [the court must] 'focus on the plain wording of the clause, which necessarily contains the best evidence of Congress' preemptive intent.").

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preemption may be inferred when federal regulation in a particular field is so pervasive as to create a reasonable inference that Congress left no room for the states to supplement it.[22] In such cases of "field preemption," the volume and complexity of federal regulations demonstrate an implicit congressional intent to displace all state law.[23] Third, preemption may be implied when state law conflicts with federal law.[24] Such a conflict arises not only when compliance with both federal and state regulations is a physical impossibility,[25] but also where state law otherwise interferes with the federal enactment.[26] Thus, the Court has found preemption when the state law stands as an obstacle to the accomplishment and execution of the full purposes and objectives of the federal law,[27] is unduly burdensome and duplicative,[28] conflicts with the purposes of the federal law,[29] or if a state law curtails or hinders a federal instrumentality.[30]

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22 *E.g.*, Crosby v. National Foreign Trade Council, 530 U.S. 363, 372 (2000) ("When Congress intends federal law to occupy the field, state law in that area is preempted"); Rice v. Santa Fe Elevator Corp., 331 U.S. 218, 230 (1947).

23 *E.g.*, Air Transp. Ass'n of Am. v. Cuomo, 520 F.3d 218, 220-21 (2d Cir. 2008) (holding that field preemption is to be "implied when the pervasiveness of the federal regulation precludes supplementation by the States, where the federal interest in the field is sufficiently dominant, or where the object sought to be obtained by federal law and the character of obligations imposed by it reveal the same purpose.").

24 Geier v. American Honda Motor Co., 529 U.S. 861, 869 (2000).

25 Florida Lime & Avocado Growers, Inc. v. Paul, 373 U.S. 132, 142 (1963).

26 McCulloch v. Maryland, 17 U.S. 316, 436 (1819) (representing the foundation for conflict preemption).

27 *E.g.*, AT&T Mobility LLC v. Concepcion, 131 S. Ct. 1740, 1749-50 (2011); Barnett Bank v. Nelson, 517 U.S. 25, 31 (1996); Hines v. Davidowitz, 312 U.S. 52, 67-68 (1941).

28 *E.g.*, Watters v. Wachovia Nat'l Bank, 550 U.S. 1, 11 (2007); Anderson Nat'l Bank v. Luckett, 321 U.S. 233, 248 (1944) ("National banks are subject to state laws, unless those laws infringe the national banking laws or impose an undue burden on the performance of the banks' functions.").

29 *Watters*, 550 U.S. at 11 ("Federally chartered banks are subject to state laws of general application. . . to the extent such laws do not conflict with the letter or the general purposes of the NBA.").

30 *Id.* at 13 ("Beyond genuine dispute, state law may not significantly burden a national bank's own exercise of its real estate lending power, just as it may not curtail or hinder a national bank's efficient exercise of any other power, incidental or enumerated under the NBA.").

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C. Presumption Against Preemption

In general, the courts will apply a "presumption against preemption," especially in a field which the states have traditionally occupied.[31] The presumption grows out of the Supreme Court's traditional "respect for the states as 'independent sovereigns in our federal system' which leads to the assumption that 'Congress does not cavalierly preempt state-law causes of action.'"[32]

However, the presumption against preemption is not triggered when the state regulates in an area where there has been a history of significant federal presence.[33] The courts have repeatedly found that Congress created an extensive federal statutory and regulatory scheme over national banks, and that the presumption against preemption is not applicable in this context.[34] As the U.S. Court of Appeals for the Ninth Circuit recently explained:

> National bank association entities . . . have often been given the benefit of the doubt in preemption questions. Generally, the presumption against preemption is not applicable in the realm of national bank regulation. "[T]he presumption [against preemption] is 'not triggered when the State regulates in an area where there has been a history of significant federal presence.' . . . [B]ecause there has been a 'history of significant federal presence' in national banking, the presumption against preemption of state law is inapplicable."[35]

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[31] Medtronic, Inc. v. Lohr, 518 U.S. 470, 485 (1996) ("In all pre-emption cases, and particularly in those in which Congress has 'legislated . . . in a field which the States have traditionally occupied,' we 'start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress." (quoting *Rice*, 331 U.S. at 230)).

[32] Wyeth v. Levine, 555 U.S. 555, 565 n.3 (2009) (quoting *Medtronic*, 518 U.S. at 485).

[33] *See, e.g.*, United States v. Locke, 529 U.S. 89 (2000).

[34] *See id.* at 108 (noting that the presumption against preemption does not apply when "there has been a history of significant federal presence," such as in the area of national banking); Wells Fargo Bank, N.A. v. Boutris, 419 F.3d 949, 956 (9th Cir. 2005) ("[T]he usual presumption against federal preemption of state law is inapplicable to federal banking regulation."). *But see* Smith v. BAC Home Loan Servicing, LP, 769 F. Supp. 2d 1033 (S.D.W.Va. 2011); Cline v. Bank of Am., N.A., No. 10-1295 (S.D.W.Va. 2011); O'Neal v. Capital One Auto Fin., Inc., No. 3:10-CV-40 (N.D.W.Va. 2011).

[35] Aguayo v. United States Bank, 653 F.3d 912, 917 n.1 (9th Cir. 2011) (quoting Bank of Am. v. City & Cnty. of San Francisco, 309 F.3d 551, 558-9 (9th Cir. 2002)). *See also* Epps

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III. THE NATIONAL BANK ACT

An overriding issue in any federal preemption question is congressional intent. As stated by the Supreme Court, "[t]he purpose of Congress is the ultimate touchstone in every preemption case."[36] "Did Congress, in enacting the Federal statute, intend to exercise its constitutionally delegated authority to set aside the laws of a State? If so, the Supremacy clause requires the courts to follow Federal, not State law."[37] In making this determination, the courts will look not only at the language of the statute, but also the overall structure and purpose of the legislation as a whole, including applicable legislative history, in order to reach a reasoned understanding of the way in which Congress intended the statute and its surrounding regulatory scheme to affect business, consumers, and the law.[38]

With this in mind, we turn to the National Bank Act.[39] The NBA provides for the chartering, regulation and supervision of national banking associations.[40] The Act is administered by the Office of the Comptroller of the Currency, a bureau within the Treasury Department.[41] The OCC is headed by the Comptroller of the Currency, who is appointed by the President, with the advice and consent of the Senate, for a term of five years.[42] Although the OCC operates under the "general directions" of the Secretary of the Treasury, the OCC has independent authority to promulgate regulations,[43] and the Treasury Department may not intervene in any matter or proceeding before the Comptroller, including enforcement actions, unless otherwise provided by law.[44]

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v. JP Morgan Chase Bank, N.A., No 10-2444 (4th Cir. Apr. 5, 2012) (finding that the presumption against preemption does not apply with respect to national bank powers).

36 *Medtronic*, 518 U.S. at 485 (citing Retail Clerks v. Schermerhorn, 375 U.S. 96, 103 (1963)).

37 Barnett Bank v. Nelson, 517 U.S. 25, 30 (1996).

38 *See, e.g.*, *Medtronic*, 518 U.S. at 486; Marquette Nat'l Bank v. First of Omaha Corp., 439 U.S. 299, 314-15 (1978) ("Close examination of the National Bank Act of 1864, its legislative history, and its historical context makes clear that . . . Congress intended to facilitate . . . a national banking system."); Abdullah v. Am. Airlines, 181 F.3d 363, 366-67 (3d Cir. 1999).

39 National Bank Act, ch. 106, 13 Stat. 99 (codified as amended in scattered sections of 12 U.S.C.).

40 12 U.S.C. § 21.

41 *Id.* § 1.

42 *Id.* § 2.

43 *Id.* § 1 (incorporating the autonomy provisions of 12 U.S.C. § 1462a(b)(3)).

44 *Id.*

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The courts have recognized that almost all of the activities of national banks are controlled by the NBA and the regulations promulgated thereunder by the OCC.[45] As the agency charged by Congress with supervision of the NBA, the OCC oversees the operations of national banks and their interactions with customers.[46] The agency exercises visitorial powers, including the authority to audit a bank's books and records, largely to the exclusion of other governmental entities, state or federal.[47]

A. Legislative History of the NBA

When the Civil War began in 1861, President Lincoln was faced with both a military and financial challenge. The U.S. Treasury did not have the resources or income to meet the vast expenses associated with carrying on a war,[48] and the government eventually had to resort to the issuance of notes, informally called "greenbacks," to finance its operations.[49] However, public acceptance was far from complete, and these notes began to be traded at a considerable discount to the official price set for gold.[50] In some western states greenbacks were not accepted, and trade continued in coin.[51] The Treasury Secretary, Salmon Chase, was particularly concerned about the impact of further issuances of greenbacks on the credit of the United States and the continuing damage it was causing to the economy.[52]

Equally disturbing was that the Federal Government had no control over state bank issued notes, which were the primary circulating paper currency at that time.[53] In his report to Congress in December, 1861, Secretary Chase

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45 Watters v. Wachovia Nat'l Bank, 550 U.S. 1, 6-7 (2007).

46 Nations Bank of N.C., N.A. v. Variable Annuity Life Ins., 513 U.S. 251, 254 (1995).

47 12 U.S.C. § 484; *see* Cuomo v. Clearing House Ass'n, 557 U.S. 519 (2009) (recognizing an exception for state judicial enforcement of non-preempted applicable state law).

48 WESLEY C. MITCHELL, A HISTORY OF THE GREENBACKS, WITH SPECIAL REFERENCE TO THE ECONOMIC CONSEQUENCES OF THEIR ISSUE: 1862-1865 10 (The University of Chicago Press 1903).

49 First Legal Tender Act, Act of Feb. 25, 1862, ch. 33, 12 Stat. 345 (declaring that greenbacks were "legal tender," but were not backed by gold or silver or other species).

50 MITCHELL, *supra* note 47, at 135-40.

51 *Id.* at 145-46.

52 *Id.* at 102-03.

53 *See* Jerry W. Markham, *Banking Regulation: Its History and Future*, 4 N.C. Banking Inst. 221-27 (2000).

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pointed out the problems with this system, and the fact that the weakest banks were responsible for some of the largest issuances of paper bills.[54]

In 1862, President Lincoln and Secretary Chase proposed to deal with both of these financial problems through the creation of a national bank system. National banks would be chartered by the Federal Government, and required to hold U.S. Treasury bonds to back their notes.[55] National bank notes were intended to circulate as currency, replacing the bank notes issued by the various state banks.[56] On January 17, 1863, in a special message to Congress on the need for funds to finance the Civil War, President Lincoln again urged that a system of federally charted banks be established to issue notes that would circulate as uniform currency.[57] The President also noted that the continued issuance of circulating notes by "suspended" state banks would soon produce disastrous consequences.[58]

A little over a month later, Congress responded to President Lincoln's pleas by enacting the National Currency Act.[59] The legislation narrowly passed over the strenuous objections of many of the states concerned about losing their exclusive right to charter banks within their jurisdiction.[60] The following year, the National Currency Act was revised and reenacted, and in 1874, Congress renamed the 1864 law the "National Bank Act."[61] However, the core features of the 1863 National Currency Act survived intact.

There can be no question that the national bank system was intended to replace state banks as the source of paper currency in the United States,[62] to

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[54] The Dep't of Treasury Dep't.: Rep. of Sec. Chase Rep. to Cong. (December 10, 1861), *available at* http://www.nytimes.com/1861/12/10/news/the-treasury-department-report-of-secretary-chase.html?pagewanted=all.

[55] President Abraham Lincoln, Annual Message to Cong. (Dec. 1, 1862), reprinted in CONG. GLOBE, 37th Cong. 3d Sess. 62 (1863).

[56] *See* Markham, *supra* note 53, at 228.

[57] Special Message of President Lincoln on Financing the War, S. JOURNAL, 37th Cong. 3d Sess. 121-22 (1863).

[58] *Id.* at 122.

[59] Act of Feb. 25, 1863, ch. 58, 12 Stat. 665.

[60] *See* Statement of Senator Sherman in CONG. GLOBE, 37th Cong. 3d Sess. 844 (1863) ("[S]urrounded by difficulties, surrounded by war, and in the midst of great troubles, [Congress was] compelled to resort to some scheme by which to nationalize and arrange upon a secure and firm basis a national currency."); *see also*, BRAY HAMMOND, SOVEREIGNTY AND AN EMPTY PURSE: BANKS AND POLITICS IN THE CIVIL WAR 321-51 (Princeton University Press 1970).

[61] *See* 12 U.S.C. §38, ch. 343, 18 Stat. 123.

[62] John Wilson Million, *The Debate on the National Bank Act of 1863,* 2 J.Pol. Econ. 251, 267 (1893–94) (regarding the Currency Act, "[n]othing can be more obvious from the debates than that the national system was to supersede the system of state banks"). In 1865

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operate distinctly from the existing state banks,[63] and that it was established with the expectation that it would entirely replace the system of state banks.[64] Representative Samuel Hooper, who reported the bill to the House, stated in support of the legislation that one of its purposes was "to render the law so perfect that the State banks may be induced to organize under it, in preference to continuing under their state charters." [65] President Abraham Lincoln, in his annual message to Congress, stated that "[c]hanges from state systems to the national systems are rapidly taking place, and it is hoped that, very soon, there will be in the United States no banks of issue not authorized by Congress."[66]

As a consequence, there was considerable concern that the states would undermine the new national bank system in order to protect state chartered banks. The National Bank Act was drafted with this concern in mind.[67] Senator Sumner stated during the Senate debate: "[c]learly, the [national] bank must not be subjected to any local government, state or municipal; it must be kept absolutely and exclusively under that government from which it derives its functions."[68]

B. Preemptive Effect of the National Bank Act

The preemptive effect of the National Bank Act has been recognized repeatedly by the courts. As early as 1874 the Supreme Court stated:

> National banks have been National favorites. They were established for the purpose, in part, of providing a currency

Congress imposed a tax of 10 percent on state bank issued notes, which had the effect of making the issuance of such notes impractical (Act of March 3, 1865, 13 Stat. 469, 484 (1865)). *See also* Veazie Bank v. Fenno, 75 U.S. 533, 538-39 (1869) for a more detailed description of federal attempts to restrict or eliminate the issuance of state bank notes through taxation.

63 *See* Markham, *supra* note 53.

64 *See id.*; Annual Report of the Comptroller of the Currency (Nov. 28, 1863) (finding that the National Banking Act was intended to supersede the state banking system).

65 *See* Representative Hooper's statement in CONG. GLOBE, 38th Cong., 1st Sess. 1256 (1864) (statement of Rep. Hooper).

66 President Abraham Lincoln, Annual Message to Cong. (Dec. 6, 1864), *in* S. JOURNAL, 38th Cong. 2d Sess. 10 (1864).

67 *See* CONG. GLOBE, 38th Cong., 1st Sess. 1451 (1864) (noting that the "object" of the National Bank Act was to "establish a national banking system" free from intrusive state regulation).

68 *See* Statement of Senator Sumner in CONG. GLOBE, 38th Cong., 1st Sess. 1893 (1864).

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> for the whole country, and in part to create a market for the loans of the general government. It could not have been intended, therefore, to expose them to the hazard of unfriendly legislation by the States, or to ruinous competition with State banks.[69]

In the following year, the Court reiterated that "the States can exercise no control over [national banks], nor in any wise affect their operation except insofar as Congress may see proper to permit."[70] In 1896, the Court declared:

> National banks are instrumentalities of the Federal government, created for a public purpose. . . . [A]n attempt, by a State, to define their duties or control the conduct of their affairs is absolutely void, wherever such attempted exercise of authority . . . frustrates the purpose of the national legislation or impairs the efficiency of these agencies of the Federal government.[71]

In 1923, the Court held that a state's attempt to control the conduct of national banks is "void whenever it conflicts with the laws of the United States or frustrates the purposes of the national legislation or impairs the efficiency of the bank to discharge the duties for which it was created."[72] In *Franklin National Bank v. New York*, the Court determined that the NBA preempted a state law prohibiting a national bank from using the word "savings" in its advertisements, holding that the state law interfered with the authority of national banks to accept deposits.[73]

Recent case law has affirmed the validity of these prior decisions. In its 1996 decision *Barnett Bank v. Nelson*, the Supreme Court held a state law was preempted because it stood as an obstacle to the accomplishment of the

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69 Tiffany v. National Bank of Mo., 85 U.S. 409, 413 (1874).

70 Farmers' & Mechanics' Nat'l Bank v. Dearing, 91 U.S. 29, 34 (1875) (citation omitted).

71 Davis v. Elmira Savings Bank, 161 U.S. 275, 283 (1896); *see also* Easton v. Iowa, 188 U.S. 220, 231-32 (1903) (finding that a state law on insolvency is preempted because "Congress has provided a symmetrical and complete scheme for the banks to be organized under the provisions of the statute." Further, if the state law was not preempted, "confusion would necessarily result from control possessed and exercised by two independent authorities.").

72 First Nat'l Bank of San Jose v. California, 262 U.S. 366, 369 (1923) (citing *Davis*, 161 U.S. at 283, 288, 290).

73 Franklin Nat'l Bank v. New York, 347 U.S. 373 (1954).

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purposes of the NBA.[74] The Court reviewed the history of judicial construction of the NBA and found it is "one of interpreting grants of both enumerated and incidental 'powers' to national banks as grants of authority not normally limited by, but rather ordinarily pre-empting, contrary state law."[75] In 2007, the Supreme Court held, in *Watters v. Wachovia Bank, N.A.*, that state laws that would "significantly burden," [76] "interfere,"[77] or "impair the exercise"[78] of NBA powers are preempted.

Although it is clear from the cases discussed above that the courts have interpreted the NBA as having a broad preemptive effect, the case law also is clear that the NBA does not occupy the field.[79] "Federally chartered banks are subject to state laws of general application in their daily business to the extent such laws do not conflict with the letter or the general purposes of the National Bank Act."[80] The OCC agrees, explaining that the states retain power to regulate national banks in areas such as contracts, debt collection, acquisition and transfer of property, and taxation, zoning, criminal, and tort law.[81] According to the OCC, application of these laws to national banks typically does not affect the content or extent of their federally-authorized activities, but instead establishes the legal infrastructure that surrounds and supports the ability of national banks to do business.[82]

IV. THE OCC'S PREEMPTION REGULATION

A. Preemptive Effect of OCC Regulations

As the agency charged by Congress with supervision of the NBA, the OCC oversees the operations of national banks and their direct operating

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74 Barnett Bank v. Nelson, 517 U.S. 25, 31 (1996).
75 *Id.* at 32-33 (citations omitted).
76 Watters v. Wachovia Nat'l Bank, 550 U.S. 1, 13 (2007).
77 *Id.* at 21.
78 *Id.* at 12.
79 *See, e.g.*, *id.*; Aguayo v. United States Bank, 653 F.3d 912 (9th Cir. 2011); Williams v. Wells Fargo Bank, N.A., No. 11-21233, 2011 WL 4901346, at *9 (S.D. Fla. Oct. 14, 2011).
80 *Watters*, 550 U.S. at 11.
81 Bank Activities and Operations; Real Estate Lending and Appraisals, 69 Fed. Reg. 1904-01 (Jan. 13, 2004) (codified at 12 C.F.R. pts. 7 and 34) [hereinafter Preemption Final Rule].
82 *Id.*

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subsidiaries.[83] The OCC "bears primary responsibility for surveillance of 'the business of banking' authorized" by the NBA.[84] "To carry out this responsibility, the OCC has the power to promulgate regulations and to use its rulemaking authority to define the 'incidental powers' of national banks beyond those specifically enumerated in the statute."[85] However, the authority of the OCC is limited to the activities of the national bank and its direct operating subsidiary,[86] and the OCC has no jurisdiction to affect the application of state law to a company controlling the bank (a "bank holding company") and the holding company's non-bank subsidiaries.[87] In other words, OCC preemption actions only apply to the activities directly performed by the national bank and (prior to the effective date of the Dodd-Frank Act) by the bank's direct operating subsidiaries.[88] The OCC preemption determinations do not apply to any other entity in a banking organization, including activities conducted by the parent company or affiliated companies that are not national banks.

In *Fidelity Federal Savings and Loan v. de la Cuesta*, the Supreme Court established that federal regulations have the same preemptive effect as federal statutes.[89] More recently, in *Grier v. American Honda Motor Co.*, the Supreme Court reiterated that agency regulations can preempt conflicting state law.[90] Thus, OCC regulations have the same preemptive effect as the Act itself.[91] Congress recognized the OCC's authority to issue regulations and other determinations with preemptive effect in the 1994 Riegle-Neal Interstate

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83 *See, e.g.*, *Watters*, 500 U.S. at 6 ("Business activities of national banks are controlled by the National Bank Act. . .and regulations promulgated thereunder by the Office of the Comptroller of the Currency. . . . As the agency charged by Congress with supervision of the NBA, OCC oversees the operations of national banks and their interactions with customers.").

84 Nations Bank of N.C., N.A. v. Variable Annuity Life Ins., 513 U.S. 251, 256 (1995) (citation omitted).

85 Martinez v. Wells Fargo Home Mortg., 598 F.3d 549, 555 (9th Cir. 2010) (citation omitted).

86 *Watters*, 550 U.S. at 20-21.

87 *Id.*

88 Hereinafter, the term "national bank" will include direct operating subsidiaries of the bank, unless otherwise indicated in the text. As of July 21, 2011, the National Bank Act no longer preempts the applicability of state law to such subsidiaries. *See* discussion *infra.*

89 Fidelity Fed. Sav. & Loan Ass'n v. De la Cuesta, 458 U.S. 141, 153 (1982).

90 Geier v. American Honda Motor Co., 529 U.S. 861, 884-5 (2000).

91 Aguayo v. United States Bank, 653 F.3d 912, 919 (9th Cir. 2011) ("The OCC's authority includes 'prescrib[ing] rules and regulations to carry out the responsibilities of the office.' This regulatory authority, which carries the same weight as federal statutes, includes interpretation of state law preemption under the NBA." (quoting 12 U.S.C. § 24)).

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Banking Efficiency Act, which established notice and comment procedures for OCC preemption determinations.[92] Congress again recognized that the OCC can preempt state law through regulations, orders or "determinations" in the Dodd-Frank Act, which established procedures for, and judicial review of, OCC preemptive actions.[93]

Regulatory intent determines if a validly promulgated rule has preemptive effect. In *Williamson v. Mazda Motor of America*, the Supreme Court held that a Department of Transportation (DOT) automobile safety standard did not preempt a more stringent state requirement because the DOT rulemaking record disclosed no preemptive intent.[94] Therefore, the Court found, a state-based civil action at issue in the litigation could proceed, because it did not "stan[d] as an obstacle to the accomplishment . . . of the full purposes and objectives" of the federal law.[95]

B. Preemption Prior to the 2004 Regulation

Prior to 2004, the OCC issued a number of agency interpretive letters and legal opinions regarding the applicability of state law to national banks. These interpretations and legal opinions can be broken down into several categories.

The OCC preempted state laws that had the effect of protecting state-chartered depository institutions from national bank competition. For example, OCC regulatory actions preempted state laws that limited the ability of national banks to advertise their permissible business activities,[96] establish branches within the state,[97] operate offices within a certain distance from state

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92 Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994, Pub. L. No. 103-32, § 114.

93 Dodd-Frank Wall Street Reform and Protection Act § 1044, 12 U.S.C.A. § 25b (2010) (authorizing the OCC to preempt state law by "regulation, order or determination.").

94 Williamson v. Mazda Motor of Am., 131 S.Ct. 1131, 1139-40 (2011).

95 *Id.* (quoting Hines v. Davidowitz, 312 U.S. 52, 67 (1941)).

96 *See, e.g.*, Office of the Comptroller of the Currency, OCC Interp. Ltr. No. 804 (Sept. 30, 1997) (noting a national bank can advertise any service that the bank lawfully offers notwithstanding state law to the contrary) (citing Franklin Nat'l Bank v. New York, 347 U.S. 373, 377-78 (1954)).

97 Office of the Comptroller of the Currency, OCC Corp. Decision 98-07 (Jan. 15, 1998) (state law prohibiting an out-of-state national bank from having branches in that state preempted); OCC Corp. Decision 95-59 (Nov. 20, 1995) (prohibiting out-of-state national banks from branching in Idaho, as permitted by federal law, preempted). Prior to 1994, national banks had limited opportunity to operate branches across state lines, and branching within a state had to be on the same basis as allowed for state chartered banks. 12 U.S.C. § 36. The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994

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chartered bank home offices,[98] locate ATM machines within the state,[99] engage in fiduciary activities,[100] and make particular types of loans.[101]

The OCC has also preempted state laws protecting specific types of businesses from competition with national banks, including insurance agencies,[102] securities firms,[103] settlement attorneys,[104] auto dealers,[105] and even auctioneers.[106] State attempts to assert licensing requirements or examination authority over national banks have also been preempted.[107]

State laws designed to provide enhanced protection for consumers are subject to preemption if they limit or restrict authorized bank powers. Such laws include state attempts to restrict or limit permissible fees and other non-

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authorized national banks to branch across state lines if certain conditions are met. Pub. L. 103-328; 108 Stat 2338 (1994).

[98] Office of the Comptroller of the Currency, OCC Interp. Ltr. No. 590 (June 18, 1992) (discussing the Illinois restrictions on the establishment of federal branches that do not limit the authority of the Comptroller to license federal branches of foreign banks in Illinois).

[99] Office of the Comptroller of the Currency, OCC Interp. Ltr. No. 939 (Oct. 15, 2001) (preempting state attempts to prevent out-of-state banks from operating ATM machines); OCC Interp. Ltr. No. 789 (June 27, 1997) (preempting state law prohibiting national banks from placing their name on ATM machines).

[100] Office of the Comptroller of the Currency, OCC Corp. Decision 97-33 (June 1, 1997) (preempting state law that prohibits an out-of-state national bank from acting as fiduciary).

[101] Preemption Determination, 66 Fed. Reg. 28,593 (May 23, 2001) (preempting state law that would have limited the ability of national banks to finance automobile purchases).

[102] *Barnett Bank*, 517 U.S. at 31–37 (1996) (preempting state restriction on national bank insurance agency activities).

[103] Office of the Comptroller of the Currency, OCC Interp. Ltr. No. 749, (Sept. 13, 1996) (preempting restrictions on the sale of annuities); Clark v. Securities Industry Association, 479 U.S. 388 (1987) (holding that state branching laws cannot prevent national banks from operating discount securities brokerage offices).

[104] National Bank Charges, 66 Fed. Reg. 34,791 (July 2, 2001), codified in 12 C.F.R. § 7.4002 (preempting state laws prohibiting national banks from charging a fee for the preparation of mortgage documents).

[105] Preemption Opinion, 66 Fed. Reg. 23,977 (May 10, 2001) (preempting prohibition on national bank selling repossessed automobiles without an auto dealer license).

[106] Preemption Determination, 65 Fed. Reg. 15,037 (Mar. 20, 2000) (preempting state restriction on national bank conducting web based auction of its certificates of deposits).

[107] OCC Interp. Ltr. (Feb. 9, 1995) (preempting state law requiring national banks to obtain a license to engage in consumer lending); OCC Interp. Ltr. (Feb. 4, 1992) (unpublished) (preempting state law requiring licensing of credit card providers).

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interest charges,[108] including service charges,[109] fees on the use of ATM machines,[110] consumer notices and disclosures,[111] and similar laws.[112]

In a controversial decision in 2003, the OCC, following similar actions by the National Credit Union Administration[113] and the Office of Thrift Supervision,[114] determined that many provisions of the Georgia Fair Lending Act[115] were preempted as to national banks.[116] The Act contained restrictions on loans meeting statutory criteria, and prohibited the use of certain features, such as negative amortization and balloon payments, in connection with these "predatory" mortgages.[117] Consumer advocates opposed the OCC action, and argued that the OCC was preventing the state from protecting its citizens.[118] The OCC, however, stated that it had no evidence that national banks were engaged in predatory lending practices.[119] Further, the OCC noted that national banks could not engage in many practices associated with predatory lending without violating applicable regulatory guidance and supervisory standards.[120] As discussed below, the OCC also decided to incorporate new anti-predatory lending rules in a formal regulation dealing with preemption more generally.

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108 Baptista v. JPMorgan Chase Bank, N.A., 640 F.3d 1194, 1197–98 (2011), *cert. denied* __ U.S. __, 2011 U.S. Lexis 5261 (Oct. 3, 2011) (holding that OCC regulations preempt state restrictions on fees and service charges).

109 Monroe Retail, Inc. v. RBS Citizens, N.A., 589 F.3d 274, 283-84 (6th Cir. 2009) (holding that national banks may charge any fee contractually agreed to, including garnishment fees).

110 Bank of Am. v. City & Cnty. of San Francisco, 309 F.3d 551 (9th Cir. 2002) (preempting state limits on ATM charges).

111 Rose v. Chase Bank U.S.A., N.A., 513 F.3d 1032, 1037–38 (9th Cir. 2008) (state disclosure requirement preempted).

112 *See, e.g.,* 12 C.F.R. §§ 7.4008(b), 34.3(b).

113 National Credit Union Administration, 02-0649, Applicability of Georgia Fair Lending Act to Federal Credit Unions (July 29, 2002).

114 Office of Thrift Supervision, P-2003-1, Preemption of Georgia Fair Lending Act (Jan. 21, 2003).

115 GA Code Ann. §§ 7–6A–1 to 7–6A–13 *et seq.*

116 Preemption Determination and Order, 68 Fed. Reg. 46,264 (Aug. 5, 2003).

117 *Id.*

118 *See, e.g.,* Comment Letter from the National Consumer Law Center to the OCC (Mar. 28, 2003) (available at http://www.nclc.org/images/pdf/preemption/archive/032803_er.pdf).

119 Preemption Determination and Order 68 Fed. Reg. 46264, 46265 (Aug 5, 2003).

120 *Id.* ("National banks' real estate lending standards are subject to a comprehensive Federal regulatory framework that addresses the types of abusive and predatory practices that the [Georgia Fair Lending Act] seeks to prohibit.").

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C. OCC Preemption Regulation

Contemporaneously with the OCC's determination relating to the Georgia Fair Lending Act, the OCC issued a notice of proposed rulemaking (NPR) to establish more generally the rules governing the applicability of state law to national banks.[121] The final regulation, published on January 13, 2004, reviewed the judicial decisions on preemption under the NBA, and, according to the preamble, attempted to distill the various formulations of when state law will be preempted into a concise test: state law may not "obstruct, impair or condition" national bank powers.[122] The regulation then listed types of state laws that were preempted, as well as laws that were not preempted under this standard.[123]

The 2004 regulation included an anti-predatory lending provision that prohibits national banks from making consumer loans, including real estate loans, "based predominantly on the bank's realization of the foreclosure or liquidation value of the borrower's collateral, without regard to the borrower's ability to repay the loan according to its terms."[124] As explained in the NPR, the requirement to underwrite a loan based on the borrower's ability to repay "reflects a bedrock principle of sound banking practices,"[125] and is consistent with the prior views of the agency that questioned the safety and soundness of consumer loans underwritten on the basis of the foreclosure value of the collateral.[126] The agency warned that "it is axiomatic that lenders following safe and sound lending practices will take reasonable steps to assure themselves and to verify that the borrower has the capacity to make scheduled payments to repay a loan, taking into account all of the borrower's obligations, including other indebtedness, insurance, and taxes, as well as

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121 Bank Activities and Operations; Real Estate Lending and Appraisals, 68 Fed. Reg. 46119, 46120 (proposed Aug. 5, 2003) (to be codified at 12 C.F.R. pt.7 and 34) [hereinafter Preemption Proposed Rule] ("Due to the number and significance of the questions that continue to arise with respect to the preemption of state laws in these areas, we believe it is now timely to provide more comprehensive standards regarding the applicability of state laws to lending, deposit-taking, and other authorized activities of national banks.").

122 Preemption Final Rule, *supra* note 81, at 1916-17; Bank Activities and Operations, 69 Fed. Reg. 1895 (proposed Jan. 13, 2004) (to be codified at 17 C.F.R. pt.1778) (another regulation issued around the same time dealing with the authority of a state to examine or take enforcement actions against a national bank) [hereinafter Visitorial Powers Rule].

123 *Id.*

124 *Id.* at 1904 (codified at 12 C.F.R. §§ 7.4008(b), 34.3(b)).

125 Preemption Proposed Rule, *supra* note 121, at 46127.

126 Preemption Final Rule, *supra* note 81, at 1904.

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principal and interest."[127] The final regulation, however, did not specify the means by which a bank could establish the financial capacity of the borrower, and left that to the discretion of the bank, leading some to characterize the rule as "weak."[128] The regulation also prohibits a national bank from engaging in any practice that would be deemed an unfair or deceptive practice under the FTC Act and regulations.[129] The OCC stated these provisions are intended to augment, not replace, other applicable predatory lending standards, including anti-predatory lending guidance previously issued by the OCC.[130]

The most significant criticism of the preemptive provisions of the regulation was that it went beyond judicial precedent, and that the standard "obstruct, impair, or condition" was not consistent with the case law.[131] Opponents of the regulation argued that *Barnett Bank* was the appropriate touchstone, and that the Supreme Court applied a more stringent standard for preemption in that case than did the OCC.[132] Some commentators focused in particular on the word "condition" as particularly aggressive, and argued that any state regulation of a national bank would be viewed as an impermissible "condition" on national bank powers.[133]

The OCC's position, at least until 2011, was that the words in the regulation were "drawn directly from applicable Supreme Court precedents" and the OCC intended the phrase "obstruct, impair or condition" to be nothing more than "the distillation of the various preemption constructs articulated by the Supreme Court . . . and not . . . a replacement construct that

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127 Preemption Proposed Rule, *supra* note 121, at 46127.

128 Wilmarth 2011, *supra* note 9, at 906.

129 Preemption Final Rule*, supra* note 81, at 1916-17 (codified at 12 C.F.R. §§ 7.4008(c), 34.3(c)).

130 *E.g.*, Guidelines for National Banks to Guard Against Predatory and Abusive Lending Practices, OCC Adv. Ltr. 2003-2 (Jan. 7, 2003); OCC Adv. Ltr. 2003-3 (Feb. 21, 2003).

131 *E.g.*, Letter from Paul Sarbanes, Senator, U.S. Senate, to John D. Hawke, Comptroller, Office of the Comptroller of the Currency (Nov. 24, 2003) ("[The OCC] now appears to be ignoring both the Supreme Court and Congress by pursing a preemption agenda that would override any state law that has any impact on a national bank.").

132 *See, e.g.*, Arthur E. Wilmarth, Jr., *The OCC's Preemption Rules Exceed the Agency's Authority and Present a Serious Threat to the Dual Banking System and Consumer Protection*, 23 Ann. Rev. Banking & Fin. L., 225 (2004) [hereinafter Wilmarth 2004]; *OCC's Proposal To Preempt Application of State Anti-Predatory Lending and Other Laws,* Center for Responsible Lending (Oct. 6, 2003), http://www.responsiblelending.org/media-center/press-releases/archives/CRLCommentonOCCProposedRulemaking03-16.pdf.

133 Wilmarth 2004*, supra* note 132, at 249.

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is in any way inconsistent with those standards."[134] Comptroller John Hawke testified before Congress to this effect,[135] and he further explained that the "key to determining the applicability to national banks of State laws . . . is not the phrase 'obstruct, impair, or condition' but *rather the case law that underlies and supports that phrase*."[136]

D. OCC Regulation Did Not Preempt All State Consumer Law

Despite the concern that the 2004 regulation effectively prevented the states from regulating any aspect of national bank activities,[137] many state laws were found to be applicable to national banks under the preemption regulation. For example, state laws prohibiting fraudulent, unfair or illegal acts or behavior have been deemed applicable to national banks.[138] National banks also may be subject to state laws prohibiting "unfair or deceptive" acts or practices,[139] including laws directed at deception,[140] unfair business practices[141] and misrepresentation.[142] State actions may be brought on the

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134 Preemption Final Rule, *supra* note 81, at 1910.

135 *Review Of The National Bank Preemtion Rules: Hearing before the Committee on Banking, Housing and Urban Affairs*, 108th Cong. 108-864 (2004) (statement of John D. Hawke, Comptroller, Office of the Comptroller of the Currency) ("(T)he preemption rule, codifies principles that have been established in almost 200 years of decisions by the Supreme Court and lower Federal courts, that have been applied in innumerable interpretations and rulings of the OCC over many years, and that have been embodied in regulations of our sister agency, the Office of Thrift Supervision for many years.").

136 *Review Of The National Bank Preemtion Rules: Hearing before the Committee on Banking, Housing and Urban Affairs*, 108th Cong. 108-864, at 100 (2004).

137 *See, e.g.*, KATHLEEN C. ENGEL & PATRICIA A. MCCOY, THE SUBPRIME VIRUS: RECKLESS CREDIT, REGULATORY FAILURES, AND NEXT STEPS 157-62 (2011); BETHANY MCLEAN & JOE NOCERA, ALL THE DEVILS ARE HERE: THE HIDDEN HISTORY OF THE FINANCIAL CRISIS 146-147 (2010).

138 Martinez v. Wells Fargo Home Mortg., 598 F.3d 549, 555 (9th Cir. 2010) ("State laws of general application, which merely require all businesses (including national banks) to refrain from fraudulent, unfair or illegal behavior do not necessarily impair a bank's ability to exercise its real estate lending powers.").

139 *Guidance on Unfair or Deceptive Acts or Practices,* OCC Adv. Ltr. No. 2002-3 (Mar. 22, 2002).

140 Mann v. TD Bank, N.A., No. 09-1062, 2009 WL 3818128 (D. N.J. Nov. 12, 2009) (holding that claims brought under the New Jersey Consumer Fraud Act regarding a bank's advertising of "free" and "no fee" gift cards was deceptive, misleading, and unlawful because it failed to disclose the existence of dormancy and replacement fees was not preempted).

141 White v. Wachovia Bank, N.A., 563 F. Supp. 2d 1358 (N.D. Ga. 2008) (holding that a claim under the Georgia Fair Business Practices Act that a bank engaged in unfair or

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grounds that a national bank violated a common law duty of "good faith and fair dealing" with customers.[143] Similarly, a national bank is subject to state law claims of "unjust enrichment."[144] State laws relating to the right to collect a debt, as well as the regulation of debt collection practices, also have been found to be applicable to national banks.[145] In *Epps v. JP Morgan Chase*, the court of appeals for the Fourth Circuit found that state laws requiring certain disclosures after an automobile was repossessed and prior to its resale were not preempted because such laws were part of the legal infrastructure establishing the bank's rights and obligations in collecting a debt.[146] In *Cline v. Bank of America, N.A*, the court found that generally applicable restrictions on abusive collection practices do not interfere in any way with the purposes and objectives of federal law.[147]

V. PREDATORY MORTGAGE LENDING

Beginning in 1999, twenty-eight states adopted "anti-predatory lending" laws and regulations prohibiting "predatory" mortgage lending.[148] The term "predatory" mortgage lending describes the use of abusive practices, including misinformation and manipulative sales techniques, to take unfair

deceptive business practices by manipulating the posting of transactions to an account in order to impose overdraft fees was not preempted).

142 Jefferson v. Chase Home Fin., No. 06-6510, 2007 U.S. Dist. LEXIS 94652, at *2 (N.D. Cal. Dec. 14, 2007) (holding that a claim regarding alleged misrepresentation in crediting payments was not preempted).

143 Gutierrez v. Wells Fargo Bank, N.A, 730 F.Supp.2d 1080 (N.D. Cal. 2010) (action based on breach of a bank's duty to act in good faith not preempted); Trombly v. Bank of Am. Corp., 715 F.Supp.2d 290, 296 (D.R.I. 2010) (holding that covenant of good faith and fair dealing is not preempted by the NBA).

144 Williams v. Wells Fargo Bank, N.A., No. 11-21233, 2011 WL 4901346, at *9 (S.D. Fla. Oct. 4, 2011). olding that unjust enrichment claim not preempted by the NBA).

145 *See* Aguayo v. United States Bank, 653 F.3d 912, 919 (9th Cir. 2011); OCC Interp. Ltr. No. 1082 (June 2007) (stating that while the "right to collect a debt" is subject to state law, the method used to collect the debt is not); *But see*, Opal v. Bate, 454 B.R. 869, 878 (Bankr. M.D. Fla. 2011) (rejecting the OCC's position).

146 Epps v. JP Morgan Chase Bank, N.A., No 10-2444 (4th Cir. Apr. 5, 2012)

147 Cline v. Bank of Am., N.A., 823 F. Supp. 2d 387, 389 (S.D. W. Va. 2011).

148 Wei Li & Keith S. Ernst, The Best Value in the Subprime Market: State Predatory Lending Reforms, Center for Responsible Lending 2 (2006) [hereinafter CRL 2006 Paper]; *See, e.g.*, 1999 N.C. Sess. Laws 332 (1999), codified at N.C. Gen. Stat. 24-1.1A, 24-1.1E, 24-2.5, 24-8, 24-10.2 (For a review of the development of state anti-predatory lending statutes); *See* Raphael W. Bostic et al., State and Local Anti-Predatory Lending Laws: The Effect of Legal Enforcement Mechanisms (2007), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1005423.

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advantage of a borrower's lack of information about loan terms and their consequences.[149] It should be distinguished from the term "subprime mortgage lending," which refers to mortgage loans made to borrowers with weakened credit histories, and is often demarcated as mortgages made to consumers with a FICO credit score of 660 or less.[150]

Subprime loans do not necessarily have abusive terms, and until the downturn in the housing market beginning in 2007, the widely accepted view was that *responsible* subprime lending provided important public benefits by increasing credit availability and home ownership opportunities for lower-income consumers.[151] State anti-predatory lending laws never targeted subprime lending generally, but instead were designed to eliminate the use of predatory practices.[152] A comprehensive study by the Center for Responsible Lending analyzed six million subprime loans made in the twenty-eight states with anti-predatory lending measures, and concluded that these laws "are working well to prevent predatory mortgage lending, but . . . also allow subprime credit not targeted by the laws to flourish."[153] The report noted that states with anti-predatory lending provisions "have struck an effective balance: Total subprime volume in states with [anti-predatory lending] reforms is similar to that found in states without significant protections."[154]

The OCC regulation issued in 2004 preempted state anti-predatory lending laws that had the effect of regulating the terms and conditions of mortgage loans made by national banks or their operating subsidiaries. In justifying this result, the OCC explained that the markets for credit products, including mortgages, were now national in scope, and the efficiency of

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[149] U.S. Department of Housing and Urban Development and Department of Treasury, Curbing Predatory Home Mortgage Lending 16 (2000).

[150] Federal Deposit Insurance Corporation and Office of Thrift Supervision, Expanded Guidance for Subprime Lending Programs, Board of Governors of the Federal Reserve System, Office of the Comptroller of the Currency 1 (2001).

[151] Consumer Protection: Federal and State Agencies Face Challenges in Combating Predatory Lending, General Accountability Office 21-22 (GAO -04-280 Jan. 2004) ("[M]ost analysts believe that only a relatively small portion of subprime loans contain features that may be considered abusive. In addition, according to officials at HUD and the Department of the Treasury, the emergence of a subprime mortgage market has enabled a whole class of credit-impaired borrowers to buy homes or access the equity in their homes.").

[152] CRL 2006 Paper, *supra* note 148, at 13 ("When states pass stronger laws against predatory lending, the goal is to reduce the prevalence of loans with abusive terms without reducing the availability of responsible mortgage credit.").

[153] *Id.* at 2.

[154] *Id.* at 13.

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national bank lending operations across state lines was impeded by having to comply with a multitude of requirements that differ state by state.[155] According to the OCC:

> When national banks are unable to operate under uniform, consistent, and predictable standards, their business suffers, which negatively affects their safety and soundness. The application of multiple, often unpredictable, different state or local restrictions and requirements prevents them from operating in the manner authorized under Federal law, is costly and burdensome, interferes with their ability to plan their business and manage their risks, and subjects them to uncertain liabilities and potential exposure.[156]

The Comptroller touted this view publicly, stating in one speech that:

> There is no question that national banks' immunity from many state laws is a significant benefit of the national charter—a benefit that the OCC has fought hard over the years to preserve. The ability of national banks to conduct a multi-state business subject to a single uniform set of federal laws, under the supervision of a single regulator, free from visitorial powers of various state authorities, is a major advantage of the national charter.[157]

Others argue that the OCC's preemption determinations were part of a race to the bottom, and that by not providing a national standard comparable to the state anti-predatory lending laws, the agency's actions were intended to lure state banks into the federal system by offering a reprieve from the more stringent anti-predatory lending restrictions imposed by the states.[158] The

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155 Preemption Final Rule, *supra* note 81, at 1907-08.

156 *Id.* at 1908.

157 John D. Hawke, Jr., Comptroller of the Currency, Office of the Comptroller of the Currency, Remarks Before the Women in Housing and Finance 2 (Feb. 12, 2002) (transcript available at http://www.occ.gov/static/news-issuances/speeches/2002/pub-speech-2002-10.pdf) (on file with the Virginia Law & Business Review Association).

158 *See* Wilmarth 2004, *supra* note 132, at 274-75.

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final report of the Financial Crisis Inquiry Commission discusses both views without reaching a conclusion.[159]

With respect to the consumer protection issues raised by the preemption of state anti-predatory lending laws, the OCC stated that predatory and abusive lending practices will not be tolerated, and that, other than isolated instances, national banks and their subsidiaries have not been responsible for predatory lending activities.[160]

A. OCC Regulatory Response to Predatory Mortgage Lending

Beginning in 2000, Comptroller Hawke raised an alarm about predatory lending practices in the mortgage lending area, which he called "a growing problem with national implications."[161] That same year, Mr. Hawke announced he would direct bank examiners to carefully review bank lending policies and practices to ensure that the only loans being made were those with a reasonable expectation of repayment without resorting to collateral.[162] He also stated that examiners would look for abusive lending practices indicating an increased risk of racial discrimination.[163]

In 2003, the OCC issued an advisory letter[164] warning national banks not to engage in predatory lending practices.[165] The letter stated that a

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[159] THE FIN. CRISIS INQUIRY COMM'N, THE FINANCIAL CRISIS INQUIRY REPORT: FINAL REPORT OF THE NATIONAL COMMISSION ON THE CAUSES OF THE FINANCIAL AND ECONOMIC CRISIS IN THE UNITED STATES at 111-13 (2011).

[160] *Id.* at 1914 (citing, among other authority, a joint HUD-Treasury study finding that predatory lending practices were largely confined to unregulated mortgage lenders, and the conclusion reached by all 46 state attorneys general that: "Based on consumer complaints received, as well as investigations and enforcement actions undertaken by the Attorneys General, predatory lending abuses are largely confined to the subprime mortgage lending market and to non-depository institutions. Almost all of the leading subprime lenders are mortgage companies and finance companies, not banks or direct bank subsidiaries.").

[161] John D. Hawke, Jr., Comptroller of the Currency, Office of the Comptroller of the Currency, Remarks Before the National Community Reinvestment Coalition, on Banks and Community Development 77 (Mar. 21, 2000).

[162] Statement of John D. Hawke, Jr., Comptroller of the Currency, Office of the Comptroller of the Currency in *Predatory Lending Practices: Hearing Before the H. Comm. on Financial Services*, 106th Cong. 19 (2000).

[163] *Id.*

[164] While advisory letters do not have the force and effect of a regulation, failure to follow an advisory letter will subject a national bank to regulatory criticism and could lead to a downgrade in the institution's report of examination. As a result, advisory letters and

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"fundamental characteristic of predatory lending is the aggressive marketing of credit to prospective borrowers who simply cannot afford the credit on the terms being offered."[166] As noted, in 2004, the OCC, as part of its preemption rule, prohibited national banks and their subsidiaries from lending "based predominantly on the bank's realization of the foreclosure or liquidation value of the borrower's collateral, without regard to the borrower's ability to repay the loan according to its terms," as well as other "abusive lending practices."[167] On January 31, 2005, the OCC issued legally enforceable mandatory residential mortgage lending standards applicable to national banks and their operating subsidiaries.[168] These standards prohibit institutions from being involved, directly or indirectly, in mortgage loans involving abusive, predatory, unfair or deceptive practices, including equity stripping and fee packing,[169] loan flipping,[170] refinancing of subsidized mortgage products,[171] or encouraging a borrower to default. These standards also require a national bank or subsidiary to carefully consider the circumstances and the possibility of violating the prohibition on making abusive, unfair or deceptive loans when a mortgage loan contains certain "high risk" provisions, such as negative amortization, balloon payments, prepayment penalties, or the absence of appropriate documentation of the borrower's ability to repay the loan.[172] In May 2005, all of the federal banking agencies issued joint guidance on Home Equity Lending.[173] This was

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similar informal guidance are often viewed by both examiners and regulated institutions as mandatory rather than discretionary instructions.

165 OCC Adv. Ltr. 2003-2 (Feb. 21, 2003).

166 *Id.* at 2.

167 Preemption Final Rule, *supra* note 81, at 1916-17, codified at 12 C.F.R. §§ 7.4008(b), 34.3(b) (2012).

168 OCC Guidelines Establishing Standards for Residential Mortgage Lending Practices, 70 Fed. Reg. 6329 (Feb. 7, 2005) (codified at 12 C.F.R. pt. 30) (2012)).

169 *Id.* at 6333 (defining "equity stripping" and "fee packing" which refer to repeated refinancing with high fees that result in depleting the homeowner's equity interest in the property).

170 *Id.* (holding that "loan flipping" is the practice of refinancing a mortgage pursuant to terms and fees that do not result in a "tangible economic benefit" to the homeowner.).

171 *Id.* (holding that mortgage made under a program that offers subsidized rates or other terms favorable to the borrower may not be refinanced unless the new loan provides a "tangible economic benefit" to the borrower relative to the subsidized mortgage).

172 *Id.* at 6333-34.

173 Credit Risk Management Guidance for Home Equity Lending, attachment to Joint Press Release, Office of the Comptroller of the Currency et al., Credit Risk Management: Guidance for Home Equity Lending, FDIC-PR-44-2005 (May 16, 2005),

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followed, in 2006, by interagency guidance on non-traditional mortgages.[174] This guidance also requires banks to assess the borrower's ability to repay the loan.[175] In 2007, the OCC and the other federal banking agencies issued joint guidance on subprime lending, requiring that borrowers must be qualified for a loan using the fully indexed rate.[176]

B. Subprime Mortgage Lending

The effectiveness of the regulatory actions described above has been much debated.[177] However, the available statistical evidence indicates that national banks and their subsidiaries did not play a significant role in the issuance of *predatory* loans, and were not dominant in the origination of non-predatory *subprime* mortgage loans.[178]

The overwhelming majority of subprime loans were originated by state-regulated financial companies, which were outside of the scope of the OCC's preemption regulation.[179] While some of the leading subprime lenders included bank holding companies and their non-bank subsidiaries, these companies are not regulated by the OCC and are not subject to the OCC's preemption rule or regulatory oversight. Since the OCC preemption regulation only applies to activities conducted by national banks and their direct operating subsidiaries, the regulation had no impact on any other

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http://www.occ.gov/news-issuances/bulletins/2005/bulletin-2005-22a.pdf (on file with the Virginia Law & Business Review Association).

174 Interagency Guidance on Nontraditional Mortgage Product Risks, 71 Fed. Reg. 58,609 (Oct. 4, 2006).

175 *Id.*

176 Statement on Subprime Mortgage Lending, 72 Fed. Reg. 37,569, at 37,571 (July 10, 2007).

177 *See Consumer Protections in Financial Services: Past Problems, Future Solutions: Hearing Before the S. Comm. On Banking, Housing and Urban Affairs, 111th Cong.* 64 (2009) (statement of Patricia McCoy) ("Generally, in lieu of binding rules, Federal banking regulators, including the OCC and OTS, issued a series of 'soft law' advisory letters and guidelines against predatory or unfair mortgage lending practices by insured depository institutions."); Wilmarth 2011, *supra* note 9, at 901.

178 As discussed above, the vast majority of subprime mortgage loans were not viewed by the states or the federal government as predatory, but rather were looked upon as a positive means to foster home ownership for lower income consumers.

179 *See* Letter from John Dugan, Comptroller of the Currency, to Elizabeth Warren, Chair, Congressional Oversight Panel (Feb. 12, 2009) ("OCC-supervised institutions accounted for approximately 12 to 14 percent of the non-prime originations: in the years 2005-2007." Foreclosure rates for these OCC regulated originators were "markedly lower" than for other types of originators.) [hereinafter Dugan, Letter].

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affiliates, such as holding companies. Thus, the mortgage lending practices of holding companies and other affiliates remained fully subject to state law.

More recently, an OCC review of subprime lending prepared for the Financial Crisis Inquiry Commission found that the vast majority of subprime lending was done outside of national banks in entities that were subject to state law.[180] The same was true in the market for so-called Alt-A mortgages, which were mortgages originated without full documentation of the income and assets of the borrower.

This conclusion is consistent with the mortgage lending activities of Countrywide Financial Corporation. Prior to its acquisition in 2008, Countrywide was one of the largest originators of subprime loans in the United States.[181] However, almost all of its mortgages were originated by holding company units, which were not subject to preemption, and those units were subject to state regulation.[182] For example, in fiscal year 2006, Countrywide's non-bank mortgage lending unit produced $421 billion of mortgages, while the national bank subsidiary produced only $23 billion of mortgages.[183] In 2007, Countrywide converted its national bank subsidiary into a federal savings association, but the mortgage lending continued to be concentrated outside of the insured depository institution, with the state-regulated units producing $385 billion in mortgages, and the federal thrift producing $18 billion in mortgages.[184] Thus, preemption was not a significant factor in the origination of these loans, since Countrywide originated almost

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180 *Subprime Lending and Securitization and the Government-Sponsored Enterprises: Hearing Before the Financial Crisis Inquiry Commission* (2010) (statement of John C. Dugan, Comptroller, Office of the Comptroller of the Currency), [hereinafter Dugan, *FCIC Testimony*].

181 *See*, J. Dunbar and D. Donald, *Who's Behind the Financial Meltdown?* (May 6, 2009, updated Sept. 7, 2011, 4:58 PM), *available at* http://www.iwatchnews.org/2009/05/06/5449/roots-financial-crisis-who-blame (noting that Countrywide Financial Corporation was the largest subprime lender in the 2005-2007 period) (on file with the Virginia Law & Business Review Association).

182 Countrywide Financial Corporation, Annual Report (Form 10-K), at 23 (Mar. 1, 2007) ("The rules, regulations and requirements of these [federal and state] entities, among other things, impose licensing obligations on the Company or its subsidiaries; establish standards for advertising as well as processing; underwriting and servicing mortgage loans and appraisal practices; prohibit discrimination; restrict certain loan features in some cases and fix maximum interest rates and fees in some states.").

183 *Id.* at 3.

184 Countrywide Financial Corporation, Annual Report (Form 10-K), at 3 (Feb. 29, 2008). Beginning in 2008, Countrywide moved its mortgage production channels to its insured federal savings association. Countrywide was acquired by Bank of America Corporation in 2008.

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all of its mortgages in state-regulated entities. A review of securities filings for other large mortgage lenders reveals a similar pattern: the subprime originations were consistently located outside of the national bank or federal thrift units and housed in state regulated mortgage departments.[185]

The role of state-regulated "shadow" financial institutions in unsafe subprime lending was recognized by the Treasury Department, which noted in its 2009 report to Congress that 94 percent of "higher-priced loans" to "lower income borrowers" were originated by non-depository institution lenders.[186] Congressman Barney Frank came to the same conclusion:

> Reasonable regulation of mortgages by the bank and credit union regulators allowed the market to function in an efficient and constructive way, while mortgages made and sold in the unregulated sector led to the crisis.
>
> At every step in the process, from loan origination through the use of exotic unsuitable mortgages to the sale of securities backed by those mortgages, the largely unregulated uninsured firms have created problems, while the regulated and FDIC-insured banks and savings institutions have not. To the extent that the system did work, it is because of prudential regulation and oversight. Where it was absent, the result was tragedy for hundreds of thousands of families who have lost, or soon will lose, their homes and for those who invested in shaky and untested, even though highly rated, securities, and have been forced to take large losses and, in many cases, shut their doors.[187]

At least one major consumer group has also acknowledged that the subprime lending originations were primarily occurring in state-regulated entities. In 2008, the Center for Responsible Lending published an "issue

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185 *See, e.g.*, Washington Mutual, Inc., Annual Report (Form 10-K/A), at 34, 43 (May 22, 2008) (Washington Mutual, Inc., which housed its subprime mortgage origination activities in a state-regulated holding company subsidiary, Long Beach Mortgage Co.). For more examples, *see* Dugan, Letter*, supra* note 179, at 7.

186 Department of the Treasury, Financial Regulatory Reform A New Foundation: Rebuilding Financial Supervision and Regulation, 69-70 (June 17, 2009).

187 Barney Frank, Op-Ed, *Lessons of the Subprime Crisis*, BOSTON GLOBE, Sept. 14, 2007. Congressman Frank made the same point on the floor of the House, *see* Statement of Representative Barney Frank 153 Cong. Rec. H13978 (daily ed. Nov. 15, 2007).

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brief" finding that the Community Reinvestment Act (CRA), which is only applicable to national banks and other insured depository institutions, did not play a significant role in the mortgage crisis because "[t]he predominant players in the subprime market—mortgage brokers, mortgage companies and the Wall Street investment banks that provided the financing—aren't covered under CRA."[188] The issue brief went on to assert that "many banks shifted the most risky lending—the loans at the root cause of this current crisis—to affiliates *to escape CRA requirements and regulatory oversight*."[189]

Prior to the issuance of the issue brief discussed above, the Center for Responsible Lending sponsored a detailed statistical analysis of 1.7 million subprime loans.[190] This analysis found that mortgage brokers accounted for between 63 percent and 81 percent of all subprime loans in 2006.[191] The study characterized these brokers as the "engine of the subprime market,"[192] and argued that although all states license mortgage brokers, licensing alone, without substantive requirements, is inadequate to protect consumers.[193] The report also noted that banks are subject to more intense regulatory and supervisory oversight:

> Despite their integral involvement in mortgage transactions, there is scant regulation of mortgage brokers compared to traditional lenders. While banks, for example, are subject to regular oversight and regulatory examinations that scrutinize the quality and legality of the loans they originate, the regulatory reviews applicable to brokers are largely focused

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188 CENTER FOR RESPONSIBLE LENDING, *CRA is Not to Blame for the Mortgage Meltdown*, at 1 (Oct. 3, 2008).

189 *Id.* (emphasis added).

190 CENTER FOR RESPONSIBLE LENDING, *Steered Wrong: Brokers, Borrowers, and Subprime Loans* (Apr. 8, 2008) (looking at a pool of 3.1 million loans, but after eliminating loans that had incomplete data, the pool was reduced to 1.7 million loans) (on file with the Virginia Law & Business Review Association).

191 *Id.* at 6.

192 *Id.* at 3.

193 *Id.* at 8 ("All states license brokers, but the breadth and depth of state broker regulation varies considerably. . .The typical state licensing regime includes basic requirements like criminal background checks, bonding, and educational or experience requirements. However, without substantive requirements, like a state predatory lending law or statutes that establish affirmative duties of a broker to a borrower, licensing in itself generally does not guard against most abusive lending practices.").

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> on ensuring that brokers meet certain bench marks in order to be licensed.[194]

Further, the report determined that, after matching loans for borrower characteristics, such as FICO scores and geographic area, subprime loans originated by mortgage brokers were significantly more expensive than similar loans made by traditional retail lenders,[195] and that mortgage brokers originated four times the number of negative amortizing loans as traditional lenders and a "disproportionate share" of ARM loans and loans with prepayment penalties.[196]

Allen Fishbein, representing the Consumer Federation of America, has testified that effective regulation of subprime lending is dependent upon the cooperation of state regulators, and suggested that they adopt parallel guidance to that issued by the federal banking agencies. He noted that the participation of state regulators is "particularly crucial for subprime lending, since the lenders and mortgage brokers they supervise and license represent the majority of these originations."[197]

More current statistics support these views. A report accompanying Comptroller Dugan's testimony before the Financial Crisis Inquiry Commission states:

> Using the most reliable data available on nonprime mortgage lending, and accurately accounting for corporate organization and regulatory responsibilities, national banks and their subsidiaries subject to OCC supervision accounted for less than 15 percent of nonprime activity. . . . In contrast, lenders supervised solely by the states accounted for well over half of nonprime lending; combining originations by those lenders with the totals for state-chartered banks reveals

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[194] *Id.* at 6 (noting that North Carolina and a number of other states establish, by statute or common law, affirmative duties that guide brokers' services to borrowers and often direct that brokers must act in the interest of the borrower).

[195] *Id.* at 14-18.

[196] *Id.* at 10-11.

[197] Statement of Allen Fishbein, Director of Housing and Credit Policy, Consumer Federation of America in *Subprime and Predatory Mortgage Lending: New Regulatory Guidance, Current Market Conditions and Effects on Regulated Financial Institutions: Hearing Before the H. Subcommittee on Financial Institutions and Consumer Credit*, 110th Cong. 10 (2007) [hereinafter Fishbein, *Testimony*].

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> that nearly three quarters of nonprime mortgages originated at lenders that were wholly or partly the responsibility of state authorities. . . . Moreover, the data show that subprime mortgages originated by OCC-supervised lenders have performed better than other subprime loans, with lower rates of foreclosure.[198]

This is not to say that national banks did not have a significant part in subprime lending activities in the mid-2000s. Some national banks made poorly underwritten subprime mortgage loans. National banks also played a role in funding loans made by non-bank lenders, through commercial loans, letters of credit, and through the purchase of mortgage-backed securities. Many banks suffered losses as a result of these endeavors.[199] National banks also assisted in the securitization process, for example, by providing liquidity support.[200] However, these types of commercial lending and investment activities were not the subject of state anti-predatory lending laws, which were directed at prohibiting predatory terms and practices in the origination of consumer mortgages.

C. Did Preemption Inhibit State Regulation of Subprime Lenders?

Another issue is whether federal preemption reduced the willingness of the states to adopt restrictions on state regulated mortgage lenders. However, federal preemption does not prevent the states from adopting restrictions that were at least as stringent as those imposed on national banks. Indeed, Alan Fishbein of the Consumer Federation of America urged the states to do just that when he testified before Congress.[201]

In the states that did take action to restrict predatory lending, those actions were often successful. The Center for Responsible Lending found that in the states that adopted significant substantive protections, the state laws were "clearly working to clean up the subprime mortgage market."[202] For example, the study determined that "the proportion of loans in New Mexico with abusive terms was 38.5 percentage points lower than states without

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198 Dugan, *FCIC Testimony*, *supra* note 180, at Appendix B.
199 *Id.* at 9-11.
200 *Id.*
201 Fishbein, *Testimony*, *supra* note 197, at 10.
202 CRL 2006 Paper, *supra* note 148, at 11.

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significant reforms."[203] In 2008, the Pew Charitable Trust released a study that noted that "two thirds of all subprime loan applications are originated by mortgage brokers" but that only four states clearly establish fiduciary duties on brokers.[204] The study encouraged states to expand their role in regulating state licensed mortgage originators.

These studies demonstrate that preemption is not a bar to effective state regulation that can reduce lending abuses. Where states have acted with strong laws, they have been successful in curbing abusive practices.

VI. THE DODD-FRANK ACT PREEMPTION AMENDMENTS TO THE NBA

The Dodd-Frank Act amended the National Bank Act by adding a new section that provides three bases under which a "state consumer financial law"[205] is preempted by the NBA. A "state consumer financial law" must "directly and specifically" regulate the manner, content, or terms and conditions of any consumer financial transaction or account.[206] Under this amendment, the NBA preempts such a state law only if –

> (A) application of a State consumer financial law would have a discriminatory effect on national banks, in comparison with the effect of the law on a bank chartered by that State;
> (B) in accordance with the legal standard for preemption in the decision of the Supreme Court of the United States in Barnett Bank of Marion County, N. A. v. Nelson, Florida Insurance Commissioner, et al., 517 U.S. 25 (1996), the State consumer financial law prevents or significantly interferes with the exercise by the national bank of its powers; and any

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203 *Id.* at 12.

204 Pew Charitable Trusts, *Defaulting on the Dream: States Respond to America's Foreclosure Crisis* 25 (Apr. 2008) www.pewtrusts.org/uploadedFiles/wwwpewtrustsorg/Reports/Subprime_mortgages/defaulting_on_the_dream.pdf.

205 Dodd-Frank Act § 1044, 12 U.S.C.A. § 25b(a)(2) (2010).

206 *Id.* at § 25b(a)(2) (2010). State licensing laws, which regulate the provider of a financial service, but not the transaction itself, would arguably not be considered to be a "state consumer financial law." *See* Cline v. Bank of Am., N.A., 823 F. Supp. 2d 387, 398 (S.D. W. Va. 2011) (holding that a state law prohibiting certain debt collection practices was not a "state consumer financial law" because the law did not "directly and specifically" regulate a financial transaction, but instead regulated debt collection practices).

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> preemption determination under this subparagraph may be made by a court, or by regulation or order of the Comptroller of the Currency on a case-by-case basis, in accordance with applicable law; or
> (C) the State consumer financial law is preempted by a provision of Federal law other than this title 62 of the Revised Statutes.[207]

Each of these preemption grounds are discussed below.

A. Discriminatory Effect

The first ground for preemption is that the state consumer financial law would have a discriminatory *effect* on national banks in comparison with state chartered banks.[208] This is puzzling because by definition a "state consumer financial law" is a law that does not directly or indirectly discriminate against a national bank.[209] A side-by-side comparison of the two provisions illustrates the problem:

Definition of State Consumer Financial Law	**Ground for Preemption of a State Consumer Financial Law**
A state consumer financial law means a state law that: (i) does not directly or indirectly discriminate against national banks, and (ii) directly and specifically regulates the manner, content, or terms and conditions of any financial transaction. . .. . .or any account related thereto, with respect to a consumer.[210]	The NBA preempts a state consumer financial law if application of that law would have a discriminatory effect on national banks, in comparison with the effect of the law on banks chartered by the state.[211]

207 Dodd-Frank Act § 1044, 12 U.S.C.A. § 25b(b)(1) (2010).
208 *Id.*
209 12 U.S.C. § 25b(a)(2) (2010).
210 *Id.*
211 12 U.S.C. § 25b(b)(1)(A) (2010).

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There is no requirement in the definition of a "state consumer financial law" that the discrimination be measured against state banks. Arguably, a state law that directly or indirectly discriminates against a national bank as compared to *any other* provider of financial services is not a state consumer financial law. These laws would be outside the scope of the new preemption rules added by the Dodd-Frank Act. It is not clear why the drafters of this provision also included discrimination as a ground for preemption of a state consumer financial law, because a discriminatory state law cannot be a "state consumer financial law."[212]

B. Barnett Standard

The second basis for preemption is that, "in accordance with the legal standard for preemption in the decision of the Supreme Court of the United States in *Barnett Bank, N.A. v. Nelson*, the state consumer protection law prevents or significantly interferes with the exercise of a national bank of its powers."[213] Opponents of preemption strenuously argue that this creates a new preemption standard, and that preemption is authorized only if the state law can be shown to *actually* prevent or create a "substantial impediment" to the exercise of a national bank power.[214] Our analysis of the language comes to a different conclusion: the legislation basically leaves intact the traditional rules for determining if a state law is preempted. We begin with a discussion of the holding in the *Barnett* case.

1. *The Legal Standard Used by the Supreme Court in* Barnett Bank v. Nelson

Decided by the Supreme Court in 1996, *Barnett Bank v. Nelson* involved a conflict between a Florida law that prohibited banks that are part of a bank holding company from selling insurance, and a federal law that authorizes such sales by national banks in towns of 5,000 or fewer people.[215] The

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212 It is possible that the drafters were distinguishing state laws that have a discriminatory "effect" and state laws that "directly or indirectly" discriminate against national banks. We could find nothing in the legislative history that explains the apparent anomaly.

213 12 U.S.C.A. § 25b(b)(1)(B) (2010); Barnett Bank v. Nelson, 517 U.S. 25 (1996).

214 *See, e.g.*, Wilmarth 2011, *supra* note 9, at 929; J. Elosta, *Recent Development: Dynamic Federalism and Consumer Financial Protection: How the Dodd-Frank Act Changes the Preemption Debate*, 89 N.C. L. REV. 1273, 1299 (May 2011) ("Dodd-Frank requires significant interference, whereas the OCC's 2004 formulation merely required obstruction or impairment.").

215 *Barnett Bank*, 517 U.S. at 28-29 (1996).

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Supreme Court determined that the Florida law was preempted by the federal law.

In reaching this decision, the Court cited with approval a host of prior precedents holding that a state law is preempted if it "hampers" a federal law, "interferes with the purposes" of a federal law, or "stand[s] as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress."[216] The Supreme Court then focused on the Florida law prohibiting banks from engaging in the business of insurance, and rejected the argument that the federal law authorizes such sales, but only when not in conflict with state law. The Court stated that "normally Congress would not want States to forbid, or to impair significantly, the exercise of a power that Congress explicitly granted."[217] The Court held that the Florida law was preempted because it *stood as an obstacle to the accomplishment of the federal purpose* of allowing national banks to sell insurance in small towns. This was the operative finding with respect to the preemption of the Florida law.

Following its holding that the Florida law was preempted, the Supreme Court elaborated on its decision. The Court explained that its decision in *Barnett* did not mean that state law could never apply to a national bank, and gave examples of state laws that were not preempted in prior decisions. During this brief digression, the Court stated that preemption does not deprive states of the power to regulate national banks where doing so does not "prevent or significantly interfere" with the national banks' exercise of their powers.[218] The Court supported this statement by citing cases in which it was held that state law was not preempted when it did not "destroy or hamper" national bank functions, did not "interfere or impair" national banks' efficiency in performing functions, and did not unlawfully "encroach on the rights and privileges of national banks."[219] The logical reading of the case is that the Court intended the phrase "prevents or significantly interferes" to include such concepts as "hamper," "impair the efficiency," and "encroach upon the rights" of national banks.

Significantly, the reference to "prevents or significantly interferes" was an elaboration on the Court's decision, but was not part of the analytic reasoning used by the Court in reaching its decision. Thus, the "prevent or significantly interfere" language was not the holding of the case. The holding was that the

216 *Id.* at 31 (quoting Hines v. Davidowitz, 312 U.S. 52, 67 (1941)).
217 *Id.* at 33.
218 *Id.*
219 *Id.* (citing Anderson Nat'l Bank v. Luckett, 321 U.S. 233, 247-52 (1944)).

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particular state law in question was preempted because it stood as an obstacle to the national bank's authority.[220] This type of discussion, which is not part of the legal reasoning used by a court to make its decision, is *obiter dictum*, and it is not considered to be part of the holding and not given precedential value. The Court has gone so far as to say that it will give no weight to statements made in prior Supreme Court decisions that were mere *obiter dictum*.[221]

This raises an interpretive issue regarding the Dodd-Frank Act language. The statute provides that a state consumer financial law is preempted if "[i]n accordance with the legal standard for preemption . . . in *Barnett Bank* . . . the state consumer protection financial law prevents or significantly interferes with the exercise of a national bank of its powers."[222] However, as noted above, "prevents or significantly interferes" is not the standard applied by the Court in *Barnett Bank*. The statute is therefore ambiguous, and two interpretations are possible. Either Congress used the phrase "prevents or significantly interferes" as a shorthand way to refer to the holding in *Barnett Bank*, and this language was intended to codify the *Barnett Bank* decision, or Congress intended to create a new and narrower preemption standard.

The argument for interpreting the Dodd-Frank Act as establishing a new standard is based on the following three points. First, the phrase "[i]n accordance with the legal standard for preemption in the decision of *Barnett Bank v. Nelson*" is prefatory to the operational language "prevents or significantly interferes," and therefore should not be given the same weight as the actual legislative directive.[223]

Second, establishing a new standard limited to "prevents or significantly interferes" is "in accordance" with *Barnett Bank*, even if it is not the standard used in that case. In other words, Congress is adopting a new standard that is

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220 *Id.* at 31.

221 *E.g.*, Allied Bruce Terminix Cos. v. Dobson, 513 U.S. 265, 296 (1995) (Dissenting opinion by Justices Thomas and Scalia); Centennial Ins. v. Ryder Truck Rental, Inc., 149 F.3d 378 (5th Cir. 1998) ("That which is '*obiter dictum*' is stated only 'by the way' to the holding and does not constitute an essential or integral part of the legal reasoning behind a decision." quoting Charles W. Collier, Precedent and Legal Authority, 1988 WIS. L. REV. 771, 772); U.S. v. Crawley, 837 F.2d 291, 292 (7th Cir. 1988) ("[A] court can determine if a particular passage in an earlier opinion is *dictum* by considering factors such as whether "the passage was unnecessary to the outcome of the earlier case…" or whether the passage can be "sloughed off without damaging the analytical structure of the opinion…."); Allied Bruce Terminix Cos. v. Dobson, 513 U.S. 265 (1995) (dissenting opinion by Justices Thomas and Scalia).

222 12 U.S.C. § 25b(b)(1)(B) (2010).

223 New York v. Federal Energy Regulatory Comm'n, 535 U.S. 1, 22 (2002) (holding that prefatory language does not undermine clear grant of statutory authority).

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consistent with the *dictum* in the *Barnett Bank* decision, even if not the actual holding.

Third, Congress did not have to act in order to maintain the *Barnett Bank* standard, and, therefore, amending the National Bank Act is an indication that Congress wanted to change the law. As stated by the Supreme Court, "[w]hen Congress acts to amend a statute, we presume it intends its amendment to have real and substantial effect."[224] Since no legislative language at all is required to maintain the status quo, the fact that Congress amended the Revised Statutes should be viewed as an indication that a change in law was desired.

We believe, however, that the more persuasive argument is that this section of the Dodd-Frank Act did nothing more than codify *Barnett Bank*. This argument is based both upon the language of the provision, its legislative history, and its consistency with the rules of statutory construction.

2. *Plain Meaning of Statute*

The phrase "[i]n accordance with the legal standard for preemption in the decision of *Barnett Bank v. Nelson*" does not appear in a general "purposes" section or "sense of the Congress" paragraph, but is in the operative text of the statute and should not be ignored. A standard that is different from the holding in *Barnett Bank* is not "in accordance" with that case, and these words would have to be ignored in order to find that a new standard was created. The Supreme Court often has stated that the courts should "give effect, if possible, to every clause and word of a statute."[225] Whether it is in prefatory language or not, it should be given effect, and the use of the phrase in this legislation demonstrates a clear intent not to override the *Barnett Bank* decision.[226]

Second, the argument that Congressional action implies intent to change the law is spurious. Congress frequently enacts legislation that is intended to codify Supreme Court decisions or other cases. For example, in 1950, Congress essentially codified the Supreme Court's decision in the case of *D'Oench, Duhme & Co. v. FDIC*, as part of revisions made to the Federal

224 Stone v. Immigration & Naturalization Serv., 514 U.S. 386, 397 (1995).

225 *See, e.g.*, Montclair v. Ramsdell, 107 U.S. 147, 152 (1883).

226 Reves v. Ernst & Young, 494 U.S. 56, 75 (1990) (holding that the statutory provision must be read in light of the prefatory language preceding it) (concurring opinion by Justice Stevens).

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Deposit Insurance Act.[227] Numerous other examples exist where Congress adopted legislation that codifies case law.[228]

Additionally, there are many instances where the courts have held that Congress was merely codifying prior judicial opinions, even though the words used in the statute are not even the same as the words used in the case law. In *Graham v. John Deere Co.*, the Supreme Court reviewed the legislative history of certain amendments to the patent laws that paraphrased prior judicial decisions, and concluded that the amendments did not change the legal standards established by those cases, even though the statutory language on its face would have had a different result.[229] More recently, the Supreme Court found that an amendment to the Patent Act should be viewed as a codification of prevailing judicial precedents, relying in large measure on the legislative history of the amendment.[230]

3. Legislative History

The genesis of the Dodd-Frank Act may be found in the legislative proposal for financial reform developed by the Administration in 2009, and submitted to Congress on June 17 of that year.[231] The Administration's proposal would have eliminated NBA preemption for state consumer protection laws.[232] This treatment of preemption was ultimately not accepted by either the House of Representatives or the Senate.

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[227] 12 U.S.C. § 1823(e). *See* Hood v. Resolution Trust Corp., 21 F.3d 1121 (10th Cir. 1994) ("12 U.S.C. 1823(e) is a codification of the *D'Oench Duhme* doctrine . . . ."); Resolution Trust Corp. v. Juergens, 965 F.2d 149, 150 (7th Cir. 1992). Some courts take the position that the legislative language is narrower than the holding in the case. *See* J. Kellog, *D'Oench Lives: But For How Long?: The Eleventh Circuit Breathes Life into an Ailing Banking Doctrine*, 30 FLA. ST. U. L. REV. 167, 183-84 (2002).

[228] *E.g.*, 19 U.S.C. § 1451 (codifying United States v. Meyers, 320 U.S. 561 (1944)); 21 U.S.C. § 387a-1 (directing appropriate regulatory amendments to be in conformance with Lorillard Tobacco Co. v. Reilly, 533 U.S. 525 (2001)); 25 U.S.C. § 640d (codifying Healing v. Jones, 210 F. Supp. 125 (D. Ariz. 1962), *aff'd*, 373 U.S. 758 (1963)).

[229] Graham v. John Deere Co., 383 U.S. 1, 15-17 (1966).

[230] Bilski v. Kappos, 130 S. Ct. 3218, 3231 (2010) (Stevens, J., Ginsburg, J., Breyer, J., Sotomayor, J., concurring).

[231] U.S. DEP'T. OF THE TREASURY, "FINANCIAL REGULATORY REFORM: A NEW FOUNDATION" 61 (2009). The Treasury Department's suggestion was incorporated as section 143 of the Consumer Financial Protection Agency Act of 2009, introduced by Representative Frank on July 8, 2009, H.R. 3126, 111th Cong. 1st Sess. § 143 (2009).

[232] *Id.*

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On December 2, 2009, then-House Financial Services Committee Chairman Barney Frank introduced a modified version of the Treasury proposal as H.R. 4173, the Wall Street Reform and Consumer Protection Act.[233] The bill provided that the OCC could preempt a state consumer financial law if the agency found that the law "prevents or significantly interferes with the ability of . . . [a] national bank to engage in the business of banking."[234] No reference was made to *Barnett Bank*. The bill also included a requirement that, in order to make a preemption determination under this standard, the OCC had to make a finding, in writing and after consulting with the Consumer Financial Protection Bureau, that another federal law provided a "substantive standard" regulating the conduct at issue.[235]

During House floor consideration, a successful amendment, principally authored by Representative Melissa Bean,[236] modified the bill to authorize NBA preemption if a state consumer financial law "prevents, significantly interferes with, or *materially impairs* the ability" of a national bank to engage in the business of banking.[237] Representative Bean explained that the addition of the words "materially impairs" was intended to establish a preemption standard that will "more accurately reflect the Supreme Court Case of *Barnett Bank v. Nelson*, which established the preemption standard currently applied to national banks."[238] She elaborated that, while the phrase "prevents or significantly interferes with" was a "shorthand" expression for the *Barnett Bank* case, it could be construed more narrowly. Therefore, she added the additional language to make sure that there would be "no question" that *Barnett Bank* would still apply to preemption under the NBA.[239]

The legislation reported by the Senate Banking Committee provided that a state consumer financial law would be preempted "in accordance with the legal standard of the decision of the Supreme Court of the United States in *Barnett Bank v. Nelson*."[240] The Senate Banking Committee report associated with the legislation clearly indicates that the Committee was under the impression that the 2004 OCC regulation went beyond the preemption

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233 H.R. 4173, 111th Cong. (as introduced to House Dec. 2, 2009).
234 *Id.* at § 4404.
235 *Id.*
236 155 CONG. REC. E3029 (daily ed. Dec. 16, 2009),155 CONG. REC. E3029 (2009).
237 H.R. 4173 111th Cong. § 4404 (as passed by House, 1st Sess. (2009) (emphasis added)).
238 155 CONG. REC. E3029 (daily ed. Dec. 16, 2009).
239 *Id.*
240 S. 3217 111th Cong. § 1044 2d Sess. (as reported by the Senate Banking Committee on Apr. 15, 2010).

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standard recognized by the Supreme Court in *Barnett Bank*. The bill was intended to restore the conflict preemption standard described in *Barnett Bank*:

> Section 1044 amends the National Bank Act to clarify the preemption standard relating to State consumer financial laws as applied to national banks. . . . *The standard for preempting State consumer financial law would return to what it had been for decades, those recognized by the Supreme Court in Barnett Bank v. Nelson . . . undoing broader standards adopted by rules, orders, and interpretations issued by the OCC in 2004.*
> Specifically, this section sets out the three circumstances under which a State consumer financial law can be preempted: (1) when the State law would have a discriminatory effect on national banks or federal thrifts in comparison with the effect of the law on a bank or thrift chartered in that State; (2) *if the State law, as described in the standard established by the Supreme Court in Barnett, "prevents or significantly interferes with a national bank's exercise of its power;"* or (3) the State law is preempted by another Federal law.[241]

During floor consideration of this the bill, Senator Carper, joined by Senators Johnson, Bayh and Warner, offered a substitute amendment for the Committee's preemption section. The amendment, which passed by a vote of eighty to eighteen,[242] retained the Committee's language on the preemption standard ("in accordance with the legal standard of the decision of the Supreme Court of the United States in *Barnett Bank*"),[243] but deleted the requirement that the OCC make a written finding that federal law provided a substantive standard regulating the activity or conduct at issue.

The conference committee reported back a modified version of the Senate language, which was enacted into law.[244] The Conference accepted the Senate version as amended by Senator Carper, with the addition of the phrase "prevents or significantly interferes" after the reference to the *Barnett* case. The conference report specifically refers to this compromise as codifying

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241 SEN. REP. NO. 111-176, 175-76 (2010) (emphasis added).
242 156 CONG. REC. S3872 (daily ed. May 18, 2010).
243 156 CONG. REC. S3916-17 (daily ed. May 18, 2010).
244 H.R. REP. NO. 111-517 (2010) (Conf. Rep.).

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Barnett Bank.[245] During Senate consideration of the conference report, Senator Carper and Senator Dodd, then-Chairman of the Senate Banking Committee, entered into the following exchange about the preemption standard:

> Mr. CARPER. Mr. President, I am very pleased to see that the conference committee on the Dodd-Frank Wall Street Reform and Consumer Protection Act retained my amendment regarding the preemption standard for State consumer financial laws with only minor modifications. I very much appreciate the effort of Chairman Dodd in fighting to retain the amendment in conference.
> Mr. DODD. I thank the Senator. As the Senator knows, his amendment received strong bipartisan support on the Senate floor and passed by a vote of 80 to 18. It was therefore a Senate priority to retain his provision in our negotiations with the House of Representatives.
> Mr. CARPER. One change made by the conference committee was to restate the preemption standard in a slightly different way, but my reading of the language indicates that the conference report still maintains the *Barnett Bank* standard for determining when a State law is preempted.
> Mr. DODD. The Senator is correct. That is why the conference report specifically cites the Barnett Bank . . . case. There should be no doubt that the legislation codifies the preemption standard stated by the U.S. Supreme Court in that case.
> Mr. CARPER. I again thank the Senator. This will provide certainty to everyone—those who offer consumers financial products and to consumer [*sic*] themselves.[246]

Codifying the existing conflict preemption standard, as explained in *Barnett Bank*, would establish "certainty." Adopting a different standard would have the opposite effect. This understanding was also held by Senator

245 *Id.* at 875.

246 156 CONG. REC. S5902 (daily ed. July 15, 2010).

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Johnson, the current Chairman of the Senate Banking Committee, who stated the following during the debate:

> One change made by the conference committee was to restate the preemption standard in a slightly different way, but it is clear that this legislation is codifying the preemption standard expressed by the U.S. Supreme Court in [the] *Barnett Bank* . . . case. This will provide certainty to consumers and those that offer consumers financial products.[247]

In July 2011, Senators Carper and Warner wrote a letter to Treasury Secretary Geithner stating their disagreement with the Treasury Department's assertion[248] that the Dodd-Frank Act established a new preemption standard:

> [W]e were the sponsors of the Senate amendment . . . and were involved in the negotiations on preemption during the conference committee. While we understand that the position of the Administration was to eliminate federal preemption for national banks, the fact is that Congress did not accept that position. Our amendment maintaining the Barnett standard passed the Senate by an overwhelming vote of 80 to 18. Both the language of the final law and its legislative history clearly demonstrate that the Barnett standard is maintained, and the Treasury position . . . was, in fact, rejected by Congress.[249]

While the courts often discount post-enactment legislative history such as this letter,[250] it confirms that the pre-enactment legislative history is an accurate reflection of the views of the authors of the provision.

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247 156 CONG. REC. S5,889 (daily ed. July 15, 2010).

248 Madison Letter, *supra* note 12.

249 Letter from Thomas R. Carper and Mark R. Warner, Senators to Timothy Geithner, U.S. Secretary of the Treasury (July 8, 2011), *available at* http://www.politico.com/static/PPM170_110707_treasurypreemption.html.

250 *See, e.g.*, Bruesewitz v. Wyeth, Inc., 131 S. Ct. 1068, 1081 (2011); Jones v. United States, 526 U.S. 227, 238 (1999).

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4. *Relevance of the Gramm-Leach-Bliley Act*

The wording for the Dodd-Frank Act preemption standard is clearly borrowed from the standard regarding NBA preemption of state restrictions on national bank insurance sales activities found in the Gramm-Leach-Bliley Act (GLBA). Section 104 of GLBA provides that:

> In accordance with the legal standards for preemption set forth in the decision of the Supreme Court of the United States in *Barnett Bank of Marion County, N.A. v. Nelson, 517 U.S. 25* . . . (1996), no State may . . . prevent or significantly interfere with the ability of a depository institution . . . to engage . . . in any insurance sales, solicitation, or crossmarketing activity.[251]

To clarify that the "prevent or significantly interfere" standard in GLBA was intended as a codification of *Barnett*, a provision was added that states: "[n]othing in this paragraph shall be construed . . . to limit the applicability of the decision of the Supreme Court in *Barnett Bank*."[252] Further, the Senate Banking Committee report associated with this legislation states that the "prevent or significantly interfere" standard is a codification of the *Barnett Bank* decision and all of the case law embodied in that decision.[253] And the conference report accompanying GLBA also states that the preemption standard for state insurance sales laws was the standard set forth in the *Barnett Bank* case.[254]

This legislative history strongly supports the position that Congress used the phrase "prevent or significantly interfere" as shorthand to codify the entire *Barnett Bank* case in the Gramm-Leach-Bliley Act, and this

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251 15 U.S.C. § 6701(d)(2)(A) (Supp. 2011). Not only is the legislative language almost word for word the same, but the Dodd-Frank Act chose to ignore more recent Supreme Court preemption cases involving the NBA and instead invoked the *Barnett* case. If the intent to duplicate the Gramm-Leach-Bliley Act was not the motivating reason, it would have made more sense for Congress to reference a more recent Supreme Court statement on the preemptive power of the NBA, such as Watters v. Wachovia Bank, N.A., 550 U.S. 1 (2007) or Cuomo v. Clearing House Ass'n, 557 U.S. 519 (2009).

252 15 U.S.C. § 6701(d)(2)(C)(iii) (Supp. 2011).

253 S. REP. NO. 106-44, at 13 (1999).

254 H.R. REP. NO. 106-434, at 156-57 (1999).

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interpretation is consistent with the GLBA case law.[255] Therefore, it is logical to presume that Congress had the same intent when it inserted almost the exact same language in the Dodd-Frank Act. This is especially persuasive in light of the fact that the same Congressional Committees were chiefly responsible for both the Gramm-Leach-Bliley Act and the Dodd-Frank Act.

5. The Barnett Bank *Standard is Consistent with existing statutory provisions and case law*

The statutory language of the judicial review section of the Dodd-Frank Act amendment directly supports the view that a codification of *Barnett Bank* was intended. Section 1044 of the Dodd-Frank Act states that a regulation or order issued by the Comptroller preempting a state law should be upheld by a court only if "substantial evidence, made on the record of the proceeding, supports the specific finding regarding the preemption of such provision in accordance with the legal standard of the decision of the Supreme Court of the United States in *Barnett Bank*."[256] It would be illogical for a court to review the sufficiency of an OCC preemption decision for compliance with *Barnett Bank* if the applicable standard for making that determination is not also *Barnett Bank*.

Moreover, the principles of statutory interpretation support the view that Dodd-Frank codified *Barnett Bank*. The courts have repeatedly disfavored statutory interpretations that would result in the implicit reversal of judicial decisions. As stated by the Supreme Court, "[t]he normal rule of statutory construction is that if Congress intends for legislation to change the interpretation of a judicially created concept, it makes that intent specific."[257] The Supreme Court has held that when Congress wants to override a judicial concept, its "intention would be clearly expressed, not left to be collected or inferred."[258] In making this determination, the courts will pay close attention to the legislative history of the provision.[259]

Recent case law also supports this view, consistently treating the Dodd-Frank Act as leaving the *Barnett Bank* preemption standard unchanged. In

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[255] *See, e.g.*, Association of Banks in Ins. v. Duryee, 270 F.3d 397, 409 (6th Cir. 2001) (interpreting the Gramm-Leach-Bliley Act's preemption statutory language to include the *Barnett* factors "hamper" and "interfere with or impair national bank's efficiency").

[256] Dodd-Frank Act § 1044, 12 U.S.C. § 25b (Supp. 2011).

[257] Noland v. United States, 517 U.S. 535, 539 (1996).

[258] Kelly v. Robinson, 479 U.S. 36, 47 (1986)(citation omitted).

[259] Henning v. Union Pac. R.R. Co., 530 F.3d 1206, 1216 (10th Cir. 2008).

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Baptista v. JP Morgan Chase Bank, N.A.,[260] the Court of Appeals for the Eleventh Circuit reviewed a state law that prevents a national bank from charging a check cashing fee to non-account holders.[261] The court concluded that, "under the Dodd-Frank Act, the proper preemption test asks whether there is a significant conflict between the state and federal statutes—that is, the test for conflict preemption."[262] The court then applied the conflict preemption principles discussed in *Barnett Bank* to its facts, and held that the state law was preempted because it was in "substantial conflict" with OCC regulations.[263]

In *Cline v. Bank of America*,[264] the U.S. District Court for the Southern District of West Virginia held that the appropriate preemption standard under the Dodd-Frank Act amendments to the NBA was the conflict preemption standard described in *Barnett Bank*. In *U.S. Bank National Association v. Schipper*, the U.S. District Court for the Southern District of Iowa specifically rejected the argument that the Dodd-Frank Act applies a more stringent preemption standard, stating instead that "the Dodd-Frank Act did not materially alter the standard for preemption."[265]

And in *Parks v. MBNA America Bank*,[266] the Supreme Court of California held that a state disclosure law was preempted by the National Bank Act, interpreting the Dodd-Frank Act language as a codification of the *Barnett Bank* case and the traditional preemption principles discussed therein.

In sum, it appears clear that the Dodd-Frank Act did not modify the traditional legal standards for determining if state law is preempted, and that the legislation simply codifies the *Barnett Bank* case.

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260 Baptista v. JP Morgan Chase Bank, N.A., 640 F.3d 1194 (11th Cir. 2011).

261 The Dodd-Frank Act preemption amendment to the NBA was not in effect until July 21, 2011, and thus the court use of that standard was premature. This does not diminish the value of the decision in providing the court's interpretation of the language.

262 *Baptista*, 640 F.3d at 1197.

263 The court also relied on the Fifth Circuit opinion in *Wells Fargo Bank, N.A. v. James*, 321 F.3d 488, 491 (5th Cir. 2003). This case pre-dated the Dodd-Frank Act, and the Eleventh Circuit's reliance on it is another indication that it did not view the new language as changing the preemption standard.

264 Cline v. Bank of Am., N.A., 823 F. Supp. 2d 387 (S.D. W. Va. 2011).

265 United States Bank Nat'l Ass'n v. Schipper, 812 F. Supp. 2d 963, 969 n.1 (S.D. Iowa 2011).

266 54 Cal. 4th 376, 385, 393, 278 P.3d 1193, 1198, 1204 (2012).

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C. Preemption Pursuant to Other Federal Law

The third basis for finding preemption of a state consumer financial law is that the law is preempted by a provision of federal law other than Title LXII of the Revised Statutes.[267] Title LXII of the Revised Statutes is a codification of the NBA. It governs the organization and powers of national banks, the establishment of the Office of the Comptroller of the Currency, the regulation of the business of national banks, and the authority to dissolve these banks and place them into receivership. Title LXII authorizes national banks to "carry on the business of banking" and to engage in activities "incidental" thereto.[268] It also includes the authority to operate branches,[269] take deposits,[270] and make commercial loans.[271]

However, the NBA is not the sole source of national bank power. National bank authority to sell insurance in towns with a population of 5,000 or fewer is based on section 13 of the Federal Reserve Act,[272] and national bank trust powers are based on a provision in freestanding legislation enacted in 1962.[273] Perhaps most significantly, the authority of a national bank to make mortgage loans is not found in Title LXII, but in section 24 of the Federal Reserve Act.[274] Thus, by the very terms of the Dodd-Frank Act, national bank mortgage lending activities (conducted directly by the bank) are not covered by the preemption amendment to the NBA.[275]

The conclusion that mortgage lending authorized under section 24 of the Federal Reserve Act (and conducted directly by a national bank) is not covered by the preemption standard in the Dodd-Frank Act is buttressed by the fact that other provisions in the Dodd-Frank Act specifically refer to section 24 of the Federal Reserve Act.[276] As is discussed below, the Dodd-

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[267] Dodd-Frank Act § 1044, 12 U.S.C. § 25b (2011).

[268] 12 U.S.C. § 24 (2011).

[269] 12 U.S.C. § 36 (2011).

[270] 12 U.S.C. § 24 (2011).

[271] *Id.*

[272] 12 U.S.C. § 92 (2006).

[273] National Bank Act of 1962, Pub. L. No. 87-722, 76 Stat. 668 (pointing to the fact that prior to 1962, trust powers were authorized by the Federal Reserve Act).

[274] 12 U.S.C. § 371 (2006).

[275] As a matter of agency discretion, the OCC may choose to comply with Dodd-Frank Act provisions when considering the relationship of state law to mortgage lending, even if not required by the statutory language.

[276] *E.g.*, Dodd-Frank Act § 1044, 12 U.S.C. § 25b (2010) ("Title 62 of the Revised Statutes and section 371 of this title do not . . . affect the applicability of any State law to any subsidiary or affiliate of a national bank . . . .").

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Frank Act states that neither Title LXII *nor section 24 of the Federal Reserve Act* preempts the application of state law to national bank subsidiaries, affiliates, and agents. Since there is no comparable reference to section 24 of the Federal Reserve Act when discussing the application of state law directly to national banks, the legislation, by its terms, does not affect the preemptive effect of section 24 with respect to national bank activities.[277]

VII. OTHER SIGNIFICANT DODD-FRANK PROVISIONS RELATING TO PREEMPTION

A. National Bank Subsidiaries and Agents

There are three separate and inconsistent subsections that deal with the applicability of state law to national bank subsidiaries, agents, and affiliates.[278]

Under the first provision, the NBA and section 24 of the Federal Reserve Act do not "preempt, annul, or affect the applicability of *any* State law to any subsidiary or affiliate of a national bank."[279] This provision applies to *any* state law, not just "state consumer financial laws." [280] Read literally, this section does not take into consideration state laws that discriminate against national banks' subsidiaries or affiliates. A state law could prohibit a national bank from using a subsidiary to engage in any activity within that state, but allow state bank subsidiaries to engage in that activity.[281] A state law could, of course, be preempted by other federal laws.

The second provision establishes a different rule for state consumer financial laws:

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[277] Some may argue that the omission of a reference to section 24 in connection with the activities of a bank itself (as opposed to a subsidiary, affiliate, or agent) was a drafting error. However, even if a court believes that this was an oversight by Congress, it is well-established that the courts will not correct a drafting error and instead will apply the statute as written. *See, e.g.*, Lamie v. United States Tr., 540 U.S. 526, 542 (2004) ("If Congress enacted into law something different from what it intended, then it should amend the statute to conform it to its intent. 'It is beyond our province to rescue Congress from its drafting errors . . . .'").

[278] The inclusion of both national bank subsidiaries and affiliates in the statute is confusing, since, under the NBA, only banks and direct subsidiaries are subject to OCC preemption.

[279] 12 U.S.C. § 25b(b)(2) (2010) (emphasis added). It is not clear why the term "affiliate" was included, since affiliates (that are not also subsidiaries) are not within the scope of national bank preemption.

[280] *Id.*

[281] Since this "anti-preemption" provision preserves *any* state law, it would preserve commercial regulations as well as consumer laws.

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> Notwithstanding any provision of [the NBA] or section 371 of this title, a State consumer financial law shall apply to a subsidiary or affiliate of a national bank . . . to the same extent that the State consumer financial law applies to any person, corporation, or other entity subject to such State law.[282]

This provision differs from the first subsection in that it deals only with state consumer financial laws rather than with all state laws. By stating that the state law "*shall apply* to a subsidiary or affiliate . . . to the same extent that the State consumer financial law applies to *any* person, corporation, or other entity,"[283] it also mandates the application of certain state laws to subsidiaries and affiliates of national banks, even if the state does not intend that effect. Under the terms of this provision, even state laws only intended to apply limitations on a certain class of lenders, such as pawn shops or payday lenders, will apply to national bank subsidiaries.

Further, if a state law is intended to exempt a class of lenders, such as community credit unions, from particular regulatory limitations, the exemption would also apply to national bank subsidiaries and affiliates by operation of this provision.

One can envision that these two Dodd-Frank Act amendments could lead to conflicting results. This first amendment provides that the NBA and section 24 of the Federal Reserve Act do not preempt state law. Thus, if a state law provides that a national bank subsidiary may not make automobile loans, that law is protected. Under the second provision, state law applicable to any lender is automatically applicable to national bank subsidiaries. Therefore, state authorization for finance companies to make automobile loans would be automatically applicable to national bank subsidiaries. As a result, there would be a direct conflict between these two sections.

The third provision is almost identical to the first, except that the third provision includes agents.[284] It states that no provision of the NBA or section 24 of the Federal Reserve Act shall be construed as preempting, annulling, or affecting the applicability of state law to any subsidiary, affiliate, or *agent* of a national bank. It differs from the first subsection in two respects:

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282 12 U.S.C. § 25b(e) (2010).
283 *Id.* (emphasis added).
284 12 U.S.C. § 25b(h) (2010).

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(i) it includes agents, and (ii) it does not use the phrase "any state law" but instead refers to "state law." There is no explanation as to why Congress decided to add a third provision, rather than simply adding the word "agent" to the first subsection. The application of all state laws to national bank agents may be particularly significant in the context of automobile loans and similar consumer product financing transactions, which are often initiated by a sales organization acting as the agent for a national bank lender when the consumer product is purchased.[285]

While it is hard to predict how a court will interpret these three subsections, it would appear that, at the very least, the preemption standards that apply to a national bank will no longer apply to a bank's subsidiary or agent. However, as a practical matter, the impact of the change with respect to subsidiaries can be mitigated. A national bank wishing to avoid compliance with preempted state law can merge a subsidiary into the parent bank, and thereby gain the benefit of OCC preemption for the subsidiary's activities, now conducted directly by the bank. The impact on agents may be greater. For example, some national banks make automobile loans by using car dealers as the banks' agents for purposes of offering the loans. These national banks will no longer be able to rely on preemption to overcome state laws that effectively prohibit this practice.

B. Case-by-Case Requirement

The Dodd-Frank Act amendment provides that, when the OCC makes a preemption determination under the *Barnett* standard, the agency may act by regulation or order on a case-by-case basis.[286] The term "case-by-case" is defined as a determination made by the Comptroller concerning the impact of a particular state consumer financial law or the law of any *other* state with "substantively equivalent" terms.[287] When making a determination that the law of the second state has substantively similar terms, the Comptroller must

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[285] Independent contractors (who do not become bank agents for purposes of initiating a financial transaction) will not be affected by these provisions, and these contractors will remain subject to state law to the same extent as they currently are. By and large, independent contractors are currently subject to state law.

[286] 12 U.S.C. § 25b(b)(1)(B) (2010) (the statute uses the verb "may," which leaves open the possibility that the OCC could also make preemption determinations by other means. For purposes of this report, we will assume that the OCC is required to make preemption determinations by regulation or order on a case-by-case basis).

[287] 12 U.S.C. § 25b(b)(3)(A) (2010)

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first consult with the Bureau of Consumer Financial Protection.[288] A court considering a preemption issue is not subject to this requirement. The Senate report associated with this language explains that the term "case-by-case" permits the OCC to make a single determination concerning multiple states' consumer financial laws, so long as the laws contain substantively equivalent terms.[289]

While the OCC may determine that similar laws in other states are preempted, this section does not explicitly provide the OCC with authority to determine that similar laws in the *same* state are preempted. To avoid this illogical result, a court may determine that the OCC has some limited authority to define a type or class of laws in any state as being preempted, thereby removing restriction of the OCC's action in the first state to one particular law. For example, if the OCC is considering a state law that prohibits a national bank from advertising the availability of its insurance agency services, the OCC may be able to issue a regulation declaring that any state law that prevents a bank from advertising any of its products is preempted.

Further, even if the OCC is limited to specific law-by-law determinations, each determination will have precedential effect. Therefore, a national bank or a court could reasonably rely on the reasoning given in a particular OCC preemption determination and apply that reasoning to analogous law. Using the prohibition on advertising insurance services as an example, an OCC determination preempting that specific law, based on the principle that a state may not prevent a national bank from advertising its products, could be used reasonably by a national bank or court to determine that state laws generally limiting advertisements are preempted.

C. Dodd-Frank Amendments Do Not Apply Prior to July 21, 2011

Section 1048 of the Dodd-Frank Act provides that the effective date of Title X of the Act, which includes the preemption amendment to the NBA, is the "designated transfer date," which was July 21, 2011.[290] Pursuant to this section, the Sixth Circuit Court of Appeals held that the preemption amendment does not apply to transactions entered into prior to July 21,

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[288] 12 U.S.C. § 25b(b)(3)(B) (2010).

[289] S. REP. NO. 111-176, 111th Cong. 2d Sess. at 176 (2010).

[290] Dodd-Frank Act § 1048, 12 U.S.C. 5551 (2010); Designated Transfer Date, 75 Fed. Reg. 57252 (Sept. 20, 2010) (designating July 21, 2011).

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2011.[291] Most of the lower courts that have considered this question have come to the same conclusion.[292]

However, one district court[293] has taken the position that the Dodd-Frank Act amendment is retroactive to July 21, 2010, the date of enactment. The basis for this position is section 1043 of the Act, which provides that the Dodd-Frank Act preemption amendments shall not affect the applicability of any OCC regulation, order, guidance, or interpretation regarding the applicability of state law to any contract entered into prior to July 21, 2010 (the date of enactment).[294] This section provides a corresponding "grandfather" provision for contracts entered into by savings associations regulated by the Office of Thrift Supervision (OTS). [295]

The logical interpretation of this grandfather provision is that it is identifying a finite group of contracts that will not be affected by any changes to preemption that may occur after July 21, 2011; for example, due to the fact that preemption will no longer apply to national bank subsidiaries and agents, or that the "occupation of the field" theory will no longer be applicable to federal savings associations. This interpretation is consistent with the Act's legislative history.[296]

The courts that have looked at this issue have come to different conclusions. As noted above, the Sixth Circuit and most of the lower courts have held that the Dodd-Frank Act does not apply to transactions occurring

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[291] Molosky v. Washington Mut., 664 F.3d 109, 113 (6th Cir. 2011) ("[The preemption] provisions came into effect on July 21, 2011, and have no retroactive effect with regard to the issues in this appeal.").

[292] *E.g.*, Williams v. Wells Fargo Bank, N.A., No. 11-21233, 2011 WL 4901346, at *13 (S.D. Fla. Oct. 14, 2011); Davis v. World Sav. Bank, FSB, 806 F. Supp. 2d 159, 172 (D.D.C. 2011).

[293] Settle v. World Sav. Bank, F.S.B., No. ED CV 11-00800 MMM, 2012 WL 1026103, at *14-15 (C.D. Cal. Jan. 11, 2012) (complaint dismissed).

[294] Dodd-Frank Act § 1043, 12 U.S.C. 5553 (2010).

[295] *Id.* ("This subchapter, and regulations, orders, guidance, and interpretations prescribed, issued, or established by the Bureau, shall not be construed to alter or affect the applicability of any regulation, order, guidance, or interpretation prescribed, issued, and established by the Comptroller of the Currency or the Director of the Office of Thrift Supervision regarding the applicability of State law under Federal banking law to any contract entered into on or before July 21, 2010, by national banks, Federal savings associations, or subsidiaries thereof that are regulated and supervised by the Comptroller of the Currency or the Director of the Office of Thrift Supervision, respectively.").

[296] S. REP. NO. 111-176, at 175 (2010) (intending that section 1043 "provide[s] stability to existing contracts" by preserving the applicability of OCC and OTS preemptive rulings to contracts that were made before the enactment date of Dodd-Frank).

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prior to July 21, 2011.[297] However, one recent case held that the Dodd-Frank preemption language became effective as of the date of enactment, noting that section 1043 protects contracts in existence on or before such date.[298] The court cited *Copeland-Turner v. Wells Fargo Bank*[299] to support this conclusion; however, the court's reliance on this case appears to be misplaced. In context, the *Copeland-Turner* opinion was only discussing the applicable date to determine if a contract is grandfathered:

> Section 1043 of the Act makes clear that the Act does not apply to contracts entered into before the Act's enactment. . . . The Act was effective July 21, 2010. Under section 1043, any contracts entered into on or before that date are not subject to the new legislation.[300]

Read in this light, it is clear that the *Copeland-Turner* case was not making a statement regarding the effective date of the Dodd-Frank Act generally, but instead was explaining that section 1043 was using the date of enactment to identify grandfathered contracts.

D. Periodic Review

The Comptroller is directed to review, through a notice and comment procedure, each preemption determination.[301] The review is to take place within the five-year period following the determination, and at least once during the succeeding five-year period. After conducting the review, the agency is to publish its decision to continue or rescind the preemption determination. Any decision to amend the determination must first be published for comments in the Federal Register. Any decision to rescind the preemption determination does not have to be published for comment. Additionally, the OCC must publish and update, at least quarterly, a list of all preemption determinations.[302]

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[297] *See Molosky*, 664 F.3d at 113; *Williams*, 2011 WL 4901346, at *13; *Davis*, 806 F. Supp. 2d at 172.

[298] *Settle*, No. ED CV 11-00800 MMM, 2012 WL 1026103, at *14.

[299] Copeland-Turner v. Wells Fargo Bank, 800 F. Supp. 2d 1132, 1137-38 (D. Or. 2011).

[300] *Id.*

[301] 12 U.S.C. § 25b(d) (2010).

[302] 12 U.S.C. § 25b(g) (2010).

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E. Occupation of the Field

The Dodd-Frank Act amendment provides that the NBA "does not occupy the field in any area of State law."[303] A similar amendment was made to the Home Owners' Loan Act, applicable to federal savings associations.[304] The NBA has never been construed to occupy the field of banking regulation,[305] and the OCC has never taken that position.[306] Thus, the impact of this provision on national bank preemption is nil. Whether it has an impact on preemption for federal savings associations is beyond the scope of this article.

VIII. JUDICIAL REVIEW

The Dodd-Frank Act amendment states that a court should not uphold an OCC preemption determination under the "prevents or significantly interferes" standard, unless substantial evidence made on the record of the proceeding supports the requisite findings in accordance with the legal standard in *Barnett Bank*.[307] Under the Administrative Procedure Act (APA), rulemakings and other determinations are typically reviewed under one of two standards: (i) the "substantial evidence" standard, or (ii) the "arbitrary [or] capricious" standard.[308] Typically, but not always, the "substantial evidence" test is used when reviewing agency actions that are predicated on facts developed through a formal hearing.[309] Notice and comment rulemaking and agency opinion letters and other determinations traditionally are not subject to review under substantial evidence, but rather under the arbitrary and

303 12 U.S.C.A. § 25b(b)(4) (2010) (referencing 62 R.S. § 5136C).

304 Dodd-Frank Act § 1046, 12 U.S.C.A. § 1465(b) (2010).

305 Aguayo v. United States Bank, 653 F.3d 912, 921-22 (9th Cir. 2011) ("The OCC has explicitly avoided full field preemption in its rulemaking and has not been granted full field preemption by Congress.").

306 *Id.* at 922.

307 12 U.S.C.A. § 25b(c) (2010) (quoting § 25b(b)(1)(B)).

308 5 U.S.C. § 706(2) (2006) (the Administrative Procedure Act provides six bases for setting aside agency action, but the "substantial evidence" standard and the "arbitrary [or] capricious" standard are the most common bases for rejecting agency determinations).

309 5 U.S.C. §§ 556, 557 (2006) (stating that a formal hearing is one in which parties are permitted to submit oral and written statements, have the right to cross-examine witnesses, the hearing is presided over by an impartial decision-maker, and the decision is based on the record developed at the hearing).

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capricious standard.[310] These alternative standards are discussed further below.

A. Arbitrary and Capricious Standard

The arbitrary and capricious standard provides that a reviewing court shall hold unlawful and set aside agency actions, findings and conclusions that are "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law."[311] This standard requires an agency to examine the relevant data and articulate a satisfactory explanation for its action, including a rational connection between the facts found and the choices made.[312] In reviewing that explanation, a court must consider whether the decision was based on a consideration of the relevant factors and whether there has been a clear error of judgment. In general,

> [A]n agency rule is arbitrary and capricious if the agency has relied on factors which Congress has not intended it to consider, entirely failed to consider an important aspect of the problem, offered an explanation for its decision that runs counter to the evidence before the agency, or is so implausible that it cannot be ascribed to a difference in view or the product of agency expertise.[313]

The focal point for judicial review under the arbitrary and capricious standard is "the administrative record already in existence, not some new record made initially in the reviewing court."[314] However, since there is no formal hearing, any evidence that was put before the decision-maker may be used to justify the agency's determination.

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310 Camp v. Pitts, 411 U.S. 138 (1973) (holding that the substantial evidence test was inappropriate for court review of OCC determinations, and that the arbitrary and capricious standard was to be used instead).

311 5 U.S.C. § 706(2)(A).

312 Motor Vehicles Mfrs. v. State Farm Mut. Auto. Ins., 463 U.S. 29 (1983).

313 *Id.* at 43.

314 *Camp*, 411 U.S. at 142.

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B. Substantial Evidence Standard

The APA states that formal rulemaking (which requires a factual on the record hearing, unlike notice and comment rulemaking) and other determinations required to be made on the basis of a formal hearing may be set aside if the agency's action is unsupported by substantial evidence.[315] Substantial evidence is "more than a mere scintilla; it must be such relevant evidence as a reasonable mind might accept as adequate to support a conclusion."[316] Evidence is not substantial to the extent it is overwhelmed by other evidence, or if the evidence constitutes mere conclusion. If an agency's decision is supported by substantial evidence, the agency's "determination must stand regardless of whether the reviewing court would resolve the issues of fact in dispute differently."[317] As one court of appeals noted, "[s]ubstantial evidence review gives the agency the benefit of the doubt, since it requires not the degree of evidence which satisfies the court that the requisite fact exists, but merely the degree which could satisfy a reasonable fact finder."[318] Under the substantial evidence test, the scope of the review is limited to the factual record generated in the formal hearing.

C. Application of Substantial Evidence Test to Preemption Determinations

While the APA provides that the substantial evidence test only applies to actions premised on a formal hearing, there are numerous instances in which Congress has specifically provided that informal agency actions, including notice and comment rulemaking, are to be reviewed under the substantial evidence standard.[319] In these situations, courts have often interpreted the two standards as being essentially the same when considering the basis for an agency's action.

For example, in *Association of Data Processing Service Organizations v. Board of Governors*, the D.C. Court of Appeals stated that the distinction between the two standards is "largely semantic," and that the provisions in the Federal

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315 5 U.S.C. § 706(2)(E).

316 Richardson v. Perales, 402 U.S. 389 (1971).

317 Bogle v. Sullivan, 998 F.2d 342, 347 (6th Cir. 1993).

318 Wilson Air Center v. Federal Aviation Admin., 372 F.3d 807, 813 (6th Cir. 2004).

319 *E.g.*, 12 U.S.C. § 1848 (regarding the Federal Reserve Board); 15 U.S.C. §§ 57(a), 1193, 1262 (regarding the Federal Trade Commission); 29 U.S.C. § 655(f) (regarding the OSHA).

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Reserve Act specifying review of the Federal Reserve Board's determinations under the substantial evidence test requires no more than a review under the arbitrary and capricious test.[320]

One difference between the two standards concerns the scope of the documents before the court for purposes of its review. The substantial evidence test is usually based on a review of a formal hearing record, while the "arbitrary and capricious" test is based on a review of all of the evidence before the agency decision-maker when the determination was made. Since the OCC preemption determinations are not required to follow a formal hearing, it is not clear if the use of the "substantial evidence" test will limit the record that a court will review. Arguably, the "record of the proceeding" should be the entire record and all documents that the Comptroller had before him when he or she makes the preemption decision.

In short, the use of "substantial evidence," rather than "arbitrary and capricious" is not likely to result in a meaningful difference in the scope or outcome of court reviews of OCC preemption determinations.

D. Deference

The Dodd-Frank Act amendment to the NBA provides that a court reviewing an OCC preemption determination "shall assess the validity of such determination depending upon the thoroughness evident in the consideration of the agency, the validity of the reasoning of the agency, the consistency with other valid determinations made by the agency, and other factors that the court finds persuasive and relevant."[321] This standard is a codification of the deference afforded in the case of *Skidmore v. Swift & Co.*,[322] and is often referred to as "*Skidmore* deference."

1. Deference Accorded OCC Preemption Rules

In *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, the Supreme Court held that ambiguities in statutes within an agency's jurisdiction to administer are delegations of authority to the agency to fill the statutory gap

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320 Association of Data Processing Serv. Org. v. Board of Governors, 745 F.2d 677, 684 (D.C. Cir. 1984) (citations omitted).

321 12 U.S.C. § 25b(b)(5)(A) (2010).

322 Skidmore v. Swift & Co., 323 U.S. 134, 139 (1944).

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in a reasonable fashion.[323] Thus, if a statute is ambiguous, and if the implementing agency's construction is reasonable, *Chevron* requires a federal court to accept the agency's construction of the statute, even if the agency's reading differs from what the court believes is the best statutory interpretation.[324]

In *United States v. Mead Corporation*, the court limited the use of *Chevron* deference to instances where "it appears that Congress delegated authority to the agency generally to make rules carrying the force of law, and that the agency interpretation claiming deference was promulgated in the exercise of that authority."[325] The Court used the OCC as an example of an agency whose determinations are owed *Chevron* deference: "the Comptroller of the Currency is charged with the enforcement of banking laws to an extent that warrants the invocation of [the *Chevron* rule of deference] with respect to his deliberative conclusions as to the meaning of these laws."[326]

2. Deference Given to OCC Preemption Determinations

When it comes to preemption determinations, additional analysis is required. In *Grier v. American Honda Motor Co.*, the Supreme Court reiterated that agency regulations with the force of law can preempt conflicting state law.[327] In *Williamson v. Mazda Motor of America, Inc.*, the Supreme Court held that a Department of Transportation regulation did not preempt state law because the rulemaking record disclosed no preemptive intent.[328] In *Wyeth v. Levine*, the Supreme Court held that agency determinations short of regulations, such as legal opinions and preamble material that conclude that a state law is preempted, will be reviewed under the *Skidmore* rules.[329] However, if Congress specifically authorized the agency to make preemption determinations, the usual *Chevron* deference rules apply.

As noted earlier, both the 1994 Riegle-Neal Interstate Banking Efficiency Act, and the Dodd-Frank Act authorize the OCC to make preemption

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323 Chevron U.S.A. v. Natural Res. Def. Council, 467 U.S. 837, 843 (1984).

324 National Cable & Telecomm. Ass'n v. Brand X Internet Serv., 545 U.S. 967, 980 (2005).

325 United States v. Mead Corp., 533 U.S. 218, 226-27 (2010).

326 *Id.* at 231 (quoting *NationsBank* at 256-257). *But see Cuomo* (holding that no deference should be given to an OCC regulation interpreting the National Bank Act where the Court felt that the interpretation was unreasonable).

327 Grier v. American Honda Motor, 529 U.S. 861 (2000).

328 Williamson v. Mazda Motor of Am., 131 S.Ct. 1131 (2011).

329 Wyeth v. Levine, 555 U.S. 555, 577 (2009).

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determinations.[330] Therefore, it appears that the OCC should be entitled to *Chevron* deference for its preemption determinations, whether in the form of regulations or legal opinions. The Dodd-Frank Act, by imposing the Skidmore standard on OCC preemption determinations, thus changes the deference that the courts will give the OCC with respect to the specific legal question of whether state law hampers, frustrates the purpose, impedes, obstructs, or otherwise interferes with the NBA and implementing regulations.

On the other hand, the Dodd-Frank Act amendment states that, except for preemption determinations, nothing in the amendment to the NBA affects the deference afforded to OCC determinations regarding the meaning or interpretation of the National Bank Act or other federal law.[331] In other words, *Chevron* deference will continue to apply to the OCC's interpretations of national bank powers. Since preemption decisions are based on a conflict between state law and federal law, once the Comptroller determines that the National Bank Act authorizes a particular activity, product or service, the preemption decision will, in many cases, logically follow. Thus, retaining *Chevron* deference with respect to the interpretation of the National Bank Act will be a key element in future preemption disputes.

IX. OCC REVISION OF ITS PREEMPTION REGULATION

A. Revised Preemption Regulation Proposal

On May 26, 2011, the OCC published a notice of proposed rulemaking to implement some of the amendments made by the Dodd-Frank Act.[332] With regard to preemption, the preamble reviewed the legislative history of section 1044 and concluded that the intent of the Dodd-Frank Act was to apply the conflict preemption standard used by the Supreme Court in *Barnett Bank*.[333] The NPR went on to state that since the Dodd-Frank Act preserved the *Barnett Bank* preemption, the OCC's rules and prior preemption determinations were preserved.[334] Nevertheless, in order to "avoid ambiguities and misunderstandings" the NPR proposed removing the phrase

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[330] *See supra* Section IV.A.

[331] 12 U.S.C. § 25b(b)(5)(B) (2010).

[332] Office of Thrift Supervision Integration; Dodd-Frank Act Implementation, 76 Fed. Reg. 30557 (proposed May 26, 2011) (to be codified at 12 C.F.R. pts. 4, 5, 7, 8, 28, 34).

[333] *Id.* at 30562.

[334] *Id.* at 30563.

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"obstruct, impair or condition" from its regulations.[335] The NPR took the position that this change would not have substantive effect, because the phrase "obstruct, impair or condition" was simply a distillation of *Barnett Bank*, and therefore precedents relying on the 2004 regulation would remain in effect.[336] The NPR also proposed to retain the list of types of laws that were preempted or not preempted.

B. Final Rule Revising Preemption Regulation

On July 21, 2011, the OCC published a final regulation revising the preemption rule.[337] The final regulation again stated that the Dodd-Frank Act codified *Barnett Bank* and does not establish a new preemption standard.[338]

The final rule also deleted the phrase "obstruct, impair, or condition."[339] However, in a rather dramatic change of position, the OCC implicitly recognized that the "obstruct, impair or condition" standard may not have been entirely consistent with *Barnett Bank.*[340] The OCC warned that determinations that relied exclusively on that standard need to be reevaluated:

> To the extent that an existing preemption precedent is exclusively reliant on the phrase "obstructs, impairs, or conditions" as the basis for a preemption determination, we believe that validity of the precedent would need to be reexamined to ascertain whether the determination is consistent with the *Barnett* conflict preemption analysis as discussed above.[341]

The OCC stated that it had not identified any prior agency issued preemption precedent that rested solely on the "obstruct, impair or condition" formulation.[342] The OCC did not evaluate whether there have

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[335] *Id.*
[336] *Id.*
[337] Office of Thrift Supervision Integration; Dodd-Frank Act Implementation, 76 Fed. Reg. 43549 (July 21, 2011) (to be codified at 12 C.F.R. pts. 4, 5, 7, 8, 28, 34).
[338] *Id.* at 43555.
[339] *Id.* at 43556.
[340] *Id.*
[341] *Id.*
[342] *Id.* at n. 43.

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been any court determinations based solely on the "obstruct, impair or condition" phrase.

The final regulation made no change with respect to the categories of laws that are preempted under the rule. The OCC explained that these categories of laws are included as preempted based on the agency's conclusion that they are preempted by application of the *Barnett Bank* standard.[343] The rule also states that OCC regulations relating to national bank charges,[344] adjustable rate mortgages,[345] and debt cancellation contracts[346] remain in effect.[347]

X. CONCLUSION

In 1863, the National Bank Act established a system for the federal chartering and regulation of banking institutions, with the intent to have a national system supersede state banks. Efforts by the states to prevent this result, and to apply state restrictions to national banks, led to a continuing debate over the preemptive effect of the National Bank Act over the past 150 years.

Recently, preemption was put in the spotlight when some argued that the preemption regulations issued by the OCC contributed significantly to the risky mortgage lending practices that led to the financial crisis. In particular, it is argued that the OCC preempted state "anti-predatory" lending laws without providing an effective national standard to prevent abusive mortgage lending practices.

We conclude that the underlying argument against preemption is not correct. National banks were largely prevented from engaging in predatory lending practices. The argument against preemption conflates predatory lending with subprime lending. The state anti-predatory lending laws were aimed at abusive lending practices, characteristic of only a fraction of the total subprime loans made. "Responsible" subprime lending was encouraged by both the states and Federal Government as a means of increasing home ownership among lower income consumers. Unfortunately, once housing

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343 *Id.*
344 12 C.F.R. § 7.4002.
345 12 C.F.R. § 34.21.
346 12 C.F.R. §§ 37.1, *et. seq.*
347 76 Fed. Reg. 43554 (2011).

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prices began to collapse, these "responsible subprime loans" began to massively default, initiating the financial crisis.

The overwhelming majority of subprime loans were originated by state regulated and state chartered entities. These entities were not subject to preemption. Many conglomerates that had national bank subsidiaries chose state-regulated affiliates to originate subprime loans, to avoid the more stringent underwriting standards imposed by the OCC.

The Dodd-Frank Act amended the NBA to include specific authority for the OCC to preempt state consumer finance laws. Some argue that this amendment applies a new and narrow standard for finding such a state law preempted. However, based on a review of the statutory language, its legislative history, cannons of statutory construction, and relevant case law, this article concludes that the Dodd-Frank Act does not make any material change in the legal standard for preemption under the NBA. Other changes made by the Dodd-Frank Act with respect to national bank preemption relate to the activities of subsidiaries and agents of national banks, and prescribe certain new procedures on the OCC when making a preemption determination.

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