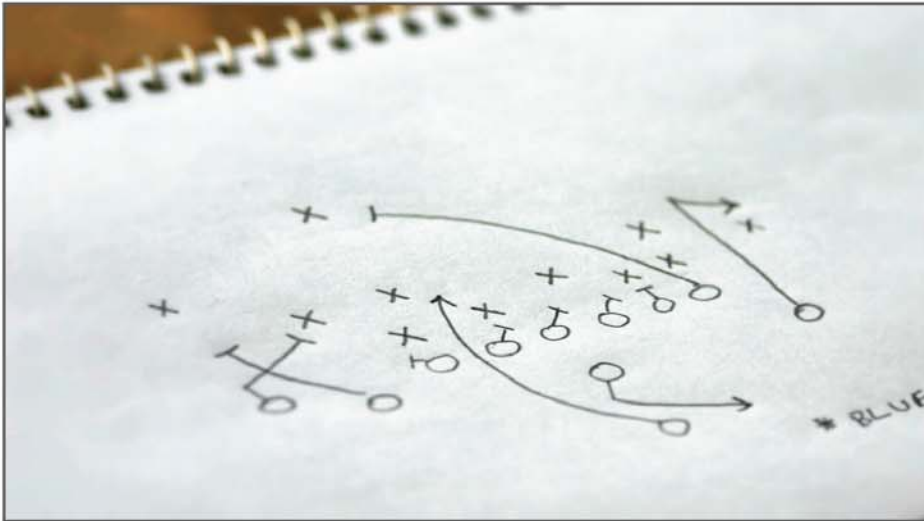


# Dodd-Frank Wall Street Reform and Consumer Protection Act Federal Preemption User Guide



This is the first of a series of user guides that will be published by Morrison & Foerster. The user guides provide an in depth discussion on specific topics raised by the Dodd-Frank Act. For our Dodd-Frank overview and brief alerts, please see our dedicated website at:

<http://www.mofo.com/resources/regulatory-reform/>.

## Introduction

This is a user guide for the provisions of the “Dodd-Frank Wall Street Reform and Consumer Protection Act,” Pub. L. No. 111-203 (“Dodd-Frank Act”), that deal with federal preemption of state consumer protection laws. More specifically, it covers the following provisions of the Dodd-Frank Act, all of which are part of Subtitle D of Title X, the “Consumer Financial Protection Act of 2010” (“CFPA”):

- Section 1041. Relation to state law.
- Section 1042. Preservation of enforcement powers of states.
- Section 1043. Preservation of existing contracts.
- Section 1044. State law preemption standards for national banks and subsidiaries clarified.
- Section 1045. Clarification of law applicable to nondepository institution subsidiaries.
- Section 1046. State law preemption standards for federal savings associations and subsidiaries clarified.
- Section 1047. Visitorial standards for national banks and savings associations.
- Section 1048. Effective date.

## Use of This Guide

This guide is designed for use by executives and managers at national banks and federal savings associations. It is intended to be a pragmatic reference piece relating to the implementation of Subtitle D of the CFPA. When implementing regulations are issued, the guidance provided by this guide will need to be refined accordingly. This guide does not provide legal advice and should not be relied upon as such.

## Organization of This Guide

For ease of reference, this guide is organized by the various sections of Subtitle D of the CFPA. With each provision, we summarize the new law, discuss its linkages to existing law, and analyze some of the more important ramifications for national banks and federal savings associations. We use some examples to help illustrate the subtleties of the CFPA, but the examples will be for illustrative purposes only.

## Framework for Federal Preemption

As a starting point, Congress creates a new framework within Subtitle D for determining preemption issues in the field of consumer protection. Based on Subtitle D, these preemption issues now fall into one of three distinct categories: (i) conflicts between the CFPA and state statutes, regulations, orders, or interpretations (“CFPA Conflicts”). CFPA Conflicts do not include Enumerated Consumer Law Conflicts or Charter Conflicts; (ii) conflicts between certain “Enumerated Consumer Laws” and any state law (“Enumerated Consumer Law Conflicts”); and (iii) conflicts (“Charter Conflicts”) between state consumer financial laws (defined below), on the one hand, and court decisions or regulations or orders of the Office of the Comptroller of the Currency (“OCC”) or Office of Thrift Supervision (“OTS”), on the other.

CFPA Conflicts and Enumerated Consumer Law Conflicts are discussed in the analysis of Section 1041. Charter Conflicts are discussed in the analysis of Section 1044.

## Background: The Bureau

Subtitle A of the CFPA establishes the new Consumer Financial Protection Bureau (“Bureau”) as an independent bureau within the Federal Reserve System. The Bureau consolidates certain consumer protection responsibilities currently handled by multiple federal agencies, including the OCC, OTS, Federal Deposit Insurance Corporation (“FDIC”), Federal Reserve Board (“FRB”), National Credit Union Administration (“NCUA”), the Department of Housing and Urban Development (“HUD”), and Federal Trade Commission (“FTC”).

Subtitles B and C of the CFPA provide the general and specific authorities of the Bureau, which, at a high level, are as follows:

- The Bureau is authorized to write consumer protection rules governing all financial institutions that offer consumer financial services or products, both depository institutions and nondepository institutions alike. Rule-writing authority under certain consumer protection laws is transferred from existing agencies and consolidated at the Bureau. In addition, the Bureau is given broad power to make rules prohibiting deceptive, unfair, or abusive practices.
- The Bureau is authorized to examine and enforce these regulations with respect to:
  - banks, thrifts, and credit unions with assets more than \$10 billion;
  - all mortgage-related businesses (lenders, servicers, mortgage brokers, and foreclosure scam operators); and
  - “larger participants,” as defined by a rule to be made by the Bureau, of a market for non-mortgage consumer financial products or services, including non-bank lenders, debt collectors, and consumer reporting agencies.
- Banks, thrifts, and credit unions with assets of \$10 billion or less will be examined for compliance with consumer protection laws and rules by the appropriate prudential regulator, although the Bureau may examine these institutions “on a sampling basis of the examinations performed by the prudential regulator.”

**Section 1041. Relation to State Law (CFPA Conflicts and Enumerated Law Conflicts)****(a) In General-**

(1) **RULE OF CONSTRUCTION-** This title, other than sections 1044 through 1048, may not be construed as annulling, altering, or affecting, or exempting any person subject to the provisions of this title from complying with, the statutes, regulations, orders, or interpretations in effect in any State, except to the extent that any such provision of law is inconsistent with the provisions of this title, and then only to the extent of the inconsistency.

(2) **GREATER PROTECTION UNDER STATE LAW-** For purposes of this subsection, a statute, regulation, order, or interpretation in effect in any State is not inconsistent with the provisions of this title if the protection that such statute, regulation, order, or interpretation affords to consumers is greater than the protection provided under this title. A determination regarding whether a statute, regulation, order, or interpretation in effect in any State is inconsistent with the provisions of this title may be made by the Bureau on its own motion or in response to a nonfrivolous petition initiated by any interested person.

**(b) Relation to Other Provisions of Enumerated Consumer Laws That Relate to State Law-** No provision of this title, except as provided in section 1083, shall be construed as modifying, limiting, or superseding the operation of any provision of an enumerated consumer law that relates to the application of a law in effect in any State with respect to such Federal law.

**(c) Additional Consumer Protection Regulations in Response to State Action-**

(1) **NOTICE OF PROPOSED RULE REQUIRED-** The Bureau shall issue a notice of proposed rulemaking whenever a majority of the States has enacted a resolution in support of the establishment or modification of a consumer protection regulation by the Bureau.

(2) **BUREAU CONSIDERATIONS REQUIRED FOR ISSUANCE OF FINAL REGULATION-** Before prescribing a final regulation based upon a notice issued pursuant to paragraph (1), the Bureau shall take into account whether--

(A) the proposed regulation would afford greater protection to consumers than any existing regulation;

(B) the intended benefits of the proposed regulation for consumers would outweigh any increased costs or inconveniences for consumers, and would not discriminate unfairly against any category or class of consumers; and

(C) a Federal banking agency has advised that the proposed regulation is likely to present an unacceptable safety and soundness risk to insured depository institutions.

(3) **EXPLANATION OF CONSIDERATIONS-** The Bureau--

(A) shall include a discussion of the considerations required in paragraph (2) in the Federal Register notice of a final regulation prescribed pursuant to this subsection; and

(B) whenever the Bureau determines not to prescribe a final regulation, shall publish an explanation of such determination in the Federal Register, and provide a copy of such explanation to each State that enacted a resolution in support of the proposed regulation, the Committee on Banking, Housing, and Urban Affairs of the Senate, and the Committee on Financial Services of the House of Representatives.

(4) **RESERVATION OF AUTHORITY-** No provision of this subsection shall be construed as limiting or restricting the authority of the Bureau to enhance consumer protection standards established pursuant to this title in response to its own motion or in response to a request by any other interested person.

(5) **RULE OF CONSTRUCTION-** No provision of this subsection shall be construed as exempting the Bureau from complying with subchapter II of chapter 5 of title 5, United States Code.

(6) **DEFINITION-** For purposes of this subsection, the term 'consumer protection regulation' means a regulation that the Bureau is authorized to prescribe under the Federal consumer financial laws.

**Analysis.** Section 1041 lays out the rules for CFPB Conflicts and Enumerated Law Conflicts. It authorizes the Bureau to make preemption determinations with respect to CFPB Conflicts, and it establishes a process by which the states may petition the Bureau to initiate a rulemaking proceeding.

Note that the procedures and approach of Section 1041 are very different from the procedures and approach reflected in Section 1044 (state law preemption standards for national banks and federal savings associations); these differences are discussed below.

- CFPB Conflicts. Section 1041(a) provides a structure for resolving conflicts between (a) the CFPB and (b) any state statute, regulation, order, or interpretation. This structure does not apply to Enumerated Consumer Law Conflicts or Charter Conflicts.
  - Rule of Construction. A state statute, regulation, order, or interpretation is preempted by the CFPB only if “any such provision of [state] law is inconsistent with the CFPB . . . and then only to the extent of the inconsistency.”

For example, assume that the Bureau issued a regulation under the CFPB that required creditors to make necessary disclosures in both English and Spanish. Assume further that a state law allowed creditors to make disclosures in English only, thereby prohibiting disclosures in Spanish. The state law would be preempted as to the prohibition of Spanish disclosures, because it would directly conflict with the Bureau’s regulation that required Spanish disclosures.

- Greater Protection Under State Law. A state statute, regulation, order, or interpretation is not treated as inconsistent with the CFPB if the protection that the state law “affords to consumers is greater than the protection provided” under the CFPB.

For example, assume that the Bureau issued a regulation under the CFPB that required creditors to make necessary disclosures in both English and Spanish. Assume further that a state law also required creditors to make disclosures in four additional languages. The state law would not be preempted under this standard because it affords greater protection to consumers than the Bureau’s regulation.

Preemption based upon an inconsistency between federal and state law has long been a basis for the exercise of the federal preemption doctrine. The inapplicability of federal preemption where a state consumer protection law is more protective of consumers also has a long history. Many of the Enumerated State Laws discussed below follow such an approach.

- Determinations Regarding Inconsistency. A determination whether a state law is “inconsistent” with the CFPB “may be made by the Bureau on its own motion or in response to a nonfrivolous petition initiated by any interested person.”

While the Bureau is authorized to determine if a state law is inconsistent with the CFPB, Section 1041 is silent regarding the authority of the federal courts to review and overrule Bureau determinations. There is every reason to expect that the federal courts have this authority. Further, while Section 1041 is silent regarding the authority of the courts to determine whether a state law is “inconsistent” with the CFPB, there is every reason to expect that the courts have this authority.

The statute does not explain *when* a petition requesting the Bureau to determine whether a particular state law is inconsistent with the CFPB will be regarded as “frivolous.” Presumably, the Bureau will establish internal guidelines regarding this issue. There are existing banking agency regulations that utilize a “frivolous” request standard (see, e.g., 12 C.F.R. § 19.23(e)), and in this context the term is likely to include repetitive, irrelevant, and dilatory petitions.

The statute also does not explain which persons will qualify as “interested persons” who are entitled to present petitions to the Bureau. Again, the Bureau is likely to establish internal guidelines regarding this issue. The federal Truth in Lending Act allows similar petitions from “any creditor, State or other interested person.” Accordingly, it is likely that “interested persons” will include banks and other institutions that may be covered by the state laws, as well as the states. “Interested persons” also may include financial services trade associations, as well as consumer groups.

The Bureau’s authority to determine inconsistencies between state and federal law does not include the right to make preemption determinations regarding Charter Conflicts. Those preemption determinations will be made by the courts or by the OCC and OTS in accordance with Section 1044, discussed below.

Many of the Enumerated Consumer Laws provide companies with a “safe harbor” against civil, criminal, and administrative liability if they comply in good faith with a regulation, order, or interpretation of the designated federal agency. See, e.g., 15 U.S.C. § 1640(f) (federal Truth in Lending Act). There is no equivalent safe harbor provision in Section 1041 for Bureau determinations, which means that companies will rely on those determinations at their own risk.

- Scope of State Laws That Are Subject to the CFPA Conflicts Rule. By its terms, the CFPA Conflicts rule is limited to conflicts between “this title,”—that is, the CFPA itself—and state statutes, regulations, orders, or interpretations. As noted above, the CFPA Conflicts rule does not apply to Enumerated Consumer Law Conflicts or Charter Conflicts. In addition, the CFPA Conflicts rule does not govern other federal preemption issues—that is, federal preemption issues that do not involve the CFPA—which should continue to be governed by existing federal preemption standards and precedents.

For example, if a state law purported to require national banks to meet certain capital requirements, that state law would not be governed by the CFPA Conflicts rule because capital is not governed by the CFPA. That state law would be preempted, just as it would have been preempted in the past.

- Enumerated Consumer Law Conflicts. Section 1041(b) provides a structure for resolving conflicts between (a) a state law and (b) the “Enumerated Consumer Laws.” In the case of the Enumerated Consumer Laws, the federal preemption issue is resolved solely by the standards set forth in each such Enumerated Consumer Law. Those standards vary considerably.

The “Enumerated Consumer Laws” are defined in Section 1002(12) of the Dodd-Frank Act to include each of the federal statutes listed below. The federal preemption provisions of the Enumerated Consumer Laws also are quoted or summarized below. Note that the preemption provisions of the Alternative Mortgage Transaction Parity Act have been amended by the Dodd-Frank Act, and that only the amended provisions are identified below. Also note that certain federal agencies’ consumer protection authorities under the Enumerated Consumer Laws will be transferred to the Bureau; these transfers of authority are not reflected in the language provided below.

- *The Alternative Mortgage Transaction Parity Act of 1982 (“AMTPA”)*—The AMTPA provides that “an alternative mortgage transaction may be made by a housing creditor in accordance with this section, notwithstanding any State constitution, law, or regulation that prohibits an alternative mortgage transaction. For purposes of this subsection, a State constitution, law, or regulation that prohibits an alternative mortgage transaction does not include any State constitution, law, or regulation that regulates mortgage transactions generally, including any restriction on prepayment penalties or late charges.” 12 U.S.C. § 3803. Note that the states were given an opportunity to opt out from the federal preemption by 12 U.S.C. § 3804, and a small number of states have exercised this opt-out right.
- *The Consumer Leasing Act of 1976*—The Consumer Leasing Act of 1976 “does not annul, alter, or affect, or exempt any person subject to the provisions of this part from complying with [State law] with respect to consumer leases, except to the extent that those laws are inconsistent with any provision of

this part, and then only to the extent of the inconsistency. . . . State law is [not] inconsistent . . . [if] such law gives greater protection and benefit to the consumer.” 15 U.S.C. § 1667e.

- *The Electronic Fund Transfer Act* (“EFTA”)—The EFTA “does not annul, alter, or affect the laws of any State relating to electronic fund transfers, except to the extent that those laws are inconsistent with the provisions of this subchapter, and then only to the extent of the inconsistency. . . . A State law is not inconsistent with this subchapter if the protection such law affords any consumer is greater than the protection afforded by [the EFTA].” 15 U.S.C. § 1693q.
- *The Equal Credit Opportunity Act* (“ECOA”)—The ECOA, as implemented by the Federal Reserve’s Regulation B, “alters, affects, or preempts only those state laws that are inconsistent with the [ECOA and Regulation B] and then only to the extent of the inconsistency. . . . A state law is not inconsistent if it is more protective of an applicant.” 12 C.F.R. § 202.11(a).
- *The Fair Credit Billing Act*—The Fair Credit Billing Act “does not annul, alter, or affect, or exempt any person subject to the provisions of this part from complying with [State law] with respect to credit billing practices, except to the extent that those laws are inconsistent with any provision of this part, and then only to the extent of the inconsistency. . . . State law is [not] inconsistent . . . if . . . such law gives greater protection to the consumer.” 15 U.S.C. § 1666(j).
- *The Fair Credit Reporting Act* (“FCRA”)—In general, the FCRA “does not annul, alter, affect, or exempt any person subject to the provisions of [the FCRA] from complying with the laws of any state with respect to the collection, distribution, or use of any information on consumers, or for the prevention or mitigation of identity theft, except to the extent that those laws are inconsistent with any provision of this subchapter, and then only to the extent of the inconsistency.” See 15 U.S.C. § 1681t(a). There is a long list of specific provisions of the FCRA that do preempt state laws, and there are various exceptions to that preemption. See 15 U.S.C. § 1681t(b)-(d). Congress has expressly excluded two provisions of the FCRA from the list of Enumerated Consumer Laws: the Red Flags Rule (15 U.S.C. § 1681m(e)) and the FCRA provision on Disposal of Records (15 U.S.C. § 1681w). These provisions therefore should be considered under the CFPB Conflicts standard set forth in Section 1041(a), discussed above.
- *The Home Owners Protection Act of 1998* (“HPA”)—The HPA provides that “[w]ith respect to any . . . residential mortgage transaction . . . [the HPA] shall supersede any [State law, except protected State law as defined by the HPA,] relating to requirements for obtaining or maintaining private mortgage insurance in connection with residential mortgage transactions, cancellation or automatic termination of such private mortgage insurance, any disclosure of information addressed by this chapter, and any other matter specifically addressed by this chapter.” 12 U.S.C. § 4908(a).
- *The Fair Debt Collection Practices Act* (“FDCPA”)—The FDCPA “does not annul, alter, or affect, or exempt any person subject to the provisions of this subchapter from complying with the laws of any State with respect to debt collection practices, except to the extent that those laws are inconsistent with [the FDCPA], and then only to the extent of the inconsistency. . . . State law is not inconsistent with this subchapter if the protection such law affords any consumer is greater than the protection provided by [the FDCPA].” 15 U.S.C. § 1692n.
- Section 43(b)-(f) of the *Federal Deposit Insurance Act* (“FDIA”)—The FDIA requires certain disclosures by depository institutions that lack federal deposit insurance. Section 43(c) provides that “[t]o ensure that current and prospective customers understand the risks involved in foregoing Federal deposit insurance, the Federal Trade Commission, by regulation or order, shall prescribe the manner and content of disclosure required under this section, which shall be presented in such format and in such type size and manner as to be simple and easy to understand.” While the states are authorized to take broad enforcement action against these uninsured depository institutions for any violation of § 43 or the

FTC regulations, once the FTC has instituted an enforcement action under § 43, the state supervisor may not bring an action against the defendant for the same violation. See 12 U.S.C. § 1831t(f)(2)(C).

- *The Gramm-Leach-Bliley Act* (“GLBA”)—GLBA provides that nothing in the GLBA “shall be construed as superseding, altering, or affecting any statute, regulation, order, or interpretation in effect in any State, except to the extent that such statute, regulation, order, or interpretation is inconsistent with the provisions of this subchapter, and then only to the extent of the inconsistency . . . a State statute, regulation, order, or interpretation is not inconsistent with the provisions of this subchapter if the protection such statute, regulation, order, or interpretation affords any person is greater than the protection provided under this subchapter and the amendments made by this subchapter, as determined by the Federal Trade Commission, after consultation with the agency or authority with jurisdiction under section 6805(a) of this title of either the person that initiated the complaint or that is the subject of the complaint, on its own motion or upon the petition of any interested party.” 15 U.S.C. § 6807. The rules for enforcement (15 U.S.C. § 6805) as they relate to financial institution safeguards of nonpublic personal information, however, are specifically excluded from the Enumerated Consumer Laws.
- *The Home Mortgage Disclosure Act of 1975* (“HMDA”)—HMDA “does not annul, alter, or affect, or exempt any State chartered depository institution subject to the provisions of this chapter from complying with [State law] with respect to public disclosure and recordkeeping by depository institutions, except to the extent that those laws are inconsistent with any provision of [the HMDA], and then only to the extent of the inconsistency. The Board is authorized to determine whether such inconsistencies exist. The Board may not determine that any such law is inconsistent with any provision of [HMDA] if the Board determines that such law requires the maintenance of records with greater geographic or other detail than is required under [HMDA], or that such law otherwise provides greater disclosure than is required under [HMDA].” See 12 U.S.C. § 2805.
- *The Home Ownership and Equity Protection Act of 1994*—15 U.S.C. § 1639 imposes restrictions on certain high-cost mortgages. “The provisions of section 1639 of this title do not annul, alter, or affect the applicability of the laws of any State or exempt any person subject to the provisions of section 1639 of this title from complying with the laws of any State, with respect to the requirements for mortgages referred to in section 1602(aa) of this title, except to the extent that those State laws are inconsistent with any provisions of section 1639 of this title, and then only to the extent of the inconsistency. See 15 U.S.C. § 1610.
- *The Real Estate Settlement Procedures Act of 1974* (“RESPA”)—RESPA “does not annul, alter, or affect, or exempt any person subject to the provisions of [RESPA] from complying with [State law] with respect to settlement practices, except to the extent that those laws are inconsistent with any provision of [RESPA], and then only to the extent of the inconsistency. . . . [No] law is inconsistent [if] such law gives greater protection to the consumer. The Secretary is authorized to determine whether such inconsistencies exist. The Secretary may not determine that any State law is inconsistent with any provision of this chapter if the Secretary determines that such law gives greater protection to the consumer. In making these determinations the Secretary shall consult with the appropriate Federal agencies.” 12 U.S.C. § 2616.
- *The Secure and Fair Enforcement for Mortgage Licensing Act of 2008* (“SAFE Act”)—The SAFE Act requires the Secretary of HUD to establish a system for licensing and registering loan originators in a state if a state has failed to do so on its own, or has failed to participate in the Nationwide Mortgage Licensing System and Registry, within a defined timeframe. The standards for such state licensing and registration are dictated by the SAFE Act. 12 U.S.C. § 5104.
- *The Truth in Lending Act* (“TILA”)—TILA provides, in part, as follows: “Except as provided in subsection (e) of this section, this part and parts B and C of this subchapter, do not annul, alter, or affect the laws of any State relating to the disclosure of information in connection with credit transactions, except to the

extent that those laws are inconsistent with the provisions of this subchapter and then only to the extent of the inconsistency. Upon its own motion or upon the request of any creditor, State or other interested party which is submitted in accordance with procedures prescribed in regulations of the Board, the Board shall determine whether any such inconsistency exists. If the Board determines that a State-required disclosure is inconsistent, creditors located in that State may not make disclosures using the inconsistent term or form, and shall incur no liability under the law of that State for failure to use such term or form, notwithstanding that such determination is subsequently amended, rescinded, or determined by judicial or other authority to be invalid for any reason.” 15 U.S.C. § 1610(a)(1). The FRB’s Regulation Z provides, in part, that “[S]tate law requirements that are inconsistent with [certain provisions of TILA and Regulation Z] are preempted to the extent of the inconsistency. A State law is inconsistent if it requires a creditor to make disclosures or take actions that contradict the requirements of the Federal law.” 12 C.F.R. § 226.28. A state law contradicts the TILA if the state law requires use of a term required by TILA but with a different amount or meaning; or requires use of a different term than the TILA term to describe the same item. *Id.* Paragraph 226.28(a)-3 of the Regulation Z Commentary states that “[g]enerally, State law requirements that call for the disclosure of items of information not covered by the Federal law, or that require more detailed disclosures, do not contradict the Federal requirements.”

- *The Truth in Savings Act* (“TISA”)—The provisions of TISA “do not supersede any provisions of [State law] relating to the disclosure of yields payable or terms for accounts to the extent such State law requires the disclosure of such yields or terms for accounts, except to the extent that those laws are inconsistent with the provisions of [TISA], and then only to the extent of the inconsistency.” 12 U.S.C. § 4312. This is a relatively narrow standard for preemption. The FRB’s Regulation DD provides that a state law is inconsistent if it requires a depository institution to make disclosures or take actions that contradict the requirements of the TISA, if it requires the use of the same term to represent a different amount or a different meaning than the TISA, or if it requires the use of a term different from that required in the TISA to describe the same item or permits a different method of calculating interest than is required under federal law. 12 C.F.R. Part 230, App. C.
- *Section 626 of the Omnibus Appropriations Act of 2009* (Pub. L. No. 111-8)—Among other things, this section authorizes the states to bring TILA actions and actions under certain FTC regulations relating to mortgage loans. However, a state ordinarily must provide 60 days’ written notice before filing the action, and this allows the FTC to intervene, remove the action to federal court, and file appeals. If the FTC itself files such an action, the state may not file a civil action of its own while the FTC action is pending. By their terms, these provisions have a preemptive effect.
- *The Interstate Land Sales Full Disclosure Act* (“ILSFDA”)—The ILSFDA requires that states meet certain legal standards with respect to disclosures concerning the sale or lease of lots. States must receive certification that their laws and regulations are substantially equivalent to federal disclosure requirements. “Nothing in [the ILSFDA] may be construed to prevent or limit the authority of any State or local government to enact and enforce with regard to the sale of land any law, ordinance, or code not in conflict with [the ILSFDA].” 15 U.S.C. § 1708.
- Additional Consumer Protection Regulations in Response to State Action. Section 1041(c)(1) gives the states a procedure by which they can ask the Bureau to issue new consumer protection regulations, or to amend an existing consumer protection regulation.
  - Notice of Proposed Rule Required. Section 1041(c)(1) requires the Bureau to “issue a notice of proposed rulemaking whenever a majority of the States has enacted a resolution in support of the establishment or modification of a consumer protection regulation by the Bureau.”

While this provision would appear to give the states an unprecedented role in the rulemaking process of a federal agency, the actual impact that the states will have on the Bureau’s regulations is not clear.

This process will be initiated only if the Bureau is requested to act by a majority of the states, and there may be few instances in which a majority of the states will agree to request the same exact action by the Bureau. Finally, while the Bureau may feel pressured to take action in response to the states' request, it is not obligated to do so. If the Bureau does take action, it is not obligated to take the specific action requested by the states.

There is uncertainty regarding how the states must request Bureau action. The statute states that the states must enact a "resolution" requesting action. Does this mean a resolution adopted by each chamber of the state legislature? Must the resolution be signed by the state's governor? Presumably, these are issues that the Bureau will need to sort out.

- Bureau Considerations Required for Issuance of Final Regulation. The Bureau is required to consider the following factors before issuing a final regulation in response to the states' request: (i) whether the proposed regulation would afford greater protection to consumers than any existing regulation; (ii) whether the intended benefits of the proposed regulation would outweigh any increased costs or inconveniences for consumers, and would not discriminate unfairly against any category or class of consumers; and (iii) whether a federal banking agency has advised that the proposal is likely to present an unacceptable safety and soundness risk to insured depository institutions. See § 1041(c)(2).

Although the Bureau is required to consider these factors before *issuing* a final regulation, the literal wording of the statute does not require the Bureau to consider these factors when deciding *whether* to issue a final regulation. Nevertheless, it is expected that the Bureau will consider these factors both in deciding whether to issue a final regulation and in determining the content of that regulation.

There is nothing in this statute that precludes the Bureau from considering other relevant factors before issuing a final regulation, including factors that are identified by banks, other financial services companies, trade groups, and others in response to the proposed rulemaking. For example, the Bureau would be expected to consider the cost of implementing the proposed regulation for the financial services industry and the impact of the proposed regulation on the availability of credit or other financial services.

- Explanation of Considerations: The Bureau must take the following actions in response to the states' request:
  - If a Final Regulation Is Issued. If the Bureau issues a final regulation, the Federal Register notice must include a discussion of its considerations for each of the required three factors identified above. The Bureau will need to do this whether the final regulation is the same as, or differs from, the requested action of the states.

Nothing in the statute precludes the Bureau from also discussing other considerations that affected its decision.

- If a Final Regulation Is Not Issued. If the Bureau does not issue a final regulation, it must publish an "explanation of such determination" in the Federal Register. It must provide a copy of the explanation to each state that requested the action, as well as to the Senate Banking Committee and House Financial Services Committee.

Note that the statute does not require the Bureau's explanation to address its considerations for each of the three factors identified above. This supports the interpretation, discussed above, that the Bureau is not technically required to consider these factors in deciding whether to issue a final regulation. Nevertheless, the Bureau is likely to address its considerations for these factors in its explanation.

- Reservation of Authority. While the states may petition the Bureau to take action, the statute confirms that the Bureau retains its own statutory authority to issue regulations, or amend its existing regulations, to enhance consumer protection standards. The Bureau can do so on its own initiative or in response to a petition from “other interested persons.” See discussion regarding “interested persons” under Section 1041, above.
- Rule of Construction. The statute confirms that the Bureau must comply with the Administrative Procedures Act when issuing regulations.
- Definition. The term “consumer protection regulation” is defined to mean a regulation that the Bureau is authorized to issue under the federal consumer financial laws.

## **Section 1042. Preservation of Enforcement Powers of States (Right of State Attorneys General and State Regulators to Bring Actions)**

### **(a) In General-**

(1) **ACTION BY STATE-** Except as provided in paragraph (2), the attorney general (or the equivalent thereof) of any State may bring a civil action in the name of such State in any district court of the United States in that State or in State court that is located in that State and that has jurisdiction over the defendant, to enforce provisions of this title or regulations issued under this title, and to secure remedies under provisions of this title or remedies otherwise provided under other law. A State regulator may bring a civil action or other appropriate proceeding to enforce the provisions of this title or regulations issued under this title with respect to any entity that is State-chartered, incorporated, licensed, or otherwise authorized to do business under State law (except as provided in paragraph (2)), and to secure remedies under provisions of this title or remedies otherwise provided under other provisions of law with respect to such an entity.

### **(2) ACTION BY STATE AGAINST NATIONAL BANK OR FEDERAL SAVINGS ASSOCIATION TO ENFORCE RULES-**

(A) **IN GENERAL-** Except as permitted under subparagraph (B), the attorney general (or equivalent thereof) of any State may not bring a civil action in the name of such State against a national bank or Federal savings association to enforce a provision of this title.

(B) **ENFORCEMENT OF RULES PERMITTED-** The attorney general (or the equivalent thereof) of any State may bring a civil action in the name of such State against a national bank or Federal savings association in any district court of the United States in the State or in State court that is located in that State and that has jurisdiction over the defendant to enforce a regulation prescribed by the Bureau under a provision of this title and to secure remedies under provisions of this title or remedies otherwise provided under other law.

(3) **RULE OF CONSTRUCTION-** No provision of this title shall be construed as modifying, limiting, or superseding the operation of any provision of an enumerated consumer law that relates to the authority of a State attorney general or State regulator to enforce such Federal law.

### **(b) Consultation Required-**

#### **(1) NOTICE-**

(A) **IN GENERAL-** Before initiating any action in a court or other administrative or regulatory proceeding against any covered person as authorized by subsection (a) to enforce any provision of this title, including any regulation prescribed by the Bureau under this title, a State attorney general or State regulator shall timely provide a copy of the complete complaint to be filed and written notice describing such action or proceeding to the Bureau and the prudential regulator, if any, or the designee thereof.

(B) **EMERGENCY ACTION-** If prior notice is not practicable, the State attorney general or State regulator shall provide a copy of the complete complaint and the notice to the Bureau and the prudential regulator, if any, immediately upon instituting the action or proceeding.

(C) **CONTENTS OF NOTICE-** The notification required under this paragraph shall, at a minimum, describe--

- (i) the identity of the parties;
- (ii) the alleged facts underlying the proceeding; and
- (iii) whether there may be a need to coordinate the prosecution of the proceeding so as not to interfere with any action, including any rulemaking, undertaken by the Bureau, a prudential regulator, or another Federal agency.

(2) BUREAU RESPONSE- In any action described in paragraph (1), the Bureau may--

(A) intervene in the action as a party;

(B) upon intervening--

- (i) remove the action to the appropriate United States district court, if the action was not originally brought there; and

- (ii) be heard on all matters arising in the action; and

(C) appeal any order or judgment, to the same extent as any other party in the proceeding may.

(c) Regulations- The Bureau shall prescribe regulations to implement the requirements of this section and, from time to time, provide guidance in order to further coordinate actions with the State attorneys general and other regulators.

(d) Preservation of State Authority-

(1) STATE CLAIMS- No provision of this section shall be construed as altering, limiting, or affecting the authority of a State attorney general or any other regulatory or enforcement agency or authority to bring an action or other regulatory proceeding arising solely under the law in effect in that State.

(2) STATE SECURITIES REGULATORS- No provision of this title shall be construed as altering, limiting, or affecting the authority of a State securities commission (or any agency or office performing like functions) under State law to adopt rules, initiate enforcement proceedings, or take any other action with respect to a person regulated by such commission or authority.

(3) STATE INSURANCE REGULATORS- No provision of this title shall be construed as altering, limiting, or affecting the authority of a State insurance commission or State insurance regulator under State law to adopt rules, initiate enforcement proceedings, or take any other action with respect to a person regulated by such commission or regulator.

**Analysis.** Section 1042 creates a new framework for determining the states' enforcement powers against financial services companies. Section 1042 addresses five different categories of actions: (i) actions by state attorneys general against all persons (other than national banks and federal savings associations) to enforce the CFPA and its regulations; (ii) actions by state regulators against state-licensed or -chartered entities to enforce the CFPA and its regulations; (iii) actions by state attorneys general against national banks or federal savings associations to enforce CFPA regulations; (iv) actions by state attorneys general or other state regulators against all persons to enforce the Enumerated Consumer Laws; (v) actions by state attorneys general or other state regulators to enforce state laws. There are limitations on the right of the state attorneys general and state regulators to bring actions with respect to the CFPA.

Section 1042 does not deprive the Bureau or other federal agencies of their respective jurisdictions to take enforcement actions in accordance with applicable federal laws.

- Category 1: Actions by State Attorneys General Against All Persons (Other than National Banks and Federal Savings Associations) to Enforce the CFPA and Its Regulations. Section 1042(a)(1) provides that state attorneys general "may bring a civil action . . . to enforce provisions of [the CFPA] or the regulations issued under [the CFPA]," against any defendant that is subject to state jurisdiction, and may "secure remedies under provisions of [the CFPA] or remedies otherwise provided under other law." The state attorney general may not

use this authority to bring actions against a national bank or federal savings bank.

An example of this authority would be an action by a state attorney general against a state-licensed finance company for violation of a Bureau regulation issued under Regulation Z.

Note that the state attorney general may secure both remedies provided under the CFPA, as well as remedies provided under other laws. For example, if state law authorized the state attorney general to pursue injunctive relief or civil money penalties, he or she could pursue those remedies in response to a violation of the CFPA or its regulations.

- Category 2: Actions by State Regulators Against State-Licensed or -Chartered Entities to Enforce the CFPA and Its Regulations. Section 1042(a)(1) provides that “a State regulator may bring a civil action or other appropriate proceeding to enforce provisions of [the CFPA] or the regulations issued under [the CFPA] with respect to any entity that is State-chartered . . . .” The state regulator is authorized “to secure remedies under provisions of this title or remedies otherwise provided under other provisions of law with respect to such an entity.”

The state regulator may not use this authority to bring actions against a national bank or federal savings association. This exclusion should not have been necessary because the authority provided by this provision was limited to actions against state-licensed or -chartered entities in the first instance.

An example of this authority would be an action by a state banking commissioner against a state-chartered commercial bank for violation of a Bureau regulation issued under Regulation Z.

Note that the state regulator may secure both remedies provided under the CFPA, as well as remedies provided under other laws. For example, if state law authorized a state banking commissioner to suspend or revoke a bank’s charter, he or she could pursue those remedies in response to a violation of the CFPA or its regulations.

- Category 3: Actions by State Attorneys General Against National Banks or Federal Savings Associations to Enforce CFPA Regulations. Section 1042(a)(2)(A) states that that, except as provided in Section 1042(a)(2)(B), the state attorneys general “may not bring a civil action . . . against a national bank or Federal savings association to enforce a provision of the [CFPA].” Section 1042(a)(2)(B) states that the state attorneys general may bring a civil action in federal or state court against a national bank or a federal savings association “to enforce a regulation prescribed under a provision of [the CFPA] and to secure remedies under [the CFPA] or remedies otherwise provided under other law.”

The contrasting language between Section 1042(a)(2)(A) (which prohibits the state attorneys general from bringing actions against national banks and federal savings associations to enforce the CFPA) and Section 1042(a)(2)(B) (which authorizes the state attorneys general to bring actions against national banks and federal savings associations to enforce the CFPA regulations) suggests that the state attorneys general may only bring actions under the CFPA regulations and not the CFPA itself. From this, it would follow that the state attorneys general are not authorized to bring actions relating to the CFPA against national banks and federal savings until the implementing regulations are issued and effective.

When the state attorneys general are authorized to act under Section 1042(a)(2)(B), they may secure remedies against national banks and federal savings associations that are provided under the CFPA, as well as remedies provided under other laws. For example, if state law authorized the state attorney general to pursue injunctive relief or civil money penalties, he or she could pursue those remedies in response to a violation of the CFPA regulations.

On its face, the special provisions in Section 1042(a)(2) are limited to state attorney general actions against national banks and federal savings associations. This subsection makes no reference to the operating subsidiaries of national banks and federal savings associations, suggesting that they are not covered. This is

conceptually consistent with Sections 1044 and 1045 of the Dodd-Frank Act which, as discussed below, preclude these operating subsidiaries from utilizing the benefits of federal preemption. If these operating subsidiaries are not governed by Section 1042(a)(2), it would follow that the state attorneys general can bring actions against them in accordance with Section 1042(a)(1), discussed under Category 1, above.

- Category 4: Actions by State Attorneys General or Other State Regulators to Enforce the Enumerated Consumer Laws. Once again, the CFPA defers to the Enumerated Consumer Laws where those laws themselves state when the state attorneys general or state regulators may take enforcement action under those laws. Section 1042(a)(3), which is characterized as a “Rule of Construction,” provides that “no provision of [the CFPA] shall be construed as modifying, limiting, or superseding . . . the authority of a State attorney general or State regulator to enforce [the Enumerated Consumer Laws].” The following Enumerated Consumer Laws authorize state attorneys general or state regulators to take enforcement action:
  - The FCRA provides that “if the chief law enforcement officer of a State . . . has reason to believe that any person has violated or is violating this [the FCRA] . . . [the officer] may bring an action to enjoin such violation in any appropriate United States district court or in any other court of competent jurisdiction.” 15 U.S.C. § 1681s(c). If the FTC or the appropriate federal regulator has brought an action, however, the state may not bring an action against the same defendant under this section of the FCRA for the same violation while the federal action is pending.
  - The FDIA provides that “an appropriate State supervisor of a depository institution lacking Federal deposit insurance may examine and enforce compliance with the requirements of this [section regarding depository institutions that lack Federal deposit insurance] and any regulation prescribed under this section.” 12 U.S.C. § 1831t(f). Note, however, that once the FTC has instituted an enforcement action of its own, the state supervisor may not bring an action against the defendant for the same violation.
  - The GLBA provides for state insurance authorities to enforce provisions of the GLBA regarding the disclosure of nonpublic personal information against insurance providers subject to the authorities’ jurisdiction. 15 U.S.C. § 6805(a).
  - The SAFE Act provides that “State licensing agenc[ies] shall have the authority to conduct investigations and examinations . . . [of] any loan originator licensed or required to be licensed under this title . . . [or of] the books and records relating to the operations of such originator.” 12 U.S.C. § 5114.
  - Section 626 of the Omnibus Appropriations Act of 2009, provides that a state official “may bring a civil action . . . to enforce the provisions . . . of the Truth in Lending Act . . . or any mortgage loan rule promulgated by the Federal Trade Commission to obtain penalties and relief provided under such Act or rule whenever the attorney general of the State has reason to believe that the interests of the residents of the State have been or are being threatened or adversely affected by a violation of such Act or rule.” If the FTC itself files such an action, the state may not file a civil action of its own while the FTC action is pending. Pub. L. No. 111-8.
- Category 5: Actions by State Attorneys General or Other State Regulators to Enforce State Laws. Section 1042(d) preserves state authority to take enforcement action under state law. This subsection addresses three preserved state authorities.
  - First, Section 1042(d)(1) preserves the authority of the state attorneys general and other state regulatory or enforcement agencies to bring actions or regulatory proceedings that arise solely under state law.

For example, this provision confirms the right of a state attorney general to bring an action under state law for a violation of the state’s unfair and deceptive acts and practices (“UDAP”) law.

Can the state attorneys general bring enforcement actions under an applicable state law against national

banks and federal savings associations? A literal reading of Section 1042(d)(1) would indicate that the answer is yes. This conclusion is consistent with Section 1047 of the Dodd-Frank Act, discussed below, which clarifies that the visitorial powers of the OCC do not restrict the authority of the state attorneys general to bring actions against national banks or federal savings associations to enforce applicable law. This conclusion also is consistent with the Supreme Court's decision in *Cuomo v. Clearing House Ass'n*, discussed below.

- Second, Section 1042(d)(2) preserves the authority of state securities regulators to “adopt rules, initiate enforcement proceedings, or take any other action with respect to a person regulated by [the state securities regulator].”

For example, this provision confirms the right of a state securities regulator to bring an enforcement action under state law against a company that unlawfully issues unregistered securities.

- Third, Section 1042(d)(3) preserves the authority of state insurance regulators to “adopt rules, initiate enforcement proceedings, or take any other action with respect to a person regulated by [the State insurance regulator].”

For example, this provision confirms the right of a state insurance regulator to bring an enforcement action under state law against a company that unlawfully engages in insurance underwriting.

- Consultation Required. Section 1042(b) limits the authority of the state attorneys general and state regulators to bring enforcement actions under the CFPA in accordance with Section 1042(a), as follows:

- Notice.

- In General. Section 1042(b)(1) requires the state attorney general or state regulator to notify the Bureau and any prudential regulator before initiating any court or administrative action against any covered person to enforce any provision of the CFPA or its regulations. The state attorney general or state regulator also must provide a copy of the complete complaint to be filed.

The term “covered person” is defined by Section 1002(8) of the Dodd-Frank Act to mean “any person that engages in offering or providing a consumer financial product or service; or his affiliate that acts as a service provider to such person.”

The content of the notice is discussed below. The obligation to provide a copy of the “complete complaint” presumably means the actual copy of the complaint to be filed, including any attachments.

- Emergency Action. There is an exception to the notice requirement where prior notice is “not practicable.” In that instance, the state attorney general or state regulator must provide the notice to the Bureau and any prudential regulator immediately upon instituting the action or proceeding.

There is no guidance as to when prior notice is “not practicable.” An example may be where immediate action must be taken to prevent substantial harm to consumers.

The obligation to provide the notice immediately upon instituting the action or proceeding should mean when the action or proceeding is filed, not when it is served.

The statute does not impose any sanctions upon a state attorney general or state regulator that fails to adhere to the notice requirements. Absent some provision in the Bureau's

implementing regulations to the contrary, the failure to adhere to the notice requirements is unlikely to affect the validity of the action or proceeding.

- Contents of the Notice. The statute imposes the following minimum requirements for the notice: (i) the identity of the parties, (ii) the alleged facts underlying the proceeding, and (iii) whether there may be a need to coordinate the prosecution of the proceeding so as not to interfere with any action by the Bureau, a prudential regulator, or another federal agency.

These are the minimum requirements. The Bureau's regulations may require more.

- Bureau Response. If a state attorney general or state regulator brings an action to enforce any provision of the CFPB or its regulations, Section 1042(b)(2) authorizes the Bureau to intervene in the action. If the Bureau elects to intervene in the action, the Bureau also has the right to (i) remove the action to federal district court, (ii) be heard on all matters, and (iii) appeal any order or judgment to the same extent as any other party in the proceeding.

Although the notice described above must be provided to both the Bureau and any prudential regulator, only the Bureau is given the right to intervene by Section 1042(b)(2). Presumably, if the prudential regulator believes that the Bureau should intervene, it will need to convince the Bureau to do so.

While a state attorney general or state regulator is required to provide notice with respect to either a court action or an administrative proceeding, the Bureau's right to intervene is limited to an "action" under Section 1042(b)(1), which presumably means a court action. This would indicate that the Bureau does not have the right to intervene in an administrative proceeding.

The ability to remove the action to federal district court will often be advantageous to national banks and federal savings associations that are attempting to limit a state attorney general's actions to those allowed by Section 1042(a)(2), discussed above.

The Bureau's authority under Section 1042(b)(2) is substantially less than the powers that Congress has given other federal agencies in analogous situations. For example, where the FTC or another federal regulator has filed a legal action or administrative proceeding under the FCRA, a state is prohibited from filing an action under Section 621(c) of the FCRA against the same defendant for the same violation while the federal action is pending. See 15 U.S.C. § 1681s(c)(4).

- Regulations. Section 1042(c) requires the Bureau to "prescribe regulations to implement the requirements of this section and . . . provide guidance in order to further coordinate actions with the State attorneys general and other regulators."

### **Section 1043. Preservation of Existing Contracts**

This title, 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 the date of enactment of this Act, 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.

**Analysis.** Section 1043 states that the CFPB and its implementing regulations, orders, guidances and interpretations will not affect national bank and subsidiary contracts that are in existence before the date of enactment of the Dodd-Frank Act.

The purpose of this section is to provide grandfathered benefits to contracts that were made when the prior regulatory regime for federal preemption was still in place. This is particularly critical for national banks and federal savings associations, which formed contracts in reliance upon OCC and OTS regulations that preempted a wide swath of state laws. See, e.g., 12 C.F.R. § 7.4008 (OCC preemption regulation for loans other than real estate loans); 12 C.F.R. § 7.4006 (applicability of state law to national bank operating subsidiaries); 12 C.F.R. § 560.2 (OTS preemption regulation for loans); and 12 C.F.R. § 559.3(n)(1) (applicability of state law to federal savings association operating subsidiaries).

- **Effect of Regulations, Orders, Guidances, and Interpretations on Other Items.** Section 1043 is silent with respect to the effect of federal agency regulations, orders, guidances, or interpretations on items (e.g., business practices) other than contracts. This fact, by itself, should not be taken to mean that such items, to the extent that they predate the effective date of Subtitle D, will necessarily be deprived of the federal preemptive benefits provided by such federal agency regulations, orders, guidances, or interpretations.
- **Effective Date.** Section 1043 is the only section in Subtitle D whose effectiveness is tied to the date of enactment of the Dodd-Frank Act. In contrast, Section 1048 states that Subtitle D becomes effective on the “designated transfer date,” a much later date. This inconsistency creates an ambiguity that may be resolved at some point by cleanup legislation.

The “designated transfer date” will be established by the Treasury Secretary, following consultation with other federal officials, within 60 days following enactment of the Dodd-Frank Act. The date will be no earlier than 180 days, and no later than 12 months, following enactment. The Treasury Secretary can establish a designated transfer date beyond the 12-month period by following certain procedures, but the designated transfer date may not be more than 18 months following enactment. See Section 1062 of the Dodd-Frank Act.

- **Servicing of Grandfathered Contract.** Section 1043 only references the contract itself and is silent regarding the servicing of the contract once the section is effective. This raises the question of whether a contract that is grandfathered under Section 1043 is also grandfathered with respect to the federal preemption of state laws that might otherwise apply to the servicing of the contract. The better answer is yes, under the theory that the grandfathering of the contract includes the continued application of federal law to the servicing of the same contract.

**Modification of Grandfathered Contract.** Section 1043 also is silent regarding the modification of a grandfathered contract after the section is effective. This raises the question of whether a grandfathered contract loses all or part of its grandfathered status when it is modified. The better analysis is that the contract retains its grandfathered status with respect to the existing terms, but is not grandfathered with respect to its new terms. Ironically, this may deter some companies from providing badly needed modifications to their customers.

#### **Section 1044. State Law Preemption Standards for National Banks and Subsidiaries Clarified (Charter Conflicts)**

(a) In General- Chapter one of title LXII of the Revised Statutes of the United States (12 U.S.C. 21 et seq.) is amended by inserting after section 5136B the following new section:

SEC. 5136C. STATE LAW PREEMPTION STANDARDS FOR NATIONAL BANKS AND SUBSIDIARIES CLARIFIED.

(a) Definitions- For purposes of this section, the following definitions shall apply:

(1) NATIONAL BANK- The term ‘national bank’ includes--

(A) any bank organized under the laws of the United States; and

(B) any Federal branch established in accordance with the International Banking Act of 1978.

`(2) STATE CONSUMER FINANCIAL LAWS- The term `State consumer financial law' means a State law that does not directly or indirectly discriminate against national banks and that directly and specifically regulates the manner, content, or terms and conditions of any financial transaction (as may be authorized for national banks to engage in), or any account related thereto, with respect to a consumer.

`(3) OTHER DEFINITIONS- The terms `affiliate', `subsidiary', `includes', and `including' have the same meanings as in section 3 of the Federal Deposit Insurance Act.

`(b) Preemption Standard-

`(1) IN GENERAL- State consumer financial laws are preempted, 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 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.

`(2) SAVINGS CLAUSE- This title and section 24 of the Federal Reserve Act (12 U.S.C. 371) do not preempt, annul, or affect the applicability of any State law to any subsidiary or affiliate of a national bank (other than a subsidiary or affiliate that is chartered as a national bank).

`(3) CASE-BY-CASE BASIS-

`(A) DEFINITION- As used in this section the term `case-by-case basis' refers to a determination pursuant to this section made by the Comptroller concerning the impact of a particular State consumer financial law on any national bank that is subject to that law, or the law of any other State with substantively equivalent terms.

`(B) CONSULTATION- When making a determination on a case-by-case basis that a State consumer financial law of another State has substantively equivalent terms as one that the Comptroller is preempting, the Comptroller shall first consult with the Bureau of Consumer Financial Protection and shall take the views of the Bureau into account when making the determination.

`(4) RULE OF CONSTRUCTION- This title does not occupy the field in any area of State law.

`(5) STANDARDS OF REVIEW-

`(A) PREEMPTION- A court reviewing any determinations made by the Comptroller regarding preemption of a State law by this title or section 24 of the Federal Reserve Act (12 U.S.C. 371) shall assess the validity of such determinations, 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 which the court finds persuasive and relevant to its decision.

`(B) SAVINGS CLAUSE- Except as provided in subparagraph (A), nothing in this section shall affect the deference that a court may afford to the Comptroller in making determinations regarding the meaning or interpretation of title LXII of the Revised Statutes of the United States or other Federal laws.

`(6) COMPTROLLER DETERMINATION NOT DELEGABLE- Any regulation, order, or determination made by the Comptroller of the Currency under paragraph (1)(B) shall be made by the Comptroller, and shall not be delegable to another officer or employee of the Comptroller of the Currency.

`(c) Substantial Evidence- No regulation or order of the Comptroller of the Currency prescribed under subsection (b)(1)(B), shall be interpreted or applied so as to invalidate, or otherwise declare inapplicable to a national bank, the provision of the State consumer financial law, unless 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 of Marion County, N.A. v. Nelson, Florida Insurance Commissioner, et al.*, 517 U.S. 25 (1996).

“(d) Periodic Review of Preemption Determinations-

“(1) IN GENERAL- The Comptroller of the Currency shall periodically conduct a review, through notice and public comment, of each determination that a provision of Federal law preempts a State consumer financial law. The agency shall conduct such review within the 5-year period after prescribing or otherwise issuing such determination, and at least once during each 5-year period thereafter. After conducting the review of, and inspecting the comments made on, the determination, the agency shall publish a notice in the Federal Register announcing the decision to continue or rescind the determination or a proposal to amend the determination. Any such notice of a proposal to amend a determination and the subsequent resolution of such proposal shall comply with the procedures set forth in subsections (a) and (b) of section 5244 of the Revised Statutes of the United States (12 U.S.C. 43 (a), (b)).

“(2) REPORTS TO CONGRESS- At the time of issuing a review conducted under paragraph (1), the Comptroller of the Currency shall submit a report regarding such review to the Committee on Financial Services of the House of Representatives and the Committee on Banking, Housing, and Urban Affairs of the Senate. The report submitted to the respective committees shall address whether the agency intends to continue, rescind, or propose to amend any determination that a provision of Federal law preempts a State consumer financial law, and the reasons therefor.

“(e) Application of State Consumer Financial Law to Subsidiaries and Affiliates- Notwithstanding any provision of this title or section 24 of Federal Reserve Act (12 U.S.C. 371), a State consumer financial law shall apply to a subsidiary or affiliate of a national bank (other than a subsidiary or affiliate that is chartered as 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.

“(f) Preservation of Powers Related to Charging Interest- No provision of this title shall be construed as altering or otherwise affecting the authority conferred by section 5197 of the Revised Statutes of the United States (12 U.S.C. 85) for the charging of interest by a national bank at the rate allowed by the laws of the State, territory, or district where the bank is located, including with respect to the meaning of ‘interest’ under such provision.

“(g) Transparency of OCC Preemption Determinations- The Comptroller of the Currency shall publish and update no less frequently than quarterly, a list of preemption determinations by the Comptroller of the Currency then in effect that identifies the activities and practices covered by each determination and the requirements and constraints determined to be preempted.’

(b) Clerical Amendment- The table of sections for chapter one of title LXII of the Revised Statutes of the United States is amended by inserting after the item relating to section 5136B the following new item:

‘Sec. 5136C. State law preemption standards for national banks and subsidiaries clarified.’

**Analysis.** Section 1044 establishes a new regime for national bank federal preemption in the area of state consumer financial laws. Section 1044 does so by adding a new Section 5136C to the National Bank Act (“NBA”). This new statute identifies three categories of state consumer financial laws that are preempted, explains the process by which the OCC may make preemption determinations, provides a standard for court reviews of OCC preemption determinations, requires periodic reviews of OCC preemption determinations and reporting to Congress, clarifies the applicability of federal preemption to operating subsidiaries, and confirms the continued viability of the interest rate exportation doctrine.

Historically, the courts have recognized a presumption against preemption of state laws, but have not applied this presumption in the case of highly regulated industries such as banking. Does new Section 5136C’s limitation of preemption to three specific categories of consumer financial laws suggest that there is now a presumption against preemption by OCC regulations and orders? The better reading of Section 5136C is that the answer should be no. While Section 5136C could have stated that there is a presumption against preemption, it does not do so. The restriction of preemption to three identified categories does not mean that, within each of those categories, there is a presumption against preemption. Moreover, in a colloquy that was added to the public record on the day of the Senate vote, Senator Christopher Dodd (D-CT) made clear that the preemption standard was intended to codify the United States Supreme Court decision in the *Barnett Bank* case (discussed below), and the cases post-dating

*Barnett Bank* have not created a presumption against preemption. Finally, the savings clause in Section 5136C, which preserves the court doctrine of showing deference to the OCC's interpretations of the NBA, suggests strongly that there is no presumption against preemption. In any event, there should be no presumption against preemption with respect to state laws other than consumer financial laws.

- State Consumer Financial Laws. A state consumer financial law is “a state law that does not directly or indirectly discriminate against national banks and that directly and specifically regulates the manner, content, or terms and conditions of any financial transaction (as may be authorized for national banks to engage in), or any account related thereto, with respect to a consumer.” See Section 5136C(a)(2).

The first criterion seems straightforward: state consumer financial laws may not treat national banks differently than state banks or other companies.

The second criterion is less clear. Are state consumer financial laws limited to those that, by their express terms, regulate the terms and the like of consumer financial transactions and accounts (e.g., a state law establishing a specific maximum debt-to-income ratio for a mortgage loan), or do those laws include state laws that do not specifically regulate loan terms and the like but, as applied, may result in restrictions on the terms and the like of consumer financial transactions and accounts (e.g., state UDAP laws)? Section 5136C(a)(2) states these laws must “directly and specifically” regulate the terms and the like of consumer financial transactions and accounts, indicating that the better interpretation is that state consumer financial laws are limited to those that, by their express terms, regulate the terms and the like of consumer financial transactions and accounts.

The definition of “state consumer financial law” in Section 5136C(a)(2) is limited to a financial transaction or an account “with respect to a consumer.” This means that the definition, and the scope of Section 5136C itself, is limited to consumers. This would exclude commercial transactions, and transactions with corporations and other business entities. This definition should also exclude other financial matters that are of concern to national banks, such as state licensing and registration laws and state laws regulating capital requirements. These categories of state laws should be governed by existing federal preemption law and precedent.

- Preemption Standard. Section 5136C(b) identifies the following three categories of state consumer financial laws that are preempted. The statute states that state consumer financial laws are not preempted in any other situations.
  - The first situation is where “the 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.” See Section 5136C(b)(1)(A).

An example would be a state law that allows state banks to provide residential mortgage loans with maximum loan-to-value ratios of 95% while limiting the maximum loan-to-value ratios of loans made by all other lenders—which would necessarily include national banks—to 80%. Because this law would have a discriminatory effect on national banks, it would be preempted with respect to national banks.

Note that any state law that directly or indirectly discriminates against national banks would be excluded from the definition of a “state consumer financial law” in the first instance. See discussion of Section 5136C(a)(2), above.

- The second situation is where, “in accordance with the legal standard for preemption in the decision of the Supreme Court . . . in *Barnett Bank of Marion County, N.A. v. Nelson, Florida Insurance Commissioner, et al.* . . . the State consumer financial law prevents or significantly interferes with the exercise by the national bank of its powers . . .” Any preemption determination under this standard may be made by a court, or by a regulation or order of the OCC “on a case-by-case basis, in accordance with applicable law.” See Section 5136C(b)(1)(B).

In *Barnett Bank*, a Florida law prohibited any Florida-licensed insurance agent that was associated with or owned by a financial institution from engaging in certain insurance agency activities. The Florida statute defined a financial institution to be “any bank [except for a] bank that is not a subsidiary or affiliate of a bank holding company and is located in city having a population of less than 5,000 people.” Barnett Bank, a national bank that was affiliated with a bank holding company, bought a Florida-licensed insurance agency with the intent to sell insurance through a branch in a town with less than 5,000 people, as expressly authorized by the NBA. The Florida Insurance Commissioner ordered the branch of Barnett Bank to stop selling the prohibited forms of insurance based on the state law. Barnett Bank filed an action for declaratory and injunctive relief, claiming that the federal statute preempted the state statute. The Court noted that “where Congress has not expressly conditioned the grant of “power” upon a grant of state permission, the Court has ordinarily found that no such condition applies.” The Court held that the federal statute in question was a specific grant of “power” to national banks, which are “not normally limited by, but rather ordinarily preempting, contrary State law.” The Court further held that “in defining the preemptive scope of statutes and regulations granting a power to national banks, [the Court] takes[s] the view that normally Congress would not want States to forbid, or impair significantly, the exercise of a power that Congress explicitly granted. To say this is not to deprive States of the power to regulate national banks, where . . . doing so *does not prevent or significantly interfere with the national bank’s exercise of its powers.*” *Id.* at 33 (emphasis added). Based on this standard, the Court held that the Florida statute was preempted. (The Court also dismissed a challenge to preemption based upon the McCarran Ferguson Act.)

The wording of Section 5136C(b)(1)(B) could raise the issue of whether the statute intended to narrow the federal preemption standard established by *Barnett Bank*. A colloquy that was added to the public record on July 15, 2010 between Senator Dodd and Senator Thomas Carper (D-DE) confirms that “the Conference Report still maintains the *Barnett* standard for determining when a State law is preempted.” As Senator Dodd stated in this colloquy, “There should be no doubt that the legislation codifies the preemption standard stated by the United States Supreme Court in that case.”

Examples of state laws that would be preempted under the *Barnett Bank* standard would be those that purport to prohibit a national bank from making mortgage loans, discounting notes, or taking deposits.

A discussion of the OCC’s required procedures for making preemption determinations is set forth below.

Note that the only agency authorized to make preemption determinations under Section 5136C is the OCC. The Bureau is not authorized to make preemption determinations under Section 5136C.

- The third situation is where “the State consumer financial law is preempted by a provision of Federal law other than [the CFPA].”

An example is 12 U.S.C. § 1701j–3, which preempts certain state laws that purport to restrict the exercise of due-on-sale clauses in mortgage documents. This statute is not part of the NBA, but it nonetheless provides the benefits of federal preemption to national banks.

- Savings Clause (Treatment of Subsidiaries and Affiliates). Section 5136C(b)(2) is the first of three provisions in Subtitle D that addresses the use of the federal preemption doctrine by subsidiaries and affiliates of national banks. Section 5136C(b)(2) states that the CFPA and 12 U.S.C. § 371 (which authorizes national banks to make real estate loans and provides certain treatment for certain discounted real estate loan notes) “do not preempt, annul, or affect the applicability of any State law” to any subsidiary or affiliate of a national bank, other than any subsidiaries or affiliates that are themselves national banks.

This subsection was particularly directed to operating subsidiaries of national banks. Currently, 12

C.F.R. § 7.4006 states that, “Unless otherwise provided by Federal law or OCC regulation, State laws apply to national bank operating subsidiaries to the same extent that those laws apply to the parent national bank.” The OCC’s extension of the federal preemption doctrine to operating subsidiaries of national banks was upheld by the Supreme Court in *Watters v. Wachovia Bank*. 550 U.S. 1 (2007). In that case, Wachovia Bank brought suit seeking declaratory and injunctive relief when Michigan regulators sought to regulate a mortgage lending corporation that was an operating subsidiary of Wachovia Bank. The Michigan regulators contended that they were not exercising visitatorial control over the national bank, but instead over a nonbank subsidiary incorporated under state law. The Court held that national banks and their operating subsidiaries operate “as a single economic enterprise.” The Court pointed to the Gramm-Leach-Bliley Act, which provides that operating subsidiaries may engage only in activities national banks may engage in directly, “subject to the same terms and conditions that govern the conduct of such activities by national banks.” Based in large part on this statutory guidance, the Court held that Wachovia’s operating subsidiary was subject to the exclusive visitatorial control of the OCC. (Another part of the opinion limited the scope of the OCC’s visitatorial powers, discussed with respect to Section 1047 of the Dodd-Frank Act, below.) Section 5136C(b)(2) overturns both the OCC’s regulation at 12 C.F.R. § 7.4006 and the Supreme Court’s decision in *Watters*.

As a result of this savings clause and other provisions in Subtitle D, an operating subsidiary of a national bank will not be able to utilize the federal preemption benefits provided to national banks by Section 5136C(b)(1). For example, a national bank operating subsidiary that engages in small-loan consumer lending will be required to hold lending licenses or registrations in every state that imposes such requirements on such lenders.

Subjecting operating subsidiaries to state consumer financial laws will require national banks that own operating subsidiaries to reconsider their organizational structure. A national bank may wish to consider merging its operating subsidiary into the bank, thereby allowing the business of the operating subsidiary to be conducted in the national bank itself. This, in turn, will provide the benefits of the federal preemption doctrine (as modified by Section 5136C) to the business of the former operating subsidiary. In concept, the national bank also could obtain a national bank charter for the operating subsidiary, enabling it to benefit from the federal preemption doctrine on its own. In addition to the expense and burden of complying with state consumer financial laws, national banks should consider the costs and benefits of such reorganizations, as well as corporate, tax, personnel, and other relevant considerations.

There are two instances in which national bank operating subsidiaries continue to enjoy exemptions from state law. The first instance is where a separate federal statute expressly preempts the state law. An example is 12 U.S.C. § 1701j-3, which preempts certain state laws that purport to restrict the exercise of due-on-sale clauses in mortgage documents. This statute applies to all lenders, and national bank operating subsidiaries can take advantage of the preemptive benefits of this statute to the same extent as any other corporation. The second instance is where the state law itself provides an exemption for a national bank operating subsidiary. See, e.g., California Financial Code § 3707, which provides an exemption from the interest rate limitations of Article XV, § 1 (the California usury law) to nonbank subsidiaries of bank holding companies.

- Case-by-Case Basis (OCC Preemption Determinations). This is the first of several subsections that regulate the process by which the OCC makes preemption determinations, and the review of those determinations by the courts.

Congress has established an arduous path for the making of preemption determinations in an effort to discourage the OCC from making a large number of those determinations. While the procedures for OCC preemption determinations are no doubt burdensome, they are by no means insurmountable. OCC should be readily able to implement those determinations. The future of national bank preemption will largely be governed by the OCC’s willingness to undertake a great number of preemption determinations.

The NBA already contains a procedure that the OCC must follow before it issues an opinion letter or interpretive rule concluding that federal law preempts a state law in the areas of community reinvestment, consumer protection, fair lending, and the establishment of interstate branches, before it makes certain determinations regarding certain discriminatory state laws affecting interstate branches. The OCC is required to publish notice of its intended issuance, take comments, consider the comments, and publish any final opinion letter or interpretive rule. There are certain exceptions. See 12 U.S.C. § 43. Nothing in Section 5136C obviates the OCC's obligation to continue to comply with these requirements.

- Definition. As noted above, Section 5136C(b)(1)(B) states that preemption determinations may be made either by a court, or by a regulation or order of the OCC on a "case-by-case basis." Section 5136C(b)(3)(A) states that the OCC must make a preemption determination "concerning the impact of a particular State consumer financial law on any national bank that is subject to that law, or the law of any other State with substantively equivalent terms."

The reference to a preemption determination for a "particular State consumer financial law" most likely means that, except as discussed below, the OCC must make a separate preemption determination for each individual state's consumer financial law. For example, existing 12 C.F.R. § 7.4008(d)(2)(iv) preempts state lending laws (for non-real estate loans) that purport to regulate the "terms of credit." Presumably, this regulation will not meet the new case-by-case standard, since it does not deal with the impact of a "particular" state consumer financial law.

Will the new case-by-case standard require a separate determination for each individual national bank? The answer should be no, because Section 5136C(b)(3)(A) expressly states that the OCC must make its preemption determination concerning the impact of a particular state consumer financial law "on *any* national bank that is subject to that law" (emphasis added).

Will the new case-by-case standard allow the OCC to make a preemption determination for one state's consumer financial law that will also apply to other states' consumer financial laws? The answer is yes, because Section 5136C(b)(3)(A) expressly states that the OCC must make its preemption determinations concerning the impact of a particular state consumer financial law "or the law of any other State with substantively equivalent terms." There is no guidance on how the "substantively equivalent terms" standard will be applied; see discussion below regarding the OCC's obligation to consult with the Bureau. A fairly clear example of the proper use of the "substantively equivalent terms" standard will be where multiple states adopt the same model act. In this situation, the OCC should be able to make a preemption determination for one state's act and then apply that preemption determination to all of the identical states' acts. However, the OCC may also be able to employ the "substantively equivalent terms" standard in other circumstances as well.

- Consultation (with the Bureau). Section 5136C(b)(3)(B) requires the OCC to consult with the Bureau and "take the views of the Bureau into account when making a determination on a case-by-case basis" that a state consumer financial law has substantively equivalent terms as one that the OCC is preempting.

The OCC's duty to consult with the Bureau and to take the Bureau's views into consideration will, as a practical matter, require the OCC to exercise its power to preempt multiple states' laws judicially.

Note that this is the only situation in which the OCC must consult with the Bureau. Where the

OCC wishes to make a preemption determination with respect to an individual state consumer law, Section 5136C(b)(3)(B) does not require it to consult with the Bureau.

- Rule of Construction. Section 5136C(b)(4) states that the NBA does not “occupy the field” in any area of state law. This means that there is no area of law that is so pervasively regulated by the NBA that there is no room left for the states to legislate. However, even though the NBA does not occupy the field in any area, individual state laws may continue to be preempted by the courts or by OCC order or regulation, in accordance with applicable law.

A historical note: When the OCC issued its preemption regulations relating to lending in 2004, those regulations did not purport to preempt the field of lending regulation. The OCC has stated that it had the authority to occupy the field of real estate lending regulation but chose not to. See, e.g., OCC Quarterly Journal “On Preemption and Visitorial Powers,” Vol. 23, No. 1 at 92 (March 2004) (“[Although the OCC] believe[s] the history of [12 U.S.C.] § 371 indicates that Congress left open the possibility that the OCC would occupy the field of national bank real estate lending through regulation, the OCC has not exercised the full authority inherent in § 371 in the final rule”). In contrast, the OTS regulation relating to lending did occupy the entire field of lending regulation for federal savings associations. Compare 12 C.F.R. § 7.4008 and § 34.4 with 12 C.F.R. § 560.2(a).

- Standards of Review. Section 5136C(b)(5) describes the standards by which the courts will review preemption determinations by the OCC. Keep in mind that, under Section 5136C(b)(1)(B), both the courts and the OCC may make preemption determinations relating to state consumer financial laws. The standards set forth below apply only to court reviews of OCC preemption determinations.
  - Preemption. Section 5136C(b)(5)(A) states that the courts shall assess the validity of the OCC’s preemption determinations under the CFPA and 12 U.S.C. § 371 (which authorizes national banks to make real estate loans and provides certain treatment for certain discounted real estate loan notes). The courts are to make this assessment based upon the thoroughness evident in the OCC’s consideration, the validity of the OCC’s reasoning, the consistency with the OCC’s other valid determinations, and other factors that the court finds persuasive and relevant to their decision.
  - Savings Clause. Section 5136C(b)(5)(B) states that Section 5136C(b)(5)(A) “shall not affect the deference that a court may afford to the Comptroller in making determinations regarding the meaning or interpretation of [the NBA] or other Federal laws.” This is a reasonably clear reference to the Supreme Court’s *Chevron* decision, which provides the framework for federal agency deference. Under *Chevron*, a court will first ask “whether Congress has directly spoken to the precise question at issue.” 467 U.S. 837, 842 (1984). If the intent of Congress is not clear, then the court asks “whether the agency’s answer is based on a permissible construction of the statute.” *Id.* at 843. If the court affirmatively answers the second question, then the agency’s “regulations are given controlling weight unless they are arbitrary, capricious, or manifestly contrary to the statute.” *Id.* at 844.

While the courts are directed to review the thoroughness of the OCC’s consideration, the validity of the OCC’s reasoning, the consistency with the OCC’s other determinations, and other relevant factors, the better reading is that this does not rise to the level of a de novo review of the OCC’s preemption determinations by the courts. Presumably, if Congress wanted the courts to make de novo reviews of the OCC’s preemption determinations, Section 5136C(b)(5) would have been so drafted. To the contrary, Section 5136C(b)(5)(A) mandates that the courts assess specific factors in the OCC’s preemption determination. This conclusion that a de novo standard is not required is corroborated by Section 5136C(b)(5)(B), which confirms that the courts must continue to show deference to the OCC, presumably in accordance with the *Chevron* standard. If Section 5136C(b)(5)(A) were to mandate a de novo

review by the courts, the preservation of OCC deference in Section 5136C(b)(5)(B) would be nonsensical.

- Comptroller Determination Not Delegable. Section 5136C(b)(6) requires the Comptroller him/herself to make state consumer financial law preemption determinations, and states that these determinations “shall not be delegable to another officer or employee of the [OCC].”

This subsection was added because the OCC’s Chief Counsel had written a succession of interpretive letters that concluded that specific state laws were preempted. The Chief Counsel will no longer be able to do so, and preemption determinations will now be made by the Comptroller in accordance with the procedures described in Section 5136C.

However, nothing in Section 5136C(b)(6) precludes the Comptroller from using the Chief Counsel’s office or other OCC employees in performing the prefatory work necessary to enable him or her to make preemption determinations. Nothing in Section 5136C(b)(6) prohibits the Chief Counsel from providing interpretive advice to the Comptroller. In practice, Section 5136C(b)(6) should have little impact on the flow of preemption determinations from the OCC.

Note that Section 5136C(b)(6) is, by its terms, limited to preemption determinations with respect to state consumer financial laws. It does not preclude the Chief Counsel from continuing to issue interpretive letters regarding preemption matters on other types of state laws.

- Substantial Evidence. Section 5136C(c) states that a state consumer financial law will not be interpreted to be preempted by an OCC regulation or order “unless 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 [*Barnett Bank*].”

The language of this subsection is unclear. The requirement of “substantial evidence, made on the record of the proceeding” could be interpreted to invoke certain procedural safeguards imposed by the Administrative Procedures Act (“APA”). The APA imposes these safeguards “when rules are required by statute to be *made on the record* after opportunity for an *agency hearing*.” 5 U.S.C. § 553(c) (emphasis added). Although Sections 5136C(b)(1)(B) and 5136C(c) do not specifically require an agency hearing, if the reference to a “proceeding” in Section 5136C(c) were deemed sufficient to qualify as a requirement for an “agency hearing” the OCC would be required to comply with additional APA procedural including restrictions on ex parte communications in the rulemaking process. See 5 U.S.C. §§ 556, 557.

Note that Section 5136C(c) is, by its terms, limited to preemption determinations with respect to state consumer financial laws. It does not require a similar record of substantial evidence to support OCC preemption determinations relating to other types of state laws.

- Periodic Review of Preemption Determinations. Section 5136C(d) requires the OCC to conduct periodic reviews of its determination that a state consumer financial law is preempted by an OCC regulation or order. Each preemption determination must be reviewed at least every five years. The review requires notice, the receipt of public comments, and publication of a notice in the Federal Register announcing the OCC’s decision to continue the preemption determination, rescind the preemption determination, or amend the preemption determination. Any notice of a proposal to amend, and the subsequent resolution of that proposal, must follow the existing procedural requirements of the NBA relating to preemption determinations. These requirements, which are set forth at 12 U.S.C. § 43, are discussed above. The OCC is required to forward reports of its preemption reviews, and its decisions relating to preempted state consumer financial laws, to the House Financial Services Committee and Senate Banking Committee.

Section 5136C(d) is yet another procedural burden that Congress has imposed on the OCC to make the preemption determination process as arduous and unpleasant as possible. The periodic review requirement is

intended to pressure the OCC to minimize the number of preemption determinations it makes and keeps in place.

Note that Section 5136C(d) is limited to preemption determinations relating to state consumer financial laws. It does not require similar periodic reviews of preemption determinations relating to other types of state laws.

- Application of State Consumer Financial Law to Subsidiaries and Affiliates. Section 5136C(e) is the second provision that confirms Congress's intent to apply state consumer financial laws to operating subsidiaries of national banks. "A State consumer financial law shall apply to a subsidiary or affiliate of a national bank (other than a subsidiary or affiliate that is chartered as 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."

This subsection further underscores Congress's rejection of the Supreme Court's *Wachovia* decision and 12 C.F.R. § 7.4006, as discussed above. Section 5136C(e) is more targeted than the broad statement in Section 5136C(b)(2), because it applies only to state consumer financial laws.

- Preservation of Powers Related to Charging Interest. Section 5136C(f) confirms that nothing in the CFPA alters or otherwise affects the ability of national banks to utilize the interest rate exportation doctrine set forth at 12 U.S.C. § 85. This specifically includes "the meaning of 'interest' under [12 U.S.C. § 85]."

The confirmation of the continued viability of 12 U.S.C. § 85 is extremely important to national banks. The specific inclusion of "the meaning of 'interest' under [12 U.S.C. § 85]" would best be interpreted to mean that 12 C.F.R. § 7.4001, the OCC regulation that interprets the meaning of interest for purposes of 12 U.S.C. § 85, remains alive and well. The validity of this regulation was upheld by the Supreme Court in *Smiley v. Citibank, N.A.*, 517 U.S. 735 (1996). The reference to the "meaning of interest" also would best be interpreted to include existing precedents relating to the preemption of state laws purporting to regulate interest calculation methods or purporting to impose notice requirements.

Note that Section 1027(o) of the Dodd-Frank Act prohibits the Bureau from establishing usury limits, except where otherwise provided by law.

The OCC Chief Counsel's office has issued several interpretive opinions concluding that national bank operating subsidiaries may also utilize the interest rate exportation doctrine set forth at 12 U.S.C. § 85. See, e.g., OCC Interpretive Letter No. 954 (December 16, 2002). Given the enactment of Sections 5136C(b)(2), 5136C(e), and 5136C(h), these letters are no longer viable.

- Transparency of OCC Preemption Determinations. Section 5136C(g) requires the OCC to publish, at least quarterly, a "list of preemption determinations by the Comptroller . . . [that are] then in effect that identifies the activities and practices covered by each determination and the requirements and constraints determined to be preempted."

This is yet another procedural burden that Congress has imposed on the OCC to make the preemption determination process arduous, and to pressure the OCC to minimize the number of its preemption determinations.

- Effect of Section 5136C on Select Existing OCC Preemption Regulations. Once Section 5136C is effective, it would be prudent to no longer rely upon the preemptive effects of 12 C.F.R. § 7.4002 (national bank charges), § 7.4007 (deposit taking), § 7.4008 (non-real estate lending), § 7.4009 (applicability of state law to national bank operations), and § 34.4 (applicability of state law to real estate loans). In contrast, the preemptive effects of OCC regulations such as 12 C.F.R. § 7.4003 (establishment and operations of a remote service unit by a national bank) should not be affected by the enactment of Section 5136C.

## Section 1045. Clarification of Law Applicable to Nondepository Institution Subsidiaries

Section 5136C of the Revised Statutes of the United States (as added by this subtitle) is amended by adding at the end the following:

(h) Clarification of Law Applicable to Nondepository Institution Subsidiaries and Affiliates of National Banks-

(1) DEFINITIONS- For purposes of this subsection, the terms 'depository institution', 'subsidiary', and 'affiliate' have the same meanings as in section 3 of the Federal Deposit Insurance Act.

(2) RULE OF CONSTRUCTION- No provision of this title or section 24 of the Federal Reserve Act (12 U.S.C. 371) shall be construed as preempting, annulling, or affecting the applicability of State law to any subsidiary, affiliate, or agent of a national bank (other than a subsidiary, affiliate, or agent that is chartered as a national bank).'

**Analysis.** Section 1045 adds Section 5136C(h) to the NBA. Section 5136C(h) is the third subsection that confirms Congress's intent to apply state law to operating subsidiaries of national banks. It states that "No provision of [the CFPA] or 12 U.S.C. § 371 (which authorizes national banks to make real estate loans and provides certain treatment for certain discounted real estate loan notes) shall be construed as preempting, annulling, or affecting the applicability of State law to any subsidiary, affiliate, or agent of a national bank (other than a subsidiary, affiliate, or agent that is chartered as a national bank)."

This subsection further underscores Congress's rejection of the Supreme Court's *Wachovia* decision and 12 C.F.R. § 7.4006, as discussed above. Section 5136C(h) is substantively similar to Section 5136C(b)(2), discussed above. Both of those subsections are more broad based than Section 5136(e) because they apply to all laws, rather than state consumer financial laws alone.

## Section 1046. State Law Preemption Standards for Federal Savings Associations and Subsidiaries Clarified

(a) In General- The Home Owners' Loan Act (12 U.S.C. 1461 et seq.) is amended by inserting after section 5 the following new section:

SEC. 6. STATE LAW PREEMPTION STANDARDS FOR FEDERAL SAVINGS ASSOCIATIONS CLARIFIED.

(a) In General- Any determination by a court or by the Director or any successor officer or agency regarding the relation of State law to a provision of this Act or any regulation or order prescribed under this Act shall be made in accordance with the laws and legal standards applicable to national banks regarding the preemption of State law.

(b) Principles of Conflict Preemption Applicable- Notwithstanding the authorities granted under sections 4 and 5, this Act does not occupy the field in any area of State law.'

(b) Clerical Amendment- The table of sections for the Home Owners' Loan Act (12 U.S.C. 1461 et seq.) is amended by striking the item relating to section 6 and inserting the following new item:

Sec. 6. State law preemption standards for Federal savings associations and subsidiaries clarified.'

**Analysis.** Section 1046 is designed to bring the preemption standards and procedures for federal savings associations into parity with those applicable to national banks.

- **In General.** Section 1046(a) establishes a new Section 6(a) of the Home Owners' Loan Act ("HOLA"), which provides that "[a]ny determination by the Director [of the OTS] or any successor officer or agency [i.e., the OCC] regarding the relation of State law to a provision of [HOLA] or any regulation or order prescribed under [HOLA] shall be made in accordance with the laws and legal standards applicable to national banks regarding the preemption of State law."

Congress took this short-handed approach with respect to controlling federal preemption determinations for federal savings associations rather than enacting a provision in HOLA that was the equivalent of Section 5136C. Congress has taken this “incorporation by reference” approach to drafting provisions in HOLA before. For example, another section of HOLA incorporates the requirements of Sections 22(g) and (h), 23A, and 23B of the Federal Reserve Act. See 12 U.S.C. § 1468.

- Principles of Conflict Preemption Applicable. Section 6(b) of HOLA states that “[n]otwithstanding the authorities granted under sections 4 and 5 [of HOLA], [HOLA] does not occupy the field in any area of State law.”

With this simple amendment, Congress has rescinded decades of precedent relating to the scope of federal savings association federal preemption. Note that the elimination of field preemption applies with respect to “any area of State law,” and is not limited to state consumer financial laws. Historical note: Section 3 of HOLA requires the Director of the OTS to “provide for the examination, safe and sound operation, and regulation of savings associations.” 12 U.S.C. § 1463(a)(1). The OTS has been granted plenary authority to regulate all aspects of the operations of federal savings associations. See, e.g., the Supreme Court’s decision in *Fidelity Federal Savings and Loan Association v. de la Cuesta*, citing legislative history in finding that Congress intended the federal thrift regulator to have “plenary authority over Federal [savings associations, and] Federal law alone would continue to govern [the activities of Federal savings associations].” 458 U.S. 141, 167 (1982) (quoting Representative Hanley).

- Effect of Section 6 on Select Existing OTS Preemption Regulations. Once Section 6 is effective, it would be prudent to no longer rely upon the preemptive effects of 12 C.F.R. § 557.12 (examples of state laws governing deposits that are preempted); § 559.3(n)(1) (extension of federal preemption benefits to operating subsidiaries of federal savings associations); § 560.2 (applicability of state lending laws); and Part 528 (nondiscrimination requirements). In contrast, the preemptive provisions of 12 C.F.R. Part 590 (first lien residential mortgage loan exemption from state usury laws) and Part 591 (enforceability of due-on-sale clauses) should remain effective because these implement provisions of other federal statutes that expressly provide for the preemption of state law.

## Section 1047. Visitorial Standards for National Banks and Savings Associations

(a) National Banks- Section 5136C of the Revised Statutes of the United States (as added by this subtitle) is amended by adding at the end the following:

“(i) Visitorial Powers-

“(1) IN GENERAL- In accordance with the decision of the Supreme Court of the United States in *Cuomo v. Clearing House Assn., L. L. C.* (129 S. Ct. 2710 (2009)), no provision of this title which relates to visitorial powers or otherwise limits or restricts the visitorial authority to which any national bank is subject shall be construed as limiting or restricting the authority of any attorney general (or other chief law enforcement officer) of any State to bring an action against a national bank in a court of appropriate jurisdiction to enforce an applicable law and to seek relief as authorized by such law.

“(j) Enforcement Actions- The ability of the Comptroller of the Currency to bring an enforcement action under this title or section 5 of the Federal Trade Commission Act does not preclude any private party from enforcing rights granted under Federal or State law in the courts.’

(b) Savings Associations- Section 6 of the Home Owners’ Loan Act (as added by this title) is amended by adding at the end the following:

“(c) Visitorial Powers- The provisions of sections 5136C(i) of the Revised Statutes of the United States shall apply to Federal savings associations, and any subsidiary thereof, to the same extent and in the same manner as if such savings associations, or subsidiaries thereof, were national banks or subsidiaries of national banks, respectively.’

(d) Enforcement Actions- The ability of the Comptroller of the Currency to bring an enforcement action under this Act or section 5 of the Federal Trade Commission Act does not preclude any private party from enforcing rights granted under Federal or State law in the courts.'

**Analysis.** Section 1047 amends the NBA and the HOLA to confirm a narrowing of the visitorial powers of the OCC (for national banks) and the OTS (or its successor, for federal savings associations). It also confirms the rights of private parties to pursue enforcement rights granted by federal and state law.

- **National Banks.** Section 1047(a) adds a new Section 5136C(i), which codifies the Supreme Court's holding in *Cuomo v. Clearing House Association, L.L.C.*, 557 U.S. \_\_\_\_, 129 S. Ct. 2710 (2009). Section 5136C(i) states that "[i]n accordance with the decision of the Supreme Court of the United States in *Cuomo v. Clearing House Assn., L.L.C.* . . . , no provision of [the NBA] which relates to visitorial powers or otherwise limits or restricts the visitorial authority to which any national bank is subject shall be construed as limiting or restricting the authority of any State to bring an action against a national bank . . . to enforce an applicable law and to seek relief as authorized by such law."

In the *Clearing House* case, the New York attorney general sent letters to several national banks requesting non-public information relating to their fair lending performance. The national banks, which were members of the Clearing House Association, brought suit to enjoin the information request, claiming that the attorney general was intruding upon the OCC's exclusive visitorial powers. Under 12 C.F.R. § 7.4000(a)(2), "visitorial powers" included "(i) Examination of a bank; (ii) Inspection of a bank's books and records; (iii) Regulation and supervision of activities authorized or permitted pursuant to federal banking law; and (iv) Enforcing compliance with any applicable federal or state laws concerning those activities." The OCC regulations prohibited state officials from exercising visitorial powers with respect to national banks, except where authorized by federal law or regulation or the court. 12 C.F.R. § 7.4000(a)(1), (b). The Supreme Court affirmed the District Court's injunction, finding that the New York attorney general was attempting to exercise visitorial powers when he or she requested nonpublic information without a subpoena, noting that such visitorial powers did not fall within any of the regulatory exceptions under 12 C.F.R. § 7.4000(b). However, the Court also vacated the lower court's decision in part, holding that state attorneys general were not prohibited from bringing judicial enforcement actions against national banks.

With the enactment of Section 5136C(i), Congress has confirmed the *Clearing House* decision's narrower construction of the OCC's visitorial powers. The visitorial powers do not preclude the state attorneys general from pursuing otherwise lawful enforcement actions against national banks, but the state attorneys general are not authorized by the new statute to enforce nonsubpoena requests for information. Note that any action by the state attorneys general against national banks must comply with other applicable laws, including Section 1042 of the Dodd-Frank Act, discussed above.

- **Federal Savings Associations.** Section 1047(b) establishes a new Section 6(c) of the HOLA, which incorporates and applies the limitations on visitorial powers relating to national banks to the visitorial powers relating to federal savings associations and their subsidiaries.
- **Enforcement Actions.** Section 1047 also preserves private parties' ability to enforce rights granted under federal and state law in the courts. Sections 1047 (a) and (b) provide, in identical language, that "the ability of the Comptroller of the Currency to bring an enforcement action under [the NBA or the HOLA, as applicable, or Section 5 of the Federal Trade Commission Act] does not preclude any private party from enforcing rights granted under Federal or State law in the courts."

Note that Section 1047 does not, in itself, grant any new rights to private parties to bring enforcement actions but merely confirms that the right of the OCC to bring enforcement actions does not preclude private parties from bringing enforcement actions of their own when they have a lawful basis for doing so.

## Section 1048. Effective date

This subtitle shall become effective on the designated transfer date.

**Analysis.** Section 1048 states that the effective date for Subtitle D is the “designated transfer date.”

See discussion regarding Section 1043 (preservation of existing contracts), above, regarding (i) the establishment of the “designated transfer date,” and (ii) the inconsistency between the effective date of Subtitle D and the effective date of Section 1043.

---

### Contacts

Joseph Gabai  
(213) 892-5284  
[jgabai@mofo.com](mailto:jgabai@mofo.com)

William Stern  
(415) 268-7637  
[wstern@mofo.com](mailto:wstern@mofo.com)

Jeremy Mandell  
(202) 887-1589  
[jmandell@mofo.com](mailto:jmandell@mofo.com)

---

### About Morrison & Foerster

We are Morrison & Foerster—a global firm of exceptional credentials. Our clients include some of the largest financial institutions, investment banks, Fortune 100, technology and life science companies. We've been included on *The American Lawyer's* A-List for seven straight years, and *Fortune* named us one of the “100 Best Companies to Work For.” Our lawyers are committed to achieving innovative and business-minded results for our clients, while preserving the differences that make us stronger. This is MoFo. Visit us at [www.mofo.com](http://www.mofo.com).

© 2010 Morrison & Foerster LLP. All rights reserved.

*Because of the generality of this update, the information provided herein may not be applicable in all situations and should not be acted upon without specific legal advice based on particular situations.*