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11 IN THE UNITED STATES DISTRICT COURT
12 FOR THE EASTERN DISTRICT OF CALIFORNIA

14 NATIONAL CITY BANK OF INDIANA
15 and
16 NATIONAL CITY MORTGAGE CO,

17 Plaintiffs,

18 v.

19 DEMETRIOS A. BOUTRIS,
20 in his official capacity as Commissioner of
21 the California Department of Corporations,

22 Defendant.

Civil Action No.: S 03-0655 LKK DAD

APPENDIX TO MEMORANDUM OF
POINTS AND AUTHORITIES IN
SUPPORT OF PLAINTIFFS' MOTION
FOR PRELIMINARY INJUNCTION

BY FAX

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Fax & File

1 Authorities Not Reported in Federal Reporter

2 Preliminary Injunction Order, *Wells Fargo Bank, N.A. v.* A
3 *Bourris*, No. 03-0157 GEB JFM (March 10, 2003)

4 OCC Interpretive Letter No. 749 (Sept. 13, 1996) B

5 OCC Interpretive Letter No. 644 (March 24, 1994) C

6 Letter from Julie L. Williams, First Deputy Comptroller D
7 and Chief Counsel, Office of the Comptroller of
8 the Currency, to Demetrios A. Boutris, Commissioner,
9 California Department of Corporations
(February 11, 2003)

10 OCC Interpretive Letter No. 614 (January 15, 1993) E

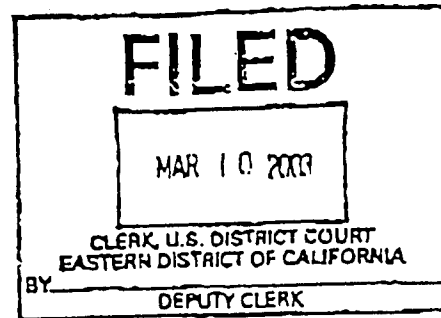
11 Preliminary Injunction Order, *Bank of America, N.A. v.* F
12 *City and County of San Francisco*, No.
13 C 99 4817 VRW (November 15, 1999)
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APPENDIX A

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APPENDIX A



IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF CALIFORNIA

WELLS FARGO BANK, N.A., and
WELLS FARGO HOME MORTGAGE, INC.,

Plaintiffs,

v.

DEMETRIOS A. BOUTRIS, in his
official capacity as Commissioner
of the California Department of
Corporations,

Defendant.

CIV. NO. S-03-0157 GEB JFM

ORDER

Plaintiffs Wells Fargo Bank, N.A. ("Wells Fargo") and Wells Fargo Home Mortgage, Inc. ("WFHMI") move for a preliminary injunction seeking to enjoin Defendant Demetrios Boutris, in his official capacity as the Commissioner of the California Department of Corporations ("the Commissioner") "from enforcing the California Residential Mortgage Lending Act, Cal. Fin. Code § 50002 et seq. (including § 50204(o)), California Civil Code § 2948.5, and the

The judge directed his staff to provide a copy of this Order to the parties and to the Office of the Comptroller of the Currency via facsimile transmission no later than 4:30 p.m. on March 10, 2003, so they could be apprized of its contents prior to official service. Nothing shall be faxed to the chambers' fax number absent the express advance approval of the judge.

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1 California Financial Lenders Law, Cal. Fin. Code § 2200C et seq.,
2 against [Wells Fargo and WFHMI]; from revoking WFHMI's licenses to do
3 business in California under those laws; and from otherwise taking any
4 action against WFHMI for continuing to do business in the state of
5 California." (Pls.' Mot. for Prelim. Inj. at 1-2.) The essence of
6 Plaintiffs' argument is that they are subject exclusively to federal
7 regulation by the Office of the Comptroller of the Currency ("OCC")
8 since federal banking law preempts the Commissioner's regulatory
9 authority over federally regulated national banks. The OCC filed an
10 amicus curiae brief in which it contends the National Bank Act
11 precludes the Commissioner from exercising visitorial powers over
12 Plaintiffs. The Commissioner opposes the motion and filed an
13 opposition to the OCC's amicus curiae brief. The Commissioner argues
14 that because WFHMI possesses California-issued licenses it is
15 obligated to comply with all licensing requirements; and that
16 "Congress has not vested in the [OCC] to the exclusion of the states,
17 the power to control or regulate operating subsidiaries of national
18 banks."¹ (Commissioner's Opp'n to OCC's Amicus Br. at 2.) The
19 Commissioner concedes "it is undisputed that the OCC has exclusive
20 regulatory authority over Wells Fargo, a national bank." (Opp'n to
21 Mot. at 2, n.1.)

22 The motion was argued March 10, 2003.²

23
24 : The Commissioner argues there is no credible evidence that
25 WFHMI is an operating subsidiary. However, an OCC letter dated
26 October 16, 2001, "confirms that [WFHMI] is an operating subsidiary of
27 Wells Fargo Bank, N.A." (Decl. of Moskowitz Ex. 1.)

28 : The OCC appeared through counsel and was allowed to argue at
the hearing. The Order filed February 19, 2003, granted the OCC's
request "to appear amicus curiae in this action so it could "present
(continued...)

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Background

1 Wells Fargo is a federal national bank organized under the
2 National Bank Act. (Pls.' Memo. of P. & A. in Support of Mot. for
3 Prelim. Inj. at 3; Decl. of Stumpf in Support of Prelim Inj. ¶ 2.)
4 WFHMI is a wholly owned operating subsidiary of Wells Fargo. (Pls.'
5 Memo. of P. & A. at 3; Decl. of Moskowitz Ex. 1.) WFHMI is licensed
6 to engage in real estate lending activities under the California
7 Residential Mortgage Lending Act ("the RMLA") and the California
8 Finance Lenders Law ("the CFLL"). (Decl. of Burns ¶¶ 5, 7, Ex. 3;
9 Decl. of Agbonkpolar ¶ 4; Decl. of Wissinger ¶¶ 5, 7.)
10 Following several regulatory examinations, the Commissioner
11 demanded on December 4, 2002, that WFHMI conduct an audit of its
12 residential mortgage loans made in California during 2001 and 2002.
13 (Decl. of Burns ¶ 15, Ex. 7.) This required audit was to identify:
14 all loans where per diem interest was charged by WFHMI in violation of
15 California Financial Code § 50204(o), those consumers entitled to a
16 refund, and instances of understating finance charges in violation of
17 the Truth in Lending Act and California Financial Code §§ 50204(i)(j)
18 and (k). (Decl. of Burns Ex. 7.) WFHMI responded to the
19 Commissioner's demand for an audit in a letter dated January 22, 2003,
20 asserting because it is an operating subsidiary of a national bank it
21 is subject to the exclusive federal regulation and supervision of the
22 OCC; however, it proposed an alternate audit to accommodate the
23 Commissioner's concerns. (Decl. of Burns Ex. 9.) The Commissioner
24

25
26 ²(...continued)
27 oral argument" and have considered the Memorandum Amicus Curiae of the
28 Office of the Comptroller of the Currency in Support of Plaintiffs'
Motion for a Preliminary Injunction filed on February 14, 2003."

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1 demanded compliance. Subsequently, Plaintiffs commenced this federal
2 lawsuit against the Commissioner on January 27, 2003. On February 4,
3 2003, the Commissioner instituted proceedings to revoke WFHMI's
4 licenses issued under the RMLA and the CFLL. (Id. ¶ 22; Decl. of
5 Wissinger Ex. 1, Ex. 2.)

6 Preliminary Injunction Standards

7 To prevail on the motion for a preliminary injunction, each
8 Plaintiff must demonstrate either: "(1) a combination of probable
9 success on the merits and the possibility of irreparable injury if
10 relief is not granted; or (2) the existence of serious questions going
11 to the merits and that the balance of hardships tips sharply in its
12 favor." Int'l Jensen, Inc. v. MetroSound U.S.A., Inc., 4 F.3d 819,
13 822 (9th Cir. 1993). "Each of these two formulations requires an
14 examination of both the potential merits of the asserted claims and
15 the harm or hardships faced by the parties." Sammartano v. First
16 Judicial Dist. Court, In and for County of Carson City, 303 F.3d 959,
17 965 (9th Cir. 2002). "The alternative standards are not separate
18 tests but the outer reaches of a single continuum," Int'l Jensen,
19 Inc., 4 F.3d at 822 (quotations and citations omitted), "in which the
20 required degree of irreparable harm increases as the probability of
21 success decreases." Sammartano, 303 F.3d at 965. When the action
22 involves the public interest, "the district court must also examine
23 whether the public interest favors the plaintiff." Id.

24 Discussion

25 Plaintiffs argue the Commissioner's attempt to enforce the
26 RMLA and the CFLL against WFHMI runs afoul of the National Bank Act.
27 Plaintiffs contend this Act grants the OCC the exclusive authority to
28 exercise visitorial powers over national banks and their operating

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1 subsidiaries; therefore, WFHMI is not required to hold a license under
2 the RMLA or the CFLL to engage in residential mortgage lending and
3 servicing business in California. (Pls.' Memo. of P. & A. at 16-17.)
4 The OCC's amicus curiae brief agrees with Plaintiffs' position,
5 stating that "in its capacity as administrator of the national banking
6 system . . . [and] pursuant to 12 U.S.C. § 484 and federal
7 regulations, the OCC has exclusive 'visitorial' power over national
8 banks and their operating subsidiaries except where federal law
9 specifically provides otherwise." (OCC Amicus Br. at 2.) The
10 Commissioner counters that the OCC seeks to exceed its visitorial
11 powers over national banks by unlawfully expanding its jurisdiction to
12 include operating subsidiaries of national banks. (Def.'s Memo. of P.
13 & A. at 13-14.)

14 National Bank Act

15 National banks are created and governed by the National Bank
16 Act. 12 U.S.C. § 21 et seq. The National Bank Act was enacted to
17 "facilitate . . . 'a national banking system,'" Marquette Nat'l Bank
18 of Minneapolis v. First of Omaha Serv. Corp., 439 U.S. 299, 314-15
19 (1978) (quoting Cong. Globe 38th Cong. 1st Sess., 1451(1864)), and "to
20

21 The OCC explains "the term 'visitorial' powers as used in
22 section 484 generally refers to the power of the OCC to 'visit' a
23 national bank to examine its activities and its observance of
24 applicable laws, and encompasses any examination of a national bank's
25 records relative to the conduct of its banking business as well as any
26 enforcement action that may be undertaken for violations of law."
27 (OCC Amicus Br. at 2-3.) 12 C.F.R. § 7.4000(a)(2) provides that
28 visitorial powers include: "examination of a bank;" "inspection of a
bank's books and records;" "regulation and supervision of activities
authorized or permitted pursuant to federal banking law; and"
"enforcing compliance with any applicable federal or state laws
concerning those activities." 12 U.S.C. § 484(a) proscribes "No
national bank shall be subject to any visitorial powers except as
authorized by Federal law, vested in the courts of justice or such as
shall be, or have been exercised or directed by Congress. . . ."

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1 protect national banks against intrusive regulation by the States."
2 Bank of America v. City and County of San Francisco, 309 F.3d 351, 361
3 (9th Cir. 2002). The National Bank Act provides that such banks
4 shall have power
5 [t]o exercise. . . all such incidental powers as
6 shall be necessary to carry on the business of
7 banking; by discounting and negotiating promissory
8 notes, drafts, bills of exchange, and other
9 evidences of debt; by receiving deposits; by
10 buying and selling exchange, coin, and bullion; by
11 loaning money on personal security; and by
12 obtaining, issuing, and circulating notes. . . .
13
14 12 U.S.C. § 24(Seventh). The United States Supreme Court stated that
15 the National Bank Act has charged the Comptroller with the supervision
16 of the Act, and that the Comptroller bears "primary responsibility for
17 surveillance of 'the business of banking' authorized by § 24
18 (Seventh)." Nationsbank of North Carolina, N.A. v. Variable Annuity
19 Life Ins. Co., 513 U.S. 251, 256 (1995); see 12 U.S.C. § 1, 26-27,
20 481. The United States Supreme Court held that the "'business of
21 banking' is not limited to the enumerated powers in § 24 Seventh and
22 that the Comptroller therefore has discretion to authorize activities
23 beyond those specifically enumerated. The exercise of the
24 Comptroller's discretion, however, must be kept within reasonable
25 bounds." NationsBank of North Carolina, N.A., 513 U.S. at 258 n.2.
26 The OCC-promulgated regulation regarding the exercise of
27 visitorial powers over national banks provides:
28 Only the OCC or an authorized representative of
the OCC may exercise visitorial powers with
respect to national banks except as provided in
paragraph (b) of this section. State officials
may not exercise visitorial powers with respect to
national banks, such as conducting examinations,
inspecting or requiring the production of books or
records of national banks, or prosecuting
enforcement actions, except in limited

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circumstances authorized by federal law. However, production of a bank's records (other than non-public OCC information under 12 CFR part 4, subpart C) may be required under normal judicial procedures.

12 C.F.R. § 7.4000.

At the March 10 hearing, the Commissioner argued that the OCC does not have exclusive visitorial powers over WFHMI because nothing in the National Bank Act authorizes the OCC to exercise this exclusive authority. Rather, the Commissioner asserted, at most the OCC has concurrent visitorial powers over WFHMI. The Commissioner further argued that should the Court find that 12 C.F.R. § 7.4006 provides the OCC with exclusive visitorial powers over WFHMI, since that regulation did not become effective until August 2001, it has no preemptive effect on the Commissioner's ability to exercise visitorial powers over WFHMI before its enactment. The OCC disagrees, arguing that the Commissioner's position violates the Congressional enactment in 12 U.S.C. § 484(a), and the intent of 12 C.F.R. § 7.4006.

Operating Subsidiaries

The OCC asserts that "[p]ursuant to their authority under 12 U.S.C. § 24 (Seventh) to exercise 'all such incidental powers as shall be necessary to carry on the business of banking,' national banks have long used separately incorporated entities to engage in activities that the bank itself is authorized to conduct. [Such authority] has been expressly recognized for nearly 40 years." (OCC Amicus Br. at 11-12.)

The Operating Subsidiary Rule, codified at 12 C.F.R. § 5.34, regulates the authority of national banks to engage in activities through operating subsidiaries. "A national bank may conduct in an operating subsidiary activities that are permissible for a national

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1 bank to engage in directly either as part of, or incidental to, the
2 business of banking, as determined by the OCC, or otherwise under
3 other statutory authority. . . .” 12 C.F.R. § 5.34(e)(1). Section
4 5.34(e)(3) provides that “[a]n operating subsidiary conducts
5 activities authorized under this section pursuant to the same
6 authorization, terms and conditions that apply to the conduct of such
7 activities by its parent national bank.” 12 C.F.R. § 7.4006 provides
8 that “[u]nless otherwise provided by Federal law or OCC regulation,
9 State laws apply to national bank operating subsidiaries to the same
10 extent that those laws apply to the parent national bank.”

11 At the March 10 hearing, the Commissioner pressed his
12 position that no provision of the National Bank Act grants national
13 banks authority to own or establish operating subsidiaries or to
14 conduct their lending activities through such subsidiaries. The OCC
15 counters that it has interpreted the language of 12 U.S.C. § 24
16 (Seventh), which authorizes national banks to exercise “all such
17 incidental powers as shall be necessary to carry on the business of
18 banking,” as authorizing national banks through the OCC to use
19 subsidiaries to conduct banking business. “Incidental powers [in § 24
20 (Seventh)] include activities that are ‘convenient or useful in
21 connection with the performance of one of the bank’s established
22 activities pursuant to its express powers under the National Bank
23 Act.’” Bank of America v. City and County of San Francisco, 309 F.3d
24 551, 562 (9th Cir. 2002) (citations omitted). The OCC’s recognition of
25 national banks’ authority to conduct authorized banking business
26 through subsidiaries dates back to 1966. At that time, the OCC issued
27 rules permitting national banks to

28

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1 acquire and hold the controlling stock interest in
2 a subsidiary operations corporation. . . . A
3 subsidiary operations corporation is a corporation
4 the functions or activities of which are limited
5 to one or several of the functions or activities
6 that a national bank is authorized to carry on.
7 * * *

8 [T]he authority of a national bank to purchase or
9 otherwise acquire and hold stock of a subsidiary
10 operations corporation may properly be found among
11 'such incidental powers' of the bank 'as shall be
12 necessary to carry on the business of banking,'
13 within the meaning of 12 U.S.C. 24 (7), or as an
14 incident to another Federal banking statute which
15 empowers a national bank to engage in a particular
16 function or activity. . . . The visitorial powers
17 vested in this Office are adequate to ascertain
18 compliance by bank subsidiaries with the
19 limitations and restrictions applicable to them
20 and their parent national banks.

21 Acquisition of Controlling Stock Interest in Subsidiary Operations

22 Corporation, 31 Fed. Reg. 11,459 at 11,459-60 (Aug. 31, 1966).

23 Plaintiffs and the OCC also argue that the Gramm-Leach-
24 Bliley Act ("GLBA") acknowledges national banks' authority to conduct
25 banking business through operating subsidiaries. See 12 U.S.C. § 24a.
26 The GLBA defines a financial subsidiary as something "other than a
27 subsidiary that . . . engages solely in activities that national banks
28 are permitted to engage in directly and are conducted subject to the
same terms and conditions that govern the conduct of such activities
by national banks. . . ." Id. § 24a(g)(3). The Commissioner disputes
the OCC's position on the GLBA, relying on a Report of the Senate
Committee on Banking, Housing, and Urban Affairs, which he argues
reveals Congress did not recognize operating subsidiaries in the GLBA.
(Commissioner's Opp'n to Amicus Br. at 5.) However, that Report
specifically addresses national banks' authority to conduct authorized
banking business through operating subsidiaries:

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1 For at least 30 years, national banks have been
2 authorized to invest in operating subsidiaries
3 that are engaged only in activities that national
4 banks may engage in directly. For example,
5 national banks are authorized directly to make
6 mortgage loans and engage in related mortgage
7 banking activities. Many banks choose to conduct
8 these activities through subsidiary corporations.
9 Nothing in this legislation is intended to affect
10 the authority of national banks to engage in bank
11 permissible activities through subsidiary
12 corporations, or to invest in joint ventures to
13 engage in bank permissible activities with other
14 banks or nonbank companies.

15 S. Rep. No. 106-44, at 6 (1999).

16 Finally, operating subsidiaries and national banks have been
17 treated as equivalents in court decisions determining whether a
18 particular activity was permissible for a national bank. See
19 NationsBank of North Carolina, N.A., 513 U.S. at 254 (brokerage
20 subsidiary acting as an agent in the sale of annuities); Marquette
21 Nat'l Bank of Minneapolis v. First of Omaha Service Corp., 439 U.S.
22 299 (1978) (credit card subsidiary); American Ins. Ass'n v. Clarke,
23 865 F.2d 278 (D.C. Cir. 1988) (subsidiary offering municipal bond
24 insurance); M & M Leasing Corp. v. Seattle First Nat'l Bank, 563 F.2d
25 1377 (9th Cir. 1977) (motor vehicle leasing by subsidiary).
26 Therefore, the OCC's interpretation that national banks are authorized
27 to conduct permissible banking business activities through operating
28 subsidiaries appears to be reasonable and entitled to deference.

As stated in First Nat'l Bank of Eastern Arkansas v. Taylor,
907 F.2d 775, 777-78 (8th Cir. 1990),

the Supreme Court has made clear that the
Comptroller's interpretation of the National Bank
Act must be given "great weight":
"It is settled that courts should give great
weight to any reasonable construction of a
regulatory statute adopted by the agency charged
with the enforcement of that statute. The

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1 Comptroller of the Currency is charged with the
2 enforcement of banking laws to an extent that
3 warrants the invocation of this principle with
4 respect to his deliberative conclusions as to the
5 meaning of these laws." The Comptroller's
6 determination as to what activities are authorized
7 under the National Bank Act should be sustained if
8 reasonable.

9 (Citations omitted); see also NationsBank of North Carolina, N.A., 513
10 U.S. at 256-57 (same).

11 OCC's Exclusive Visitorial Powers over Operating
12 Subsidiaries

13 Notwithstanding the likelihood that Plaintiffs will prevail
14 on their claim that WFHMI has the status of an operating subsidiary of
15 a national bank, the Commissioner contends he has joint visitorial
16 powers over WFHMI at least prior to August 2001. The OCC counters,
17 "Because federal law prohibits the [Commissioner] from exercising
18 visitorial powers over a national bank engaged in real estate lending
19 pursuant to federal law, the [Commissioner] may not exercise
20 visitorial power over the national bank conducting that activity
21 through an operating subsidiary licensed by the OCC, absent federal
22 law dictating a contrary result." (OCC Amicus Br. at 14.) The OCC
23 explained in its interpretive letter to the Commissioner, dated
24 February 11, 2003, the following:

25 As an operating subsidiary of a national bank,
26 WFHMI is subject to ongoing supervision and
27 examination by the OCC in the same manner and to
28 the same extent as the [Wells Fargo] Bank. . . .
[P]ursuant to 12 U.S.C. § 484, and 12 C.F.R. §
5.34(e)(3) and 7.4006, the OCC has exclusive
visitorial authority over national banks and their
operating subsidiaries except where Federal law
provides otherwise. This authority pertains to
activities expressly authorized or recognized as
permissible for national banks under Federal law
or regulation, or by OCC issuance or
interpretation, including the content of those

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activities and the manner in which, and standards whereby, those activities are conducted. As a result, States are precluded from examining or requiring information from national banks or their operating subsidiaries or otherwise seeking to exercise visitorial powers with respect to national banks or their operating subsidiaries in those respects. Thus, Federal law precludes examination of WFRMI by the [Commissioner].

(Id. Ex. 1 at 1-2.) Because the OCC's construction of the National Bank Act is articulated in an amicus brief and an interpretive letter "does not make it 'unworthy of deference.'" Bank of America, 309 F.3d at 563 n.7. The OCC's amicus brief and interpretive letter appear to be "both persuasive and consistent with the National Bank Act and OCC regulations and thus at least 'entitled to respect.'" Id.

During the March 10 hearing, OCC pointed to the Third Circuit decision in Nat'l State Bank, Elizabeth, N.J., v. Long, 630 F.2d 981 (3d Cir. 1980), as support for its position that the OCC has exclusive visitorial powers over WFRMI whether or not the enforcement of California law is involved. Long reveals, "Questions about the applicability of state legislation to national banks must be distinguished from the related inquiry of who is responsible for enforcing national bank compliance." Long, 630 F.2d at 987-88. In light of the respect that is to be given to the OCC's construction of the National Bank Act articulated in its brief and its interpretive letter where it opines it has exclusive visitorial power over WFRMI as a subsidiary of a national bank, Plaintiffs are likely to prevail on the merits of their claim that the OCC's recognition of WFRMI's status as an operating subsidiary is all that is needed for it to conduct its residential mortgage lending in California. Accordingly, the Commissioner's argument that he has dual visitorial powers with the OCC is not likely to prevail because allowing the Commissioner to

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1 exercise visitorial powers over WFHMI would appear to "result in
2 unnecessary and wasteful duplication of effort on the part of the bank
3 and the state agency. From that standpoint enforcement exclusivity in
4 the [OCC] is reasonable and practical." Id. at 988.

5 The foregoing discussion reveals that Plaintiffs have shown
6 probable success on the merits of their claim that WFHMI is a wholly-
7 owned operating subsidiary of Wells Fargo licensed by the OCC to
8 engage in real estate lending activities in California, and that
9 therefore "the National Bank Act preempts the Commissioner's
10 authority" to prohibit WFHMI from doing this business in California
11 and from exercising visitorial power over Plaintiffs. First Nat'l
12 Bank of Eastern Arkansas, 907 F.2d at 778.

13 Hardships Faced by the Parties

14 Plaintiffs contend they will suffer irreparable harm if the
15 Commissioner is allowed to exercise visitorial powers over them.
16 According to Plaintiffs,

17 The California residential mortgage market
18 accounts for a significant share of WFHMI's annual
19 loan production volume, and generates hundreds of
20 millions of dollars each year in gross revenue for
21 WFHMI. . . . Plaintiffs know of no way that they
22 can recover these revenues if they ultimately
succeed on the merits of this action but are
impeded in their business activities by the
Commissioner's actions to stop WFHMI from
continuing its business operations in California
for some period of time before they obtain a
favorable final decision from this Court.

23 (Pls.' Memo. of P. & A. at 21.) Plaintiffs argue that Wells Fargo
24 will also be irreparably harmed because the Commissioner's actions
25 "threaten to disrupt substantially the majority of the Bank's
26 residential mortgage lending and servicing business in California,
27 which the Bank undertakes through WFHMI." (Id.) In addition,
28

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1 Plaintiffs estimate that the manual audit demanded by Defendant of
2 more than 300,000 mortgage loan files will cost WFHMI "at least \$60
3 per loan file (including file retrieval and manual file review by
4 specially trained outside personnel), for a total audit cost of at
5 least \$18 million." (Pls.' Memo. of P. & A. at 21-22.) Plaintiffs
6 contend such costs cannot be recovered. (*Id.* at 22.)

7 Public Interest

8 The public interest also favors Plaintiffs' position because
9 they have a probability of succeeding on their position that since
10 Wells Fargo is a national bank and WFHMI is an operating subsidiary of
11 a national bank they are subject to the exclusive visitorial power of
12 the OCC. "Because national banks are considered federal
13 instrumentalities, states may neither prohibit nor unduly restrict
14 their activities." First Nat'l Bank of Eastern Arkansas, 907 F.2d at
15 778. Further, Plaintiffs have shown the possibility of irreparable
16 injury if relief is not granted. Moreover, a serious federal and
17 state regulatory dispute is involved and the balance of hardships tips
18 sharply in Plaintiffs' favor on the issue that the National Bank Act
19 prohibits the Commissioner from exercising visitorial powers over
20 Plaintiffs. Therefore, the Commissioner is preliminarily enjoined
21 from exercising visitorial powers over Plaintiffs.

22 Revocation of California Issued Licenses

23 WFHMI has not shown, however, a probability of success on
24 the merits of its claim that the Commissioner should be enjoined from
25 revoking the California licenses issued under the RMLA and the CFLL.
26 As stated in the ruling on Plaintiffs' motion for a temporary
27 restraining order, filed on March 6, 2003:
28

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1 Plaintiffs have not shown that California's
2 licensing revocation proceeding must be stayed
3 while Plaintiffs litigate their claims in federal
4 court that WFHMI does not have to possess
5 California licenses to do the national banking
6 business it does in California. . . .

7
8 It would be ironic for an injunction to issue in
9 such circumstances since WFHMI could have avoided
10 the harm it contends it will suffer had it chosen
11 to comply with the requirements of the California
12 licenses it possesses. . . .

13 Although it is unclear why WFHMI subjected itself to the
14 Commissioner's regulatory authority by virtue of having become a
15 California licensee, this does not seem to have an effect on WFHMI's
16 right to conduct federally permissible banking activities authorized
17 by the OCC. See ANR Pipeline Co. v. Iowa State Commerce Com'n, 828
18 F.2d 465, 467-68 (8th Cir. 1987) (revealing that even though the
19 Pipeline Company unnecessarily obtained a state permit, it could
20 continue doing work on an interstate gas pipeline under federal
21 authority notwithstanding the Company's violation of the state
22 permit's requirement).

23 Conclusion

24 Therefore, the Commissioner is preliminarily enjoined from
25 exercising visitatorial powers over Plaintiffs or from otherwise
26 preventing WFHMI from operating in California; however, the portion of

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FHA NO. 910 550 4224

P. 1.

1 Plaintiffs' motion seeking to preliminarily enjoin the Commissioner
2 from revoking WFHMI's California issued licenses is denied.

3 IT IS SO ORDERED.

4 DATED: March 10, 2003


5 GARLAND E. BURRELL, JR.
6 UNITED STATES DISTRICT JUDGE
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APPENDIX B

APPENDIX B

LEXSEE 1996 occ ltr lexis 116

Comptroller of the Currency
Washington, DC 20219

Release Date: October 1996

Interpretive Letter #749

1996 OCC Ltr. LEXIS 116

September 13, 1996

[*1]

This responds to your letter of July 10, 1996, requesting an opinion from the Office of the Comptroller of the Currency ("OCC") confirming that 12 U.S.C. § 24(Seventh) preempts Texas insurance licensing laws that prevent or significantly interfere with a national bank's authority to act as agent in the sale of annuities.

We believe that section 24(Seventh) does preempt Texas insurance licensing laws with respect to annuities sales by national banks to the extent that those laws prevent or impair the ability of national banks to exercise their authority under section 24(Seventh) to sell annuities. We do not believe that the McCarran-Ferguson Act, 15 U.S.C. § 1012, insulates Texas law in this case for two reasons: First, annuities are not "insurance" within the meaning of the Act. Second, even if annuities were insurance for that purpose, laws that have the effect of negating or impairing the corporate powers of an entire class of entity -- in this case the authority of national banks to sell annuities -- are not laws "regulating the business of insurance" within the meaning of the McCarran-Ferguson Act. However, as we discuss below, this does not mean that all Texas law in this [*2] area is inapplicable to national banks. n1

n1 Please note that we recently expressed similar conclusions in a letter dated August 9, 1996, to Commissioner Bomer of the Texas Insurance Department in connection with his request for an opinion on this issue submitted to the Office of the Texas Attorney General.

Background

National banks derive their authority to sell annuities from section 24(Seventh) of the National Bank Act, which provides that national banks shall have the power to exercise "all such incidental powers as shall be necessary to carry on the business of banking." The Supreme Court, in *NationsBank of North Carolina, N.A. v. Variable Annuity Life Insurance Company*, U.S. 130 L.Ed.2d 740, (1995) ("VALIC"), upheld the Comptroller's conclusion that this power includes the power to sell fixed and variable annuities as agent.

Sections 3.01, 3.75, and 21.07-1 of the Texas Insurance Code effectively prohibit national banks from selling annuities as agent in Texas. These provisions of Texas law require sellers of annuities to have a license, and a license is only available to a corporation if (1) the corporation is organized under [*3] the Texas Business Corporation Act, the Texas Professional Corporation Act, or the Texas Limited Liability Company Act, and (2) each officer, director, and shareholder of the corporation is individually licensed as an agent.

A national bank would be unable to satisfy these criteria because it is federally chartered. A subsidiary of a national bank would be unable to satisfy these criteria because its parent bank, as a shareholder, could not get a license. Thus, Texas law would prohibit a national bank even from purchasing an existing, licensed Texas annuity agency.

We also understand that the Texas Commissioner of Insurance may have considered an alternative limitation that would allow only national banks located in places with 5,000 or fewer inhabitants to sell annuities. Since the authority to sell annuities derives from section 24(Seventh), not section 92, this limitation is not imposed by federal law. n2 The proposed restriction would be an absolute prohibition for national banks not located in places of 5,000 or fewer inhabitants.

n2 The power to sell annuities is not subject to any geographic limitation based on the location of the customer. Therefore, a national bank may sell annuities to customers located anywhere. [*4]

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Ordinarily, when Federal law and state law so clearly conflict, the state law will be preempted by the Federal provision. Your question presents the issue, however, of whether the McCarran-Ferguson Act, 15 U.S.C. § 1012, may insulate the provisions of the Texas Insurance Code at issue, and/or the above-described limitation, from preemption by section 24(Seventh). For the reasons discussed below, it is our opinion that section 24(Seventh) does preempt these state law provisions.

Discussion

A. The McCarran-Ferguson Act

Section 2(b) of the McCarran-Ferguson Act, 15 U.S.C. § 1012(b), protects certain insurance-related state laws from federal preemption. Section 2(b) provides that a federal law shall not be construed to "invalidate, impair, or supersede" a state law "enacted for the purpose of regulating the business of insurance," unless the federal law "specifically relates to the business of insurance."

In this case, the federal law at issue is 12 U.S.C. § 24(Seventh). As was noted above, the OCC has interpreted section 24(Seventh) to permit national banks to sell annuities as agent, and the Supreme Court has affirmed that interpretation. To the extent that [*5] the Texas Insurance Code would prohibit a national bank from exercising that power, section 24(Seventh) would "invalidate, impair, or supersede" it. Thus, the McCarran-Ferguson Act will insulate the Texas provisions from the ordinarily applicable Federal preemption standards, if the restrictions in Texas law regulate the business of insurance. We believe that the Texas licensing restrictions do not meet this test, for two reasons: First, because annuities are not "insurance" for McCarran-Ferguson Act purposes, and, second, because requirements that have the effect of negating the existing corporate authority of national banks to sell annuities, are regulating, if anything, the powers of a particular class of entity, not the "business of insurance."

B. Annuities as "Insurance" under the McCarran-Ferguson Act

The Supreme Court has already explicitly held in *SEC v. Variable Annuity Life Ins. Co. of America*, 359 U.S. 65, (1959) ("SEC") that variable annuities are not insurance for purposes of the McCarran-Ferguson Act. Although the Supreme Court has not specifically addressed whether fixed annuities are insurance for purposes of the McCarran-Ferguson Act, [*6] Supreme Court decisions in other contexts, and numerous other authorities, lead to a similar negative conclusion.

1. Annuities and Insurance are Distinct Products

The scope of the term "insurance" in the McCarran-Ferguson Act is a federal question, not controlled by Texas or other state law definitions. SEC at 69. Neither the statute or the legislative history of the McCarran-Ferguson Act define the term, however. n3 Nevertheless, "insurance" has a commonly-understood meaning, and, absent a contextual basis for concluding otherwise, words in statutes are presumed to have their usual meaning. This is especially true where, as here, a statute does not define a term. See 2A Sutherland, *Statutory Construction* § 47.23 (4th ed. 1984). n4

n3 See H.R. Rep. No. 143, 79th Cong., 1st Sess (1945), reprinted in 1945 U.S.C.C.A.N. 670.

n4 See *Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205, 211-213 (1979) ("Since the [McCarran-Ferguson Act] does not define the 'business of insurance,' the question for decision is whether the [contracts at issue] fall within the ordinary understanding of the phrase, illumined by any light to be found in the structure of the Act and its legislative history."). [*7]

Dictionary definitions of "insurance," for example, describe it as a contract for indemnification against risk of loss. In 1945, when the McCarran-Ferguson Act was enacted, the third edition of Black's Law Dictionary (1933) was in use and defined insurance as: "A contract whereby, for a stipulated consideration, one party undertakes to compensate the other for loss on a specified subject by specified perils." By contrast, the definition of "annuity" from the same edition describes annuities variously as: "a yearly sum stipulated to be paid to another in fee, or for life, or years, and chargeable only on the person of the grantor;" "a fixed sum, granted or bequeathed, payable periodically but not necessarily annually;" or a contract "by which one party delivers to another a sum of money, and agrees not to reclaim it so long as the receiver pays the rent agreed upon." Thus, when Congress enacted the McCarran-Ferguson Act, an "annuity" was clearly distinct from "insurance."

That distinction continues today. For example, Black's Law Dictionary (1990) defines "insurance" as follows:

A contract whereby, for a stipulated consideration, one party undertakes to compensate the other [*8] for loss on a specified subject by specified perils....A contract whereby one undertakes to indemnify another against

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loss, damage, or liability arising from an unknown or contingent event and is applicable only to some contingency or act to occur in future. An agreement by which one party for a consideration promises to pay money or its equivalent or to do an act valuable to other party [sic] upon destruction, loss, or injury of something in which another party has an interest.

See also Webster's Third International Dictionary (1971) ("coverage by contract whereby for a stipulated consideration one party undertakes to indemnify or guarantee another against loss by a specified contingency or peril"); Random House Dictionary (1973) ("coverage by contract in which one party agrees to indemnify or reimburse another for any loss that occurs under the terms of the contract"); Oxford English Dictionary (Compact ed. 1971) ("a contract by which the one party (usually a company or corporation) undertakes, in consideration of a payment (called a premium) proportioned to the nature of the risk contemplated, to secure the other against pecuniary loss, by payment of a sum [*9] of money in the event of destruction of or damage to property (as by disaster at sea, fire, or other accident), or the death or disablement of a person"); *Helvering v. Le Gierse*, 312 U.S. 531, 542 (1941) ("Historically and commonly, insurance involves risk-shifting and risk-distributing."). Legal encyclopedias have defined insurance similarly. C.J.S. states, "Insurance has been said to be best defined as a contract whereby one undertakes to indemnify another against loss, damage, or liability arising from an unknown or contingent event." 44 C.J.S. § 2(a). Am. Jur. defines insurance as a contract that provides for the payment of "a certain or ascertainable sum of money on a specified contingency." 43 Am. Jur. 2d Insurance § 1. See also 1 Couch on Insurance 3d (1995) § 1:6 ("Essentially, insurance is a contract by which one party (the insurer), for a consideration that usually is paid in money, either in a lump sum or at different times during the continuation of the risk, promises to make a certain payment, usually of money, upon the destruction or injury of 'something' in which the other party (the insured) has an interest.").

Annuities do not involve indemnification against [*10] risk of loss. Investors who purchase annuities are not seeking to pool a catastrophic risk such as death, injury or property damage, but are instead seeking a guaranteed, long-term return on their assets. Most commonly, annuities are marketed as a tax-sheltered means of saving for retirement. n5 The element of mortality risk, which is present in some annuities, derives from the investor's willingness to price a contractual arrangement based on the length of his life in

order to increase the return he will receive during his lifetime. This risk is essentially an investment risk, not an insurance risk. In upholding the Comptroller's determination that annuities are not insurance for purposes of another federal law -- 12 U.S.C. § 92 -- the Supreme Court stated,

By making an initial payment in exchange for a future income stream, the customer is deferring consumption, setting aside money for retirement, future expenses, or a rainy day. For her, an annuity is like putting money in a bank account, a debt instrument, or a mutual fund. Offering bank accounts and acting as agent in the sale of debt instruments are familiar parts of the business of banking.... In sum, modern annuities, [*11] though more sophisticated than the standard savings bank deposits of old, answer essentially the same need. By providing customers with the opportunity to invest in one or more annuity options, banks are essentially offering financial investment instruments of the kind congressional authorization permits them to broker.

VALIC at 814. n6

n5 See *Helping Consumers Shelter Income*, ABA Banking Journal, July 1989, at 16-21 (discussing investment and tax shelter characteristics of annuities).

n6 See also *Helvering v. Le Gierse*, *supra* ("Any risk that the prepayment [premium] would earn less than the amount paid to respondent as an annuity was an investment risk similar to the risk assumed by a bank; it was not an insurance risk"); *In Re Howerton*, 21 Bankr. 621, 623 (1982) ("Both life insurance and annuity contracts may take various forms but the heart of the distinction between them is this: life insurance is a promise to pay a sum certain on the death of the insured and an annuity is essentially a form of investment which pays periodically during the life of the annuitant or during a term fixed by contract rather than on the occurrence of a future contingency."); *Daniel v. Life Ins. Co. of Virginia*, 102 S.W.2d 256, 260 (Tex. Civ. App. 1937) ("[An annuity] is essentially a form of investment, and uniformly held to be such, regardless of the fact that in its usual form payments are contingent upon continuity of the life of the grantee."); 1 J. Appleman, *Insurance Law and Practice*, § 84 (1981) ("annuity contracts must... be recognized as investments rather than as insurance"). See also *SEC v. United Benefit Life Ins. Co.*, 387 U.S. 202, 207-208 (1967) ("In fixing the necessary premium [for a fixed annuity] mortality experience is a subordinate factor and the planning problem is to decide what interest and expense rates may

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be expected. There is some shifting of risk from policyholder to insurer, but no pooling of risks among policyholders. In other words, the insurer is acting in a role similar to that of a savings institution...."). [*12]

Most authorities hold that annuities are not insurance, because they do not incorporate the element of indemnification against risk. Courts considering the status of annuities as "insurance" have held that annuities are not insurance for purposes of federal tax law, n7 several state tax laws, n8 bankruptcy law, n9 and other laws. n10 Legal encyclopedias also agree that, because annuities do not involve this type of indemnification against risk of loss, they are not insurance. See 44 C.J.S. § 2(b) ("Generally an annuity contract is not a contract of insurance"); 43 Am. Jur. 2d Insurance § 5 ("Contracts for annuities differ materially from ordinary life insurance policies, and are not generally regarded as such. Consequently, a company engaged merely in selling annuities does not conduct an insurance business, and is not an insurance company unless made so by a broad statutory definition of insurance companies.").

n7 See *Helvering v. Le Gierse*, supra; *Keller v. Commissioner of Internal Revenue*, 312 U.S. 543 (1941) (Under federal tax law which excludes "amounts receivable as insurance" from decedent's gross estate for tax purposes, annuities are not treated as insurance.). [*13]

n8 See *Kernochan v. U.S.*, 29 F.Supp. 860 (Cl. Ct. 1939); *In re Sothorn's Estate*, 257 A.D. 574, 14 N.Y.S.2d 1 (1939); *In re Rhodes' Estate*, 197 Misc. 232, 94 N.Y.S.2d 406 (N.Y. Surr. Ct. 1949) (Annuity contracts are not within New York tax law exemption, applicable to insurance payable to a designated beneficiary, from estate taxes.); *People v. Knapp*, 193 A.D. 413, 184 N.Y.S. 345 (1920); *Commonwealth v. Metropolitan Life Ins. Co.*, 254 Pa. 510, 98 A. 1072 (1916); *Daniel v. Life Ins. Co. of Virginia*, supra; *State v. Ham*, 54 Wyo. 148, 88 P.2d 484 (1939) (Consideration paid for annuity contracts is not subject to tax law which taxes all "premiums" paid for insurance, because annuities are not insurance.)

n9 See *New York State Association of Life Underwriters, Inc. v. New York State Banking Department*, 83 N.Y.2d 353, 632 N.E.2d 876 (1994) (Because "the great weight of authority supports the position that annuities are not insurance," New York state-chartered banks may sell annuities as agent); *In re Walsh*, 19 F.Supp. 567 (D. Minn. 1937) (Annuity policy

owned by bankrupt was not within insurance exemption to Minnesota bankruptcy law and therefore trustee in bankruptcy was entitled to the cash surrender value of the policies.); *In Re Howerton*, 21 Bankr. 621, 623 (1982). [*14]

n10 See *Carroll v. Equitable Life Assurance Co.*, 9 F.Supp. 223 (W.D. Mo. 1934) (Defendant, a mutual insurance company forbidden by law to issue insurance contracts except by a "mutual plan," was nonetheless authorized to sell annuity contracts without a mutual plan because annuity contracts are investments rather than insurance.); *Succession of Rabouin*, 201 La. 227, 9 So.2d 529 (1942) (Insurance is not considered part of the decedent's estate for purposes of the law of "forced heirship," but annuities are part of the estate because they are not insurance.).

The two leading treatises on insurance law, Couch and Appleman, also distinguish annuities from insurance. See 1 J. Appleman, *Insurance Law and Practice*, § 84 (1981) ("annuity contracts must... be recognized as investments rather than as insurance"); 1 Couch on Insurance 3d (1995) § 1:22 ("In consequence of the fact that annuities are not ordinarily regarded as insurance, it naturally follows that most litigation involving annuities does not present any aspect of what would ordinarily be regarded as insurance law. The subject of annuities is thus not treated in detail in this text."). The Couch treatise even [*15] has a separate section entitled "Annuity as distinguished from insurance," which states,

An annuity contract differs materially from an ordinary life insurance contract in that it is payable during the life of the annuitant rather than upon any future contingency, and in many instances it is paid for in a single payment which is not generally regarded as a premium. Consequently, a company engaged in selling annuities is not subject to a statute applicable to "insurers" unless the statute expressly so declares.

19 Couch on Insurance 2d (Rev. ed. 1983) § 81:2.

The recent Court of Appeals decision which found that annuities would be insurance for purposes of the McCarran-Ferguson Act, *American Deposit Corp. and Blackfeet National Bank v. Schacht*, 84 F.3d 834 (7th Cir. 1996) ("*Blackfeet*"), fundamentally mistook these essential distinctions between annuities and insurance. In that case, an Illinois statute effectively prohibited a national bank from issuing an annuity-like deposit instrument. A national bank challenged this prohibition on the grounds that the bank had authority under the

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National Bank Act, as interpreted by the OCC, to issue an annuity-like product [*16] called a "Retirement CD." In its decision, the court noted several reasons why annuities should be considered insurance. n11 All, however, have fundamental flaws.

n11 In a lengthy and comprehensive dissent, however, Judge Flaum concluded, "Annuities are not 'insurance', and thus a national bank selling them is not engaged in 'the business of insurance.' The modern literature on insurance powerfully affirms this conclusion, and the history of insurance caselaw is in accord." 84 F.3d 834, Slip. Op. at 63, 64 (7th Cir. 1996) (emphasis in original).

First, the court noted that annuities involve mortality risk. However, the Supreme Court in *VALIC* rejected the notion that mortality risk is a determinative indicator that a product is insurance. For example, as the Court pointed out, a life interest in property involves mortality risk, and such an interest is certainly not insurance. *VALIC*, 130 L.Ed.2d at 751.

Second, the *Blackfeet* court reasoned that annuities should be considered insurance because they protect the insured against the risk of running out of money:

The purpose of purchasing a life insurance policy on a family's breadwinner and of purchasing [*17] a lifetime annuity is essentially the same. The individual who purchases the life insurance policy insures against no longer having the money produced by the breadwinner, and the person who purchases a lifetime annuity insures against no longer having sufficient money produced by his assets.

Slip. Op. at 13. This argument, too, fails to hold up, since it would characterize any long-term income stream -- a bank account, a long-term lease, or a long-term bond -- as insurance because the holder is protected against not receiving income. n12 It is possible to describe virtually any asset as protecting against some type of "risk." Insurance is not merely protection against risk -- it is indemnification against risk of loss. See 1 Couch on Insurance 3d (1995) § 1:9 ("The primary requisite essential to a contract of insurance is the assumption of a risk of loss and the undertaking to indemnify the insured against such loss."). See generally 1 Couch on Insurance 3d (1995) § § 1:12-23 (distinguishing various forms of risk transfer such as suretyship, guarantees, warranties, and annuities from insurance).

n12 Some annuities have a life term rather than a fixed term, but, as was noted above, this feature does not transform them into insurance. An interest in real property does not become "insurance" if it is divided into a life estate and a remainder interest. [*18]

Third, the *Blackfeet* court contended that a fixed annuity is insurance because it

insures the purchaser against a decline in the market--a single, contingent event. The purchaser is given the comfort that should a depression occur in the market, causing rates of interest to fall significantly, he will not suffer a "loss" of future income, but will continue to receive the rate of interest guaranteed in his Retirement CD contract.

Id. Again, the court confused indemnification against risk of loss with protection against other types of risk, in this case, investment risk. The shifting of investment risk does not make a product insurance. Treasury bonds, bank accounts, and other guaranteed obligations have no investment risk, but they are in no way considered insurance.

Thus, the *Blackfeet* court's decision was analytically flawed to a profound degree. We therefore believe that, on balance, the court's reasoning is clearly outweighed by the precedents and analysis that reach the opposite conclusion.

2. A Product Does Not Become "Insurance" Because It Is Sold by Insurance Companies

Annuities are not part of the "business of insurance" simply because [*19] they have historically been offered primarily by insurance companies. The Supreme Court specifically rejected this approach to interpretation of the McCarran-Ferguson Act, stating,

The statute did not purport to make the States supreme in regulating all the activities of insurance companies; its language refers not to the persons or companies who are subject to state regulation, but to laws 'regulating the business of insurance.' Insurance companies may do many things which are subject to paramount federal regulation; only when they are engaged in the 'business of insurance' does the statute apply.

SEC v. National Securities, Inc., 393 U.S. 453, 459-60 (1969) ("*National Securities*") (emphasis in original).

Similarly, as the Supreme Court pointed out in *VALIC*,

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The sale of a product by an insurance company does not inevitably render the product insurance. For example, insurance companies have long offered loans on the security of life insurance...but a loan does not thereby become insurance.

130 L.Ed.2d at 750. Insurance codes and the authority of insurance regulators will naturally address the activities that insurance companies have traditionally [*20] engaged in. *National Securities* makes it clear that the business of insurance companies — what insurance companies typically do, and what insurance regulators typically regulate — is not the same as the business of insurance under the McCarran-Ferguson Act.

Even where state insurance codes cover annuities, moreover, they generally distinguish annuities from insurance. For example, the Texas Insurance Code section at issue here, Art. 21.07-1, defines a "life insurance agent" as one who sells "insurance or annuity" contracts. The definition of "life insurance company" in Art. 3.01, Sec. 1 of the Texas Insurance Code also distinguishes between insurance and annuities.

Thus, with a few isolated exceptions, courts and other legal authorities have understood the term "insurance" to refer to a contractual obligation to indemnify the insured against a risk of loss, and have accordingly classified annuities as products that are not insurance. The Supreme Court has already addressed variable annuities and found variable annuities *not* to be insurance for purposes of the McCarran-Ferguson Act. In the absence of language in the McCarran-Ferguson Act suggesting that the context [*21] somehow requires an unusual interpretation of the term "insurance," therefore, the commonly-understood meaning must prevail, and fixed as well as variable annuities should not be considered to be insurance for purposes of the McCarran-Ferguson Act.

As discussed in more detail in section D below, this result does not mean that all Texas state laws are inapplicable to annuity sales by national banks. What it does mean, however, is that state laws that purport to apply to national banks' sales of annuities must be evaluated under longstanding, judicially developed standards of federal preemption. This is a particularly appropriate result here, since the Supreme Court has directly ruled that annuity sales are authorized for national banks under their corporate banking powers pursuant to 12 U.S.C. § 24 (Seventh). See *YALIC*, *supra*.

C. "Regulating the Business of Insurance" under the McCarran-Ferguson Act

It is axiomatic that the McCarran-Ferguson Act shields from Federal preemption state laws enacted for the purpose of regulating the business of insurance in order to provide special status for laws that *do that*. When a state law does *something else*, as is the case [*22] here, where the effect of the law, if it regulates anything, is to regulate the powers of national banks as a class of entity, the state law is not within the scope of protection designed by the McCarran-Ferguson Act. State regulation that negates or impairs the existing corporate activity of an entire class of entity is regulation of that type of entity, not regulation of the activity that constitutes the "business of insurance." See *Hartford Fire Ins. Co. v. California*, 509 U.S. 764, 125 L.Ed.2d 612, 629 (1993) ("The business of insurance' should be read to single out one activity from others, not to distinguish one entity from another.").

In fact, caselaw emphasizes that the McCarran-Ferguson Act should be construed narrowly, so as to avoid displacing other federal statutes and their underlying regulatory interests. See *Women in City Government United v. City of New York*, 515 F. Supp. 295, 303 (S.D.N.Y. 1981); *FTC v. Manufacturers Hanover Consumer Servs.*, 567 F. Supp. 992, 995 (E.D. Pa. 1983). This approach is particularly appropriate in this case, where the Supreme Court has specifically determined that the authority of national banks to conduct the "business [*23] of banking" includes the authority to sell both fixed and variable annuities.

The Supreme Court has stated that state laws enacted "for the purpose of regulating the business of insurance" under the McCarran-Ferguson Act are those laws "that possess the 'end, intention, or aim' of adjusting, managing, or controlling the business of insurance." *U.S. Dep't. of Treasury v. Fabe*, 508 U.S. 491, 113 S. Ct. 2202, 2210 (1993) ("*Fabe*"). As the Court emphasized in *Fabe*, "the focus of McCarran-Ferguson is upon the relationship between the insurance company and its policyholders." *Fabe*, 113 S. Ct. at 2212. In *Fabe*, the Supreme Court was concerned with whether an Ohio statute governing the priority of claims filed in a proceeding to liquidate an insolvent insurer was preempted by a federal priority statute, or was protected by the McCarran-Ferguson Act. In deciding to apply McCarran-Ferguson protections to the Ohio statute, the court considered the relationship between the insured and the insurer, and concluded that to the extent that the Ohio priority statute regulated the resolution of policyholders' claims against an insurer, it was a law enacted for the

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purpose of regulating [*24] the business of insurance.
Id.

Fabe was not the first time that the Supreme Court has considered the relationship between the insured and the insurer in applying the McCarran-Ferguson Act. In *National Securities, supra*, the Court examined a state statute requiring an insurance commissioner to certify that insurance company mergers were equitable to stockholders in order to determine whether it was protected by the McCarran-Ferguson Act. Because the Court found that the effect of the statute was to protect the stockholders, not the policy holders, it concluded that the statute was not enacted for the purpose of regulating insurance. *National Securities, supra*, 393 U.S. at 459. In deciding the case, the *National Securities* Court, like the *Fabe* Court, focused upon the relationship between the insured and the insurer, observing that the core of the "business of insurance" is

the relationship between insurer and insured, the type of policy which could be issued, its reliability, interpretation, and enforcement.

Id. In dicta, the Court gave as examples of activities that could constitute the business of insurance: fixing of rates, selling and [*25] advertising of policies, and licensing of companies and agents. 393 U.S. at 460.

Thus, under the standards set by the Supreme Court in *Fabe* and *National Securities*, licensing of agents could constitute regulation of the business of insurance if the licensing standards have the end result, intention or aim of adjusting, managing or controlling the relationship between insurer and insured, the types of policies issued, or their reliability, interpretation, and enforcement. The Texas state law provisions at issue here simply do none of that. They regulate neither the "transferring or spreading [of] a policyholder's risk," nor any other practice that is "an integral part of the policy relationship between the insurer and the insured." *Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119, 129 (1982) ("*Pireno*"); see also *Fabe*, 113 S.Ct. at 2209, 2213-216. Rather, they deprive an entire category of entity -- national banks -- of the capacity to exercise a corporate power they possess under Federal law.

Courts of appeals that have examined state insurance laws that attempt to restrict the authorized activities of national banks have generally concluded that state [*26] law restrictions on the powers of national banks to conduct those activities do not fall within the preemption shield of the McCarran-Ferguson Act. n13 See e.g.; *Owensboro Nat'l Bank v. Stephens*, 44 F.3d 388 (6th Cir.

1994), cert. denied, 134 L.Ed.2d 519 (U.S. 1996) ("*Owensboro*"); *First Nat'l Bank of E. Ark v. Taylor*, 907 F.2d 775, 780 (8th Cir.), cert. denied, 498 U.S. 972 (1990) (McCarran-Ferguson Act does not immunize state insurance law restrictions from preemption because sale of debt cancellation contracts by national banks is an authorized activity of national banks and does not constitute the "business of insurance" within the meaning of the McCarran-Ferguson Act); *United Auto. Ass'n v. Muir*, 792 F.2d 356 (3d Cir. 1986), cert. denied, 479 U.S. 1031 (1987) ("*Muir*"); *Independent Banker's Ass'n of Am. v. Heimann*, 613 F.2d 1164, 1170-71 (D.C. Cir. 1979), cert. denied 449 U.S. 823 (1980) (Comptroller's regulation of disposition of income from sale of credit life insurance by national banks does not fall within the McCarran-Ferguson Act's protections). Although the state statutory restrictions examined by the courts of appeals differed in certain [*27] respects, the differences in specific features of the statutes were insignificant in resolving the issue of whether the state's statutory prohibition or restriction fell within the protection of the McCarran-Ferguson Act. Of more significance to the courts in resolving the issue was whether the state statutes regulated the "business of insurance," or something else.

n13 State courts have also examined the issue of whether the McCarran-Ferguson Act protects state anti-affiliation statutes. See *First Advantage Ins., Inc. v. Green*, 652 So.2d 562 (La. Ct. App. 1995), cert. granted, vacated and remanded, 64 U.S.L.W. 3656 (U.S. April 1, 1996).

In *Owensboro*, the Sixth Circuit Court of Appeals examined a Kentucky statute that prohibited national banks from acting as or affiliating with insurance agents except in strictly limited circumstances. In specifically rejecting the claim that the McCarran-Ferguson Act protected the Kentucky statute from preemption, the Sixth Circuit concluded that the Kentucky statute was not a law that regulated the business of insurance. *Id.* at 392. In reaching its conclusion, the court relied upon the criteria used by the Supreme Court, [*28] in *Pireno* when it found that certain practices of the petitioner Union Labor Life Insurance Co. did not constitute the "business of insurance" for purposes of the McCarran-Ferguson Act. Thus, the *Owensboro* court considered whether the practice or activity restricted by the statute had the effect of transferring or spreading policyholder risk, was an integral part of the policy relationship between the insurer and the insured, and was a practice limited to entities within the insurance industry. *Owensboro*, 44 F.3d at 391-92. Because the court found that the Kentucky law in no way governs the manner in

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which the activities constituting the "business of insurance" are conducted, the court concluded that the law was "enacted for the purpose of regulating certain conduct by bank holding companies, not the business of insurance." *Owensboro*, 44 F.3d at 392.

Similarly, in *Muir*, *supra*, the Court of Appeals for the Third Circuit rejected a claim that the McCarran-Ferguson Act immunized a Pennsylvania statute prohibiting mergers between financial institutions and insurance companies. In rejecting the claim, the court emphasized that the "affiliation between insurers [*29] and banks has no integral connection to the relationship between the insured and the insurer." 792 F.2d at 364. Thus, the court concluded that laws such as Pennsylvania's "have no part in the business of insurance under McCarran-Ferguson." *Id.* n14

n14 The *Blackfeet* case briefly considered this point in the context of issuance by a national bank of an annuity-like product, the Retirement CD. However, in that situation, the bank's role as issuer of the instrument in question at least could be analogized to the role of an insurer in the insurance context. No such similarity exists when a bank is simply selling, as agent, an instrument issued by another entity.

The effect of the Texas provisions at issue is to exclude national banks from participating in insurance agency activities, not to regulate the relationship between the insurer and the insured. Excluding national banks as a group from even qualifying to obtain licenses to sell annuities does not transfer or spread policyholder risk; it is not an integral part of the relationship between an insurer and its insured, and it is not aimed at a practice limited to entities within the insurance industry. As the Sixth [*30] Circuit, in *Owensboro*, correctly observed:

excluding a person from participation in an activity...is different from regulating the manner in which that activity is conducted. The former is regulation of the person; the latter is regulation of the activity.

Owensboro, 44 F.3d at 392. Accordingly, the preemption shield of the McCarran-Ferguson Act does not apply to Texas's statutory prohibitions or to any limitation that would restrict the selling of annuities by national banks to banks located in places with 5,000 or fewer inhabitants, and those provisions must be analyzed according to traditional preemption analysis.

D. Preemption of State Laws that Conflict with a Federal Statute

To the extent at state law or other regulatory actions prohibit or impede national banks from exercising their federally-granted power to sell annuities as agent, the state action is preempted by section 24(Seventh). A state law in conflict with a federal statute is "without force," whether or not Congress has expressed an intent to preempt or has otherwise occupied the field regulated by the state. See generally *Barnett Bank of Marion County v. Nelson*, 517 U.S. . [*31] 134 L.Ed.2d 237 (1996); *CSX Transp., Inc. v. Easterwood*, 507 U.S. 658, 113 S. Ct. 1732, 1737 (1993); *Cipollone v. Liggett Group, Inc.*, 505 U.S. 504, 112 S. Ct. 2608, 2617 (1992); *MacDonald v. Mansanto Co.*, 27 F.3d 1021, 1023 (5th Cir. 1994). When such a conflict occurs, a state's claim that the area is one that it has traditionally regulated is immaterial. *Fidelity Fed Sav. & Loan Ass'n v. De la Cuesta*, 458 U.S. 141, 153 (1982). A conflict between state and federal law can occur either because compliance with both state and federal law is a "physical impossibility," *Florida Lime & Avocado Growers, Inc. v. Paul*, 373 U.S. 132, 142-43 (1963), or because the state law stands "as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941). See *Barnett*, 116 S. Ct. at 1103.

The general principles of federal preemption apply with full force to state laws that affect the Federally-authorized activities of national banks. Since their creation, national banks have been recognized as appropriate "instruments designed to be used to aid the government in the administration of an important [*32] branch of public service." *Farmers' & Mechanics' Nat'l Bank v. Dearing*, 91 U.S. 29, 33 (1876). See, e.g., *First Nat'l Bank v. California*, 262 U.S. 366, 363-69 (1923); *Davis v. Elmira Sav. Bank*, 161 U.S. 275, 283 (1896). In applying federal preemption principles to conflicting state and federal laws that concern the conduct of national banks, the Supreme Court has long maintained that

an attempt by a State to define [a national bank's] duties or control the conduct of [a national bank's] affairs is void whenever it conflicts with the laws of the United States or frustrates the purposes of the national legislation or impairs the efficiency of the bank to discharge the duties for which it was created.

Davis v. Elmira Sav. Bank, 161 U.S. at 283. Accord *Easton v. Iowa*, 188 U.S. 220, 238 (1903); *Owensboro Nat'l Bank v. Owensboro*, 173 U.S. 664, 667-68 (1899).

Finally, state statutes that limit a national bank power conflict with federal law even if the federal law does not

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impose a requirement, but merely provides authority to act. *Barnett*, 113 S. Ct. at 1108; *Fidelity Fed Sav. & Loan Ass'n v. De la Cuesta*, 458 U.S. 141, 155 (1982); *Franklin* [*33] *Nat. Bank v. New York*, 347 U.S. 373, 375-379 (1954) (federal statute permitting, but not requiring, national banks to receive savings deposits, preempts conflicting prohibitory state statute). Instruction on this point is provided by *Fidelity Fed Sav. & Loan Ass'n v. De la Cuesta*, 458 U.S. 141, 155 (1982), where the Supreme Court decided that California law restricting the exercise of "due-on-sale" mortgage clauses conflicted with a federal regulation generally permitting the use of such clauses by federal thrift institutions. The Court observed that the conflict was not eliminated because the federal regulation "permits, but does not compel," the inclusion of due-on-sale clauses, because the California restriction had effectively eliminated the ability of a federal savings and loan to provide for such clauses "at its option." *Id.* at 155.

As the Supreme Court explained in *Barnett*, Congressional grants of both enumerated and incidental powers to national banks are generally interpreted in the context of national bank legislation as grants of authority "not normally limited by, but rather ordinarily preempting, contrary state law." *Barnett*, 116 S. Ct. at 1108. The [*34] Court reasoned that in defining the preemptive scope of statutes and regulations granting a power to national banks, "normally Congress would not want States to forbid, or impair significantly, the exercise of a power that Congress explicitly granted." *Id.* But, as the Court in *Barnett* recognized "to say this is not to deprive States of the power to regulate national banks, where doing so does not significantly interfere with the national bank's exercise of its powers." *Id.* n15

n15 As examples of this principle, the court cited *Anderson National Bank v. Luckett*, 321 U.S. 233, 247-252 (1944) (State statute administering abandoned deposit accounts did not unlawfully encroach on the rights and privileges of national banks; national banks are subject to state laws unless those laws infringe the national banking laws or impose an undue burden on the performance of national bank functions.); *McClellan v. Chipman*, 164 U.S. 347, 358 (1896) (Application to national banks of state statute forbidding certain real estate transfers by insolvent transferees would not destroy or hamper national banks' functions.); and *National Bank v. Commonwealth*, 76 U.S. (9 Wall.) 353, 362 (1869) (National banks subject to state law taxing bank shares that does not "interfere with, or impair [national banks'] efficiency in performing the function by which they are designed to serve [the Federal] Government."). [*35]

Under this standard, therefore, Texas state laws that interfere with national banks' exercise of their power to sell annuities would *not* be preempted if the extent of the interference is *insignificant*. n16 Clearly, that is not the case here. The state law provisions described at the outset of this letter would effectively prevent national banks from selling annuities. And, even if those provisions were read to allow annuities sales by national banks located in places with 5,000 or fewer inhabitants, the effect would, by any gauge, be a significant interference with the authority granted to national banks to sell annuities since some national banks (those not located in places with 5,000 or fewer inhabitants) would be prevented from selling annuities *at all*, and others would be precluded from basing their annuities sales in many locations. Accordingly, under either approach to the Texas state law at issue, the state law provisions would be preempted by section 24(Seventh) of the National Bank Act, which contains no such limitations on national banks' authority or eligibility to sell annuities.

n16 This test, and the cases cited by the Supreme Court, all reflect that the extent to which state law may diminish the ability of national banks to exercise their powers is limited, e.g., state law applies if it does not "encroach" on the rights of national banks; if the law would not "hamper," "infringe," or impose an "undue burden" on national bank functions; if the applicable state law would not "impair the efficiency" of those functions. [*36]

E. Conclusion

To summarize, national banks have authority under the National Bank Act to sell annuities as agent. In our opinion, the McCarran-Ferguson Act does not shield from preemption Texas laws that wholly or partially prevent national banks from selling annuities for two reasons: (1) annuities are not "insurance" for purposes of the McCarran-Ferguson Act, and (2) the McCarran-Ferguson Act does not shield a state law that results in negating the Federally-authorized corporate power of national banks to sell annuities.

These conclusions do not, however, place annuities outside the scope of federal and state laws. Variable annuities are covered by federal securities laws, and both fixed and variable annuity sales by national banks will be subject to state laws that are not preempted under recognized standards of federal preemption. n17

Apr-03-03

01:07pm

From-Covington & Burling San Francisco

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n17 For example, as noted in section D, a state law would *not* be preempted if it did not prevent national banks from exercising their Federally authorized powers, and if the extent to which the law actually interfered with or impaired the ability of national banks to exercise those powers was insignificant.

Very truly yours. ["37]

Julie L. Williams
Chief Counsel

Apr-03-03 01:08pm From-Covington & Burling San Francisco

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APPENDIX C

APPENDIX C

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Office of the Comptroller of the Currency Quarterly Journal

1994 OCC QJ LEXIS 192: 13-3 O.C.C. Q.J. 87

September, 1994

[*1] Interpretive Letters

644 - May 1994

TEXT: H. Gary Pannell, District Counsel
Southeastern District
Marquis One Tower
245 Peachtree Center Ave., NE
Atlanta, GA 30303-1223

Dear Mr. Pannell:

This is in response to your request for an opinion on the applicability of certain provisions of the Georgia Residential Mortgage Act, O.C.G.A. 7-1-1000, *et. seq.* ("the Act"), to national banks operating in Georgia. For the reasons discussed below, national banks cannot be required to register with the Georgia Department of Banking and Finance ("DBF"), nor can they be compelled to pay a \$ 6.50 fee to the DBF for every mortgage loan they close in Georgia.

I. The Georgia Residential Mortgage Act

The Act purports to apply to all persons who transact business directly or indirectly as mortgage brokers or mortgage lenders in Georgia. A mortgage broker is defined as any person who directly or indirectly solicits, processes, places or negotiates mortgage loans for others; a mortgage lender is any person who, directly or indirectly, makes, originates, or purchases mortgage loans or who services mortgage loans. The Act's provisions extend to any mortgage lender or mortgage broker, even [*2] those located outside Georgia, if the property securing the mortgage loan is located in the state.

The Act contains registering and licensing requirements for all mortgage brokers and lenders unless exempted. Banks, savings institutions, building and loan associations and credit unions chartered under federal or state law that have offices in Georgia are exempt from

the licensing and registration requirements under the Act. O.C.G.A. 7-1-1001(a)(1). However, federally chartered institutions with no business location in the state must register with the DBF if they engage in residential mortgage lending activities in Georgia. O.C.G.A. 7-1-1001(b). In addition, out-of-state banks with a business location in Georgia, such as a representative office or a loan production office, must register with the DBF as a foreign bank. O.C.G.A. 7-1-590. Such institutions must register on forms provided by the DBF and pay an annual registration fee of \$ 800.

All mortgage lenders and brokers, even if exempt from the Act's licensing and registration requirements, must pay a fee of \$ 6.50 per mortgage loan closed in Georgia. Along with this fee, all mortgage lenders and brokers must submit [*3] a form to the DBF that contains the name of the institution, its license and registration number (if applicable), and the number of loans closed during the reporting period. The DBF can issue administrative orders to enforce compliance with any provision of the Act. Failure to comply with such an order may result in civil fines of up to \$ 1,000 per day and imprisonment of responsible employees for not more than one year. O.C.G.A. 7-1-1018(c) and -1019.

II. Discussion

A. Federal Preemption

The supremacy clause of the Constitution provides that "[t]his Constitution, and the Laws of the United States which shall be made in Pursuance thereof . . . shall be the supreme Law of the Land . . . any Thing in the Constitution or Laws of any State to the Contrary notwithstanding." U.S. Const. art. VI, cl. 2. Thus, "[t]he constitution and laws of a state, so far as they are repugnant to the constitution and laws of the United States, are absolutely void." *Cohen v. Virginia*, 19 U.S. (6 Wheat.) 264, 414 (1821)(Marshall, C.J.). However, non-conflicting state and federal authority in a particular area may coexist if Congress has not moved to assert

1994 OCC QJ LEXIS 192. *; 13-3 O.C.C. QJ. 87

exclusive federal jurisdiction. [*4] See *California Coastal Comm'n v. Granite Rock Co.*, 480 U.S. 572 (1987).

There are many occasions when national banks are legitimately bound by state law. Nevertheless, national banks derive their powers and authority under federal law, and they are not subject to state law if it conflicts with some paramount federal law. *Flood v. City Nat'l Bank of Clinton*, 220 Iowa 935, 263 N.W. 321 (1935), cert. denied, 298 U.S. 666 (1936). As the Supreme Court explained:

National banks are instrumentalities of the Federal government created for a public purpose, and as such necessarily subject to the paramount authority of the United States. It follows that an attempt by a state to define their duties, or control the conduct of their affairs, is absolutely void, whenever such attempted exercise of authority expressly conflicts with the laws of the United States, and either frustrates the purpose of the national legislation, or impairs the efficiency of these agencies of the Federal government to discharge the duties for the performance of which they were created.

McClellan v. Chipman, 164 U.S. 347, 356-57 (1896).

In my opinion, the registration and fee provisions [*5] of the Georgia Residential Mortgage Act are preempted by federal banking law.

B. Registration

The Act exempts most federally chartered banks from its licensing and registration provisions. O.C.G.A. 7-1-1001(b). As noted above, however, out-of-state banks with a business location, such as a loan production office, in Georgia are required to register annually with the DBF; out-of-state federally chartered institutions with no business location in the state must also register with the DBF if they engage in residential lending in Georgia. O.C.G.A. 7-1-590 and 1001(b). Such institutions are required to pay an annual registration fee of \$ 800. O.C.G.A. 80-5-1-.02(c)(3). These requirements are inapplicable to national banks.

Under the Act, "[n]o person required to register under this subsection shall transact business in this state directly or indirectly as a mortgage broker or a mortgage lender unless such person is registered with the department." Thus, the Act attempts to predicate the ability of national banks located outside Georgia to do business in Georgia upon their registration with the DBF. As such, the Act's registration provision amounts to a state licensing [*6] requirement. "A license is in the

nature of a special privilege, entitling the licensee to do something that he would not otherwise be entitled to do without the license." OCC Interpretive Letter No. 122, *Fed. Banking L. Rep. (CCH) P 185,203* (August 1, 1979); see also 51 Am. Jur. 2d *Licenses and Permits*, § 1 (1970). The Georgia requirement clearly fits this description because registration is mandatory and failure to comply with the Act is punishable as a misdemeanor, with accompanying fines or imprisonment. O.C.G.A. 7-1-1017(d).

As instrumentalities of the federal government, national banks are not required to obtain state approval for the exercise of the powers granted to them by Congress. See *Bank of America v. Lima*, 103 F. Supp. 916 (D. Mass. 1952) (Exercise of national bank powers is not subject to state approval and states have no authority to require national banks to obtain a license to engage in any activity permitted to them by federal law.) National banks are authorized by federal law to exercise "incidental powers . . . necessary to carry on the business of banking. . . ." 12 U.S.C. 24 (Seventh). The mortgage lending activities that are the subject [*7] of the Georgia Act are directly related to a national bank's express authority to lend money secured by personal or real property. Consequently, these federally authorized activities are not subject to the qualification that they must be further authorized by state officials.

C. The Georgia Residential Mortgage Act Per Loan Fee

The Act requires that "[a]ny person who closes mortgage loans . . . regardless of whether said person is required to be licensed or registered . . . shall pay the Department a per loan fee of \$ 6.50 for each mortgage closed by that person on and after January 1, 1994." 80-5-1-.04. The Act is notably silent on the purpose of this fee. This office has in the past suggested that a fee imposed by a state or municipality may be applicable to national banks if it constitutes a tax instead of a payment to support a licensing system. See Letter of Richard V. Fitzgerald (October 22, 1986) ("Fitzgerald letter"). However, the per loan fee at issue does not constitute a permissible state tax.

Under 12 U.S.C. 548, national banks are subject to state taxation to the same extent as state banks:

For the purposes of any tax law enacted under authority [*8] of the United States or any State, a national bank shall be treated as a bank organized and existing under the laws of the State or other jurisdiction within which its principal office is located.

1994 OCC QJ LEXIS 192, *; 13-3 O.C.C. Q.J. 87

12 U.S.C. 548. One factor that distinguishes a licensing fee from a tax is the existence of a licensing scheme that vests the licensing authority with discretion to grant or deny the license based upon an applicant's adherence to certain proscribed rules or standards. Fitzgerald letter at 3. As discussed above, the Act creates such a scheme that purports to apply to at least some national banks.

A second factor that distinguishes a licensing fee from a tax is that the former generally bears a reasonable relationship to the cost of administering a specific regulatory program. *Arends v. Police Pension Fund of Peoria, et al.*, 130 N.E. 2d 517 (Ill. 1955). A tax, on the other hand, is typically paid to the state general fund and used for any state purpose. The per loan fee imposed by the Act is paid directly to the Georgia DBF instead of the state treasury. Clearly, then, the per loan fee is intended to offset the administrative costs associated with the Act. To the extent those [*9] costs would largely be associated with the licensing and supervision provisions of the Act, national banks are not required to help defray them.

Even assuming that the licensing and registration fees paid by non-exempt mortgage lenders and brokers cover the costs associated with the administration of those provisions, the per loan fee would still be inapplicable to national banks. In addition to the licensing and registration provisions, the Act contains various other restrictions of the practices of mortgage lenders and brokers. For example, the Act contains disclosure and advertising requirements. O.C.G.A. 80-11-1-.01 and .02. Assuming for the sake of this discussion that such provisions are applicable to national banks, national banks should not have to pay for state enforcement of these laws.

Under 12 U.S.C. 482, the OCC is the exclusive supervisor of national banks and is authorized by Congress to assess fees against national banks to pay for the cost of their supervision. This authority includes examination for compliance with applicable state laws. *Natl State Bank, Elizabeth, N.J. v. Long*, 630 F.2d 981 (3d Cir. 1980); see *Conference of Fed. Sav. & Loan Ass'ns* [*10] *v. Stein*, 604 F.2d 1256 (9th Cir.), *aff'd*

mem., 445 U.S. 921 (1979) (federal regulator is the proper authority to enforce state laws applicable to federal thrifts.) "Since this Office examines national banks for compliance with state consumer laws, and the banks pay for this procedure . . . it would be difficult to justify a requirement that national banks pay [similar] fees in support of them" to state regulators. Letter of J. T. Watson, Deputy Comptroller of the Currency (January 7, 1975) (unpublished).

Because the Georgia Residential Mortgage Act Per Loan Fee is not a permissible state tax and is intended to defray the costs of inapplicable licensing requirements or for state enforcement powers that do not extend to national banks, it is preempted by federal law. *

* This conclusion is consistent with Executive Order 12612, which allows federal preemption of a state law "only when the statute contains an express preemption provision or there is some other firm or palpable evidence compelling the conclusion that the Congress intended preemption of State law, or when the exercise of State authority directly conflicts with the exercise of Federal authority under the Federal statute." The statutes discussed above constitute such firm and palpable evidence of Congressional intent to preempt state law in this area. In addition, the exercise of state authority by the Georgia DBF directly conflicts with the exercise of federal authority over national banks. [*11]

III. Conclusion

Although state laws may embody important state policy, under the supremacy clause the relative importance to a state of its own law is not material when there is a conflict with federal law; any state law that interferes with, or is contrary to federal law, must yield. Therefore, it is my conclusion that the provisions of the Georgia Residential Mortgage Act discussed in this letter are preempted by federal law, with respect to national banks.

Peter Liebesman
Assistant Director
Bank Operations and Assets Division

Apr-03-03 01:09pm From-Covington & Burling San Francisco

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T-154 P.017/041 F-063

APPENDIX D



Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

February 11, 2003

Demetrios A. Boutris
Commissioner
California Department of Corporations
1515 K Street, Suite 200
Sacramento, California 95814-4052

Dear Mr. Boutris:

It has come to the attention of the Office of the Comptroller of the Currency ("OCC") that the California Department of Corporations ("Department") has sent its agents into one of the offices of Wells Fargo Home Mortgage, Incorporated ("WFHMI"), in order to conduct an examination of its mortgage operations. For the reasons set forth below, I urge you to suspend these efforts so that we may constructively discuss the status of, and OCC's authority with respect to, WFHMI.

It appears that the examination is being conducted pursuant to licensing provisions under California's Residential Mortgage Lending Act ("California Act") and other provisions of California law. Such an examination violates Federal law.¹ WFHMI is a wholly-owned operating subsidiary of Wells Fargo Bank, N.A. ("Bank"), a national bank chartered by the OCC. Pursuant to federal regulations, the OCC has authorized the Bank to conduct the mortgage banking business through WFHMI and has licensed WFHMI as an operating subsidiary of the Bank for that purpose. As an operating subsidiary of a national bank, WFHMI is subject to ongoing supervision and examination by the OCC in the same manner and to the same extent as the Bank.²

¹ Wells Fargo Bank, N.A., and WFHMI recently filed suit in the United States District Court for the Eastern District of California to obtain a judicial determination confirming that WFHMI is not subject to licensing by the Department or to the Department's supervisory, regulatory or enforcement authority and seeking injunctive relief. That case is *Wells Fargo Bank, N.A. v. Demetrios A. Boutris*, No. S 03-0157 GEB JFM, filed January 27, 2003.

² Twelve C.F.R. § 5.34(e)(3) provides that -

[a]n operating subsidiary conducts activities authorized under this section pursuant to the same authorization, terms and conditions that apply to the conduct of such activities by its parent national bank. If, upon examination, the OCC determines that the operating subsidiary is operating in violation of law, regulation, or written condition, or in an unsafe or unsound manner or otherwise threatens the safety or soundness of the bank, the OCC will direct the bank or operating subsidiary to take appropriate remedial action, which may include requiring the bank to divest or liquidate the operating subsidiary, or discontinue specified activities. OCC authority

As discussed in detail below, pursuant to 12 U.S.C. § 484, and 12 C.F.R. §§ 5.34(e)(3) and 7.4006, the OCC has exclusive visitorial authority over national banks and their operating subsidiaries except where *Federal* law provides otherwise. This authority pertains to activities expressly authorized or recognized as permissible for national banks under Federal law or regulation, or by OCC issuance or interpretation, including the content of those activities and the manner in which, and standards whereby, those activities are conducted. As a result, States are precluded from examining or requiring information³ from national banks or their operating subsidiaries or otherwise seeking to exercise visitorial powers with respect to national banks or their operating subsidiaries in those respects. Thus, Federal law precludes examination of WFHMI by the Department. Moreover, for the reasons discussed below, operating subsidiaries – like their parent national banks – need not obtain the approval of a State to engage in an activity that they have been licensed to conduct under Federal law. Accordingly, any State licensing requirements upon which the Department relies to assert jurisdiction do not apply to the Bank or WFHMI.⁴

Background

The OCC's exclusive visitorial authority over national bank operations is established by 12 U.S.C. § 484.⁵ Paragraph (a) of that section states that --

[n]o national bank shall be subject to any visitorial powers except as authorized by Federal law, vested in the courts of justice or such as shall be, or have been

under this paragraph is subject to the limitations and requirements of section 43 of the Federal Deposit Insurance Act (12 U.S.C. 1831v) and section 113 of the Gramm-Leach-Bliley Act [GLBA] (12 U.S.C. 1820a).

The provisions of the Federal Deposit Insurance Act and the GLBA referenced in the regulation pertain to the functional regulation of securities, insurance, and commodities firms. These provisions are not relevant to mortgage lending and servicing activities conducted by WFHMI.

³ The OCC currently maintains information sharing agreements with 48 States, the District of Columbia, and Puerto Rico. These agreements provide a mechanism through which State regulators may seek and obtain supervisory information from the OCC. Typically, the OCC will make confidential bank examination information available to State bank regulatory agencies if they demonstrate a specific regulatory need for the examination information (e.g., in connection with a merger of a national bank into a State bank, where the State bank regulator must approve the transaction), and if the State agency has entered into an appropriate information sharing/confidentiality agreement with the OCC governing the use of the information. In OCC Advisory Letter 2002-9 (Nov. 25, 2002) ("AL 2002-9"), the OCC outlined a procedure to address circumstances when State officials raise issues concerning potential violations of laws by national banks, including when State officials may seek information from a national bank about its compliance with any law or for other purposes. The advisory letter is available on the OCC's website at www.occ.treas.gov/ftp/advisory/2002%2D9.txt.

⁴ We note that the California Act already contains an exemption from State licensing requirements for national banks, Cal. Fin. Code § 50003(g), but fails to recognize the status of national bank operating subsidiaries as entities through which national banks operate pursuant to a federal license granted by the OCC.

⁵ "Visitorial powers" generally refers to the power to "visit" a national bank to examine the conduct of its business and to enforce its observance of applicable laws. See, e.g., *Guthrie v. Harkness*, 199 U.S. 148, 158 (1905) (the word "visitation" means "inspection; superintendence; direction; regulation") (internal quotations omitted).

exercised or directed by Congress or by either House thereof or by any committee of Congress or of either House duly authorized.

Paragraph (b) of the statute then permits lawfully authorized State auditors or examiners to review a national bank's records "solely to ensure compliance with applicable State unclaimed property or escheat laws upon reasonable cause to believe that the bank has failed to comply with such laws."

This provision, enacted with the creation of the national banking system in 1863, is integral to the design and structure of the national banking system and fundamental to the character of national banks. Congress enacted the National Currency Act ("Currency Act") in 1863 and the National Bank Act the year after for the purpose of establishing a new national banking system that would operate distinctly and separately from the existing system of State banks. At that time, both proponents and opponents of the new national banking system expected that it would supersede the existing system of State banks.⁶ Given this anticipated impact on State banks and the resulting diminution of control by the States over banking in general, proponents of the national banking system were concerned that States would attempt to undermine it.

The allocation of any supervisory responsibility for the new national banking system to the States would have been inconsistent with the need to protect national banks from State interference. Congress, accordingly, established a Federal supervisory regime and created a Federal agency within the Department of Treasury—the OCC—to carry it out. Congress granted the OCC the broad authority "to make a thorough examination of all the affairs of [a national] bank,"⁷ and solidified this Federal supervisory authority by vesting the OCC with exclusive

⁶ Representative Samuel Hooper, who reported the bill to the House, stated in support of the legislation that one of its purposes was "to render the law [i.e., the Currency Act] so perfect that the State banks may be induced to organize under it, in preference to continuing under their State charters." Cong. Globe, 38th Cong., 1st Sess. 1256 (March 25, 1864). Opponents of the legislation believed that it was intended to "take from the States . . . all authority whatsoever over their own State banks, and to vest that authority . . . in Washington . . ." Cong. Globe, 38th Cong., 1st Sess. 1267 (March 24, 1864) (statement of Rep. Brooks). See also statement of Rep. Pruyn (stating that the legislation would "be the greatest blow yet inflicted upon the States . . .") Cong. Globe, 38th Cong., 1st Sess. 1271 (March 24, 1864); statement of Sen. Sumner ("Clearly, the [national] bank must not be subjected to any local government, State or municipal; it must be kept absolutely and exclusively under that Government from which it derives its functions.") Cong. Globe, 38th Cong., 1st Sess., at 1893 (April 27, 1864).

⁷ See, e.g., *Tiffany v. National Bank of the State of Missouri*, 35 U.S. 409, 412-413 (1874) ("It cannot be doubted, in view of the purpose of Congress in providing for the organization of national banking associations, that it was intended to give them a firm footing in the different states where they might be located. It was expected they would come into competition with state banks, and it was intended to give them at least equal advantages in such competition National banks have been national favorites. They were established for the purpose, in part, of providing a currency for the whole country, and in part to create a market for the loans of the general government. It could not have been intended, therefore, to expose them to the hazard of unfriendly legislation by the states, or to ruinous competition with state banks."). See also B. Hammond, *Banks and Politics in America from the Revolution to the Civil War*, 725-34 (1957); P. Studenski & H. Kraoss, *Financial History of the United States*, 155 (1st ed. 1952).

⁸ Act of June 3, 1864, c. 106, § 54, 13 Stat. 116, codified at 12 U.S.C. § 481.

visitorial powers over national banks. These provisions assured, among other things, that the OCC would have comprehensive authority to examine all the affairs of a national bank and protected national banks from potential State action by establishing that the authority to examine and supervise national banks is vested *only* in the OCC, unless otherwise provided by *Federal law*.⁹

In *Guthrie v. Harkness*, 199 U.S. 148 (1905), the Supreme Court recognized how the National Bank Act was designed to operate:

Congress had in mind, in passing this section [i.e., section 484] that in other sections of the law it had made full and complete provision for investigation by the Comptroller of the Currency and examiners appointed by him, and, authorizing the appointment of a receiver, to take possession of the business with a view to winding up the affairs of the bank. It was the intention that this statute should contain a full code of provisions upon the subject, and that no state law or enactment should undertake to exercise the right of visitation over a national corporation. Except in so far as such corporation was liable to control in the courts of justice, this act was to be the full measure of visitorial power.

Id. at 159. The Supreme Court also has recognized the clear intent on the part of Congress to limit the authority of States over national banks precisely so that the nationwide system of banking that was created in the Currency Act could develop and flourish. For instance, in *Easton v. Iowa*, 188 U.S. 220 (1903), the Court stated that Federal legislation affecting national banks—

has in view the erection of a system extending throughout the country, and independent, so far as powers conferred are concerned, of state legislation which, if permitted to be applicable, might impose limitations and restrictions as various and as numerous as the States It thus appears that Congress has provided a symmetrical and complete scheme for the banks to be organized under the provisions of the statute [W]e are unable to perceive that Congress intended to leave the field open for the States to attempt to promote the welfare and stability of national banks by direct legislation. If they had such power it would have to be exercised and limited by their own discretion, and *confusion would necessarily result from control possessed and exercised by two independent authorities.*

Id. at 229, 231-232 (emphasis added). The Court in *Farmers' and Mechanics' Bank*, 91 U.S. 29 (1875), after observing that national banks are means to aid the government, stated—

⁹ Writing shortly after the Currency Act and National Bank Act were enacted, then-Secretary of the Treasury, and formerly the first Comptroller of the Currency, Hugh McCulloch observed that "Congress has assumed entire control of the currency of the country, and, to a very considerable extent, of its banking interests, prohibiting the interference of State governments . . ." Cong. Globe, 39th Cong., 1st Sess., Misc. Doc. No. 100, at 2 (April 23, 1866).

Being such means, brought into existence for this purpose, and intended to be so employed, the States can exercise no control over them, nor in any wise affect their operation, except in so far as Congress may see proper to permit. Any thing beyond this is "an abuse, because it is the usurpation of power which a single State cannot give."

Id. at 34 (citation omitted).

Congress recently affirmed the OCC's exclusive visitorial powers with respect to national banks operating on an interstate basis in the Riegle-Neal Interstate Banking Act of 1994 ("Riegle-Neal").¹⁰ Riegle-Neal makes interstate operations of national banks subject to specified types of laws of a "host" State in which the bank has an interstate branch to the same extent as a branch of a State bank of that State, *unless* the State law is preempted by Federal law. For those State laws that are not preempted, the statute makes clear that the authority to enforce the law is vested in the OCC. See 12 U.S.C. § 36(f)(1)(B) ("The provisions of any State law to which a branch of a national bank is subject under this paragraph shall be enforced, with respect to such branch, by the Comptroller of the Currency."). This approach is another, and very recent, recognition of the broad scope of the OCC's exclusive visitorial powers with respect to national banks.

Application of Federal Law to the Operating Subsidiaries

In section 121 of the Gramm-Leach-Bliley Act ("GLBA"), Congress expressly acknowledged that national banks may own subsidiaries that engage "solely in activities that national banks are permitted to engage in directly and are conducted subject to the same terms and conditions that govern the conduct of such activities by national banks."¹¹

Consistent with section 121, the OCC regulations state that "[a]n operating subsidiary conducts activities authorized under [12 C.F.R. § 5.34] pursuant to the same authorization, terms and conditions that apply to the conduct of such activities by its parent national bank."¹² Addressing this point in the context of State laws, section 7.4006 of our regulations specifically states that "[u]nless 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."¹³

In order for a subsidiary to operate in the manner contemplated by section 121 of GLBA, the subsidiary must be subject to the same regulation and supervision as is its parent national bank. As described at the outset of this letter, our regulations at § 5.34(e)(3) require that result, which

¹⁰ Pub. L. 103-328, 108 Stat. 2338 (Sept. 29, 1994).

¹¹ Pub. L. No. 106-102, § 121, 113 Stat. at 1378, *codified at* 12 U.S.C. § 24a(2)(3).

¹² 12 C.F.R. § 5.34(e)(3).

¹³ 12 C.F.R. § 7.4006.

is entirely consistent with the concept of an operating subsidiary as an OCC-licensed entity through which national banks conduct bank-permissible activities. The terms and conditions governing the conduct of activities in an operating subsidiary include being subject to the same visitorial powers as are exercised with respect to the parent. Accordingly, just as 12 U.S.C. § 484 prevents the Department from exercising visitorial powers over the Bank, so too do section 484 and OCC regulations prevent the Department from exercising visitorial powers over WFHMI, an OCC-licensed operating subsidiary through which the Bank conducts authorized mortgage banking activities.

It is important in this context to understand that while the Department may not examine and supervise WFHMI, the operating subsidiary is subject to an extensive regime of Federal law and regulations and the Bank and WFHMI are subject to comprehensive and continuous supervision by the OCC. The Bank is part of the OCC's Large Bank Program. This means that its activities and those of its subsidiaries are examined on a continuous basis by teams of examiners specifically assigned to, and in most cases physically present at the facilities of, the Bank and its subsidiaries.

With regard to the application of State licensing requirements, it is well established that a State may not condition a national bank's exercise of a permissible Federal power on obtaining the State's prior approval, including the imposition of State licensing requirements as a predicate to the exercise of that power.¹⁴ The result is the same whether the national bank exercises the power directly, or through an operating subsidiary that has been licensed by the OCC. In both cases, the bank, or the operating subsidiary, has obtained a *Federal* license to conduct its business.

When the OCC charters a national bank, it grants the bank a license to commence the banking business under 12 U.S.C. § 27. When a national bank acquires or establishes an operating subsidiary through which the bank will conduct bank-permissible activities, the OCC grants a license for the operating subsidiary to conduct those activities pursuant to 12 C.F.R. § 5.34. Requirements for establishing or acquiring an operating subsidiary are expressly described in OCC regulations as "Licensing requirements."¹⁵ Accordingly, when WFHMI was established as an operating subsidiary of the Bank and was licensed by the OCC as an entity through which the Bank was authorized to conduct its mortgage lending business, WFHMI did not then, and does

¹⁴ See *First National Bank of Eastern Arkansas v. Taylor*, 907 F.2d 775, 780 (8th Cir. 1990) (the National Bank Act precludes a State regulator from prohibiting a national bank, through either enforcement action or a license requirement, from conducting an activity that the Comptroller has reasonably determined is authorized by the National Bank Act); *Ass'n. of Banks in Insurance, Inc. v. Duryae*, 55 F. Supp. 2d 799, 812 (S.D. Ohio 1999), *aff'd*, 270 F.3d 397 (6th Cir. 2001) (even the most limited aspects of State licensing requirements such as the payment of a licensing fee are preempted because they "constitute impermissible conditions upon the authority of a national bank to do business within the state"). The OCC also has opined previously that State laws purporting to require the licensing of activities authorized for national banks under Federal law are preempted. See OCC Interpr. Ltr. No. 749 (Sept. 13, 1996) reprinted in [1996-1997 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-114 (State law requiring national banks to be licensed by the State to sell annuities would be preempted); OCC Interpr. Ltr. No. 644 (March 24, 1994), reprinted in [1994 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,553 (State registration and fee requirements imposed on mortgage lenders would be preempted).

¹⁵ 12 C.F.R. § 5.34(b).

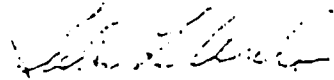
not now, also need a State-issued license to do that business. Just as the Bank has a Federal license to conduct the banking business and needs no additional State license, so too does WFHMI have a federal license for the Bank to conduct its mortgage lending business through WFHMI and needs no additional State-granted permit to do so. Section 7.4006 similarly confirms that State licensing requirements are equally inapplicable to Federally-authorized activities conducted by a national bank directly or through a federally-licensed operating subsidiary. In practical effect, therefore, your actions would have the effect of depriving the Bank and WFHMI of the right to conduct a mortgage lending business they have been authorized to conduct under a license issued under Federal law.

I must also note that these conclusions that the OCC's exclusive visitorial powers preclude the Department from examining and asserting supervisory authority over, or applying state licensing requirements to WFHMI are not intended to imply that any of the substantive provisions of the California Act apply to WFHMI. Instead, under Federal law¹⁶ and principles of preemption established by the courts,¹⁷ provisions of the California Act may well be preempted. This letter, however, addresses only the issues of whether the Department may conduct an examination of WFHMI and whether WFHMI is required to obtain a State license in order to conduct mortgage banking activities that it is authorized to conduct under a Federally-granted license.

I hope the foregoing helps to clarify our concerns with regard to the Department's recent actions. I urge you to suspend the Department's efforts to examine and regulate WFHMI so that we may the opportunity to have a more constructive discussion of our relative roles.

If you have any questions regarding this letter, please do not hesitate to contact Horace G. Sneed, Assistant Director, Litigation Division, at (202) 874-5280.

Sincerely,



Julie L. Williams
First Senior Deputy Comptroller and Chief Counsel

Cc: Stanley S. Stroup, Executive Vice President, General Counsel

¹⁶ See, e.g., 12 U.S.C. §§ 371, 1735f-7, 1735f-7a, and 3601 *et. seq.*

¹⁷ See, e.g., the cases cited in note 12, *supra*.

Apr-03-03 01:11pm From-Covington & Burling San Francisco

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T-154 P.025/041 F-063

APPENDIX E

LEXSEE 1993 occ ltr lexis 8

Comptroller of the Currency
Washington, DC 20219

March 1993 SBJ 35A, SBJ 35E

Interpretive Letter No. 614

1993 OCC Ltr. LEXIS 8

January 15, 1993

[*1] This is in response to your inquiry concerning statutory provisions from three states that purport to impose requirements on lenders, including national banks, that issue credit cards to customers in those states. In your letter, you opined that such statutes would not be applicable to national banks. For the reasons discussed below, I agree with your conclusions.

DISCUSSION

Visitation and Enforcement Authority

With limited exceptions, Congress has granted the OCC exclusive supervision and enforcement authority with respect to national banks. 12 U.S.C. § 484(a); 12 C.F.R. § 7.6025(b). The only exception to this rule is found in 12 U.S.C. § 484(b), which permits a very limited state review of national bank records to ensure compliance with state escheat or unclaimed property laws and, even then, only upon "reasonable cause."

The Supreme Court has stated that "no state law or enactment should undertake to exercise the right of visitation over a national corporation." *Guthrie v. Harkness*, 199 U.S. 148, 159 (1905). The term "visitation" has been expansively defined to include any act of a superintending official to inspect, regulate, or control the operations of [*2] a bank to enforce the bank's observance of the law. *First National Bank of Youngstown v. Hughes*, 6 F. 737, 740 (6th Cir. 1881), appeal dismissed, 106 U.S. 523 (1883). Although there may be no comprehensive definition of "visitorial" powers, they certainly include the examination of a bank's books and records. *National State Bank. Elizabeth, N.J. v. Long*, 630 F.2d 981 (3d Cir. 1980). Furthermore, state-law-required registrations and

investigations of national banks are "visitations" and, therefore, are preempted by federal law as an unauthorized state attempt to superintend or regulate a national bank's activities. See Letter from James F.E. Gillespie, Jr., Senior Attorney, Legal Advisory Services Division ("LASD") (Aug. 11, 1986) (unpublished) ("Gillespie letter").

The enforcement authority of the OCC has not been limited to the enforcement of federal law. Although states have an important interest in ensuring that their laws are obeyed, the OCC is the exclusive regulator of national banks. It is, therefore, the province of the OCC, not state regulators, to examine national banks for compliance with state laws. *Long*, 630 F.2d at 988. See generally [*3] 12 U.S.C. § 1818(b) et seq. Cf. *Conference of Fed. Sav. & Loan Ass'ns v. Stein*, 604 F.2d 1256 (9th Cir.), aff'd mem., 445 U.S. 921 (1979) (federal regulator is the proper authority to enforce state laws applicable to federal thrifts). Congress has delegated to the OCC the authority to issue cease and desist orders and to take other enforcement actions, including levying civil money penalties, against national banks to ensure that they comply with laws applicable to them, including state laws. *Long*, 630 F.2d at 988-89. See generally 12 U.S.C. § 1818(b) et seq.

In light of the foregoing legal authority, the OCC consistently has maintained that state attempts to exercise supervisory and enforcement authority over national banks are preempted. See, e.g., Interpretive Letter No. 475, [1989-1990 Transfer Binder] *Fed. Banking L. Rep.* P83,012 (Mar. 22, 1989); Gillespie letter, supra; letter from Peter Liebesman, Assistant Director, LASD (Dec. 13, 1983) (unpublished); Interpretive Letter No. 122, [1981-1982 Transfer Binder] *Fed. Banking L. Rep.* (CCH) P85,203 (Aug. 1, 1979). As the regulatory agency charged with administering the national banking [*4] laws, the OCC's interpretation is entitled to deference. *Clarke v. Securities Indus. Ass'n*, 479 U.S. 388, 403-04 (1987).

Application of Preemption Principles to Statutes at Hand

Most of the state statutes about which you inquired involve attempts by the states to exercise supervisory powers over national banks and are preempted with respect to national banks.

1993 OCC Ltr. LEXIS 8. *

The Idaho Credit Code n1 ("Idaho Code") requires credit card issuers, licensed in the state, to maintain records that will enable the Director of the Department of Finance to determine whether the licensee is complying with the provisions of the Idaho Code. Idaho Code § 28-46-304(1). The Idaho Code also requires issuers of credit cards to Idaho residents to file both a composite annual report and an annual notification with the Director. Idaho Code § 28-46-202 and -304(2). While the Idaho Code provides that some examination, investigation, and enforcement powers over supervised financial organizations, including national banks, should be exercised by their appropriate regulator, the Director is given the authority to exercise all other powers of the statute over such supervised institutions. Idaho Code § [*5] 28-46-105(1). In addition, the Director is authorized to bring civil actions to restrain violations of the Idaho Code and to recover civil penalties for repeated and intentional violations. Idaho Code § 28-46-110 and -113(2). These Idaho Code sections purport to grant visitatorial powers to the Director over national bank credit card issuers, inasmuch as they mandate maintaining records and filing notifications with the Director and provide that statutory violations are subject to civil action by the Director. As such, these provisions are preempted with respect to national banks. The OCC, rather than state officials, will enforce any state laws that apply to national banks.

n1 The Idaho Credit Code appears to exempt out-of-state issuers from its requirements. However, any credit card issuers, including national banks, that do not utilize an out-of-state mailing address would not be exempted. Thus, the Idaho Credit Code ostensibly applies to national banks located in Idaho that issue credit cards, as well as any national banks with application processing facilities located in that state. See Idaho Code § 28-41-201(3).

The Wisconsin Consumer Act ("Wisconsin Act") [*6] requires any person, including a national bank, making consumer credit transactions in which a finance charge exceeding 12% is imposed, to file a notification with the Commissioner of Banking within 30 days after commencing business within the state and annually thereafter. Wis. Stat. § 426.201. An annual fee based on the issuer's average monthly outstanding credit balance must be paid by all persons required to file notifications. Wis. Stat. § 426.202(2). The Wisconsin Act also requires such persons to submit data to the Commissioner to support computation of the annual fee. Wis. Stat. § 426.202(4). The notification requirement is mandatory and failure to comply is grounds for legal action, which may be brought by the Commissioner, to

recover fees or civil action to recover civil money penalties against violators of the notification and fee requirements. Wis. Stat. § 426.301. Clearly, the required submission of financial records is an exercise of visitatorial power over national bank credit card issuers and is preempted. The notification requirement and enforcement provision likewise are exercises of visitatorial power and are preempted with respect to national banks. See [*7] Letter from Mitchell G. Stern, Senior Attorney, Central District (June 26, 1989) (opining that the notification requirement of the Wisconsin Consumer Act constitutes an act of bank supervision which is preempted by federal law) (unpublished). Accordingly, the Commissioner may not enforce these statutory requirements against national banks.

The Wyoming Uniform Consumer Credit Code's notification requirement is substantially similar to those in the Idaho Code and the Wisconsin Act. See Wyo. Stat. § 40-14-630 and -631. State officials are authorized to bring legal actions to recover fees or civil action to recover civil money penalties against violators of the state's notification and fee requirements. See Wyo. Stat. § 40-14-610 and -613(b). See also Wyo. Stat. § 40-14-605. Although the Administrator of the Banking Division has not enforced these provisions against national banks, the statutory requirements remain in the Code. The Wyoming notification and enforcement provisions are preempted with respect to national banks.

Licensing Authority

As instrumentalities of the federal government, national banks' powers are granted by Congress. One of the powers [*8] expressly granted to national banks by federal law is that of lending money on personal security. 12 U.S.C. § 24 (Seventh). The exercise of this power cannot be subject to the approval of state officials, and states have no power to require national banks to obtain a license to engage in an activity that is permitted to them by federal law. See *Bank of America v. Lima*, 103 F. Supp. 916 (D. Mass. 1952). The OCC consistently has taken the position that state laws that attempt to license the lawful activities of national banks, whether domiciled in that state or not, are preempted. See, e.g., letter from Bruce Oliver, Attorney, Northeastern District (Apr. 26, 1988) (unpublished) (lending to out-of-state borrowers); letter from Richard V. Fitzgerald, Chief Counsel (Oct. 22, 1986) (unpublished) (license to operate); Gillespie letter, supra (securities brokerage); Interpretive Letter No. 122, supra (municipal finance consulting); letter from Roberta Walsh Boylan, Assistant Director, LASD (June 14, 1978) (unpublished) (out-of-state loan servicing).

1993 OCC Ltr. LEXIS 8. *

The Idaho Code prohibits the issuance of credit cards by issuers, including national banks, which are either located [*9] in Idaho or use an Idaho mailing address, to Idaho residents unless the issuer first obtains a license from the Director of the Department of Finance. Idaho Code § § 28-46-301 through -303. These sections of the Idaho Code, relevant to licensing, are preempted with respect to national banks.

CONCLUSION

In sum, the Idaho, Wisconsin and Wyoming statutes about which you inquired impose state licensing

requirements upon national banks or subject national banks to visitation or enforcement by state officials. These provisions are preempted with respect to national banks.

I trust this reply has been responsive to your request.

Sincerely,

Wallace S. Nathan
Director
Bank Operations and Assets Division

Apr-03-03 01:13pm From-Covington & Burling San Francisco

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T-154 P.029/041 F-063

APPENDIX F

APPENDIX F

Page 1

Not Reported in F.Supp.2d
(Cite as: 1999 WL 33429989 (N.D.Cal.))

H

Only the Westlaw citation is currently available.

United States District Court, N.D. California.

BANK OF AMERICA, N.A., et al., Plaintiffs,
v.
CITY AND COUNTY OF SAN FRANCISCO, et
al., Defendants.

No. C 99-4817 VRW.

Nov. 15, 1999.

Covington & Burling, Washington, D.C., By: E.
Edward Bruce, Covington & Burling, San
Francisco, California, By: Richard Darwin,
Reported By: Diane E. Skillman, Official Court
Reporter, Computerized Transcription By Eclipse,
for Plaintiffs Bank of America & Wells Fargo.

Pillsbury, Madison & Sutro LLP, San Francisco,
California, By: Michael Kass, Rodney Peck, for
Plaintiff California Bankers Association.

Louise H. Remme, City Attorney, San Francisco,
California, By: Daniel Bernhard, Deputy City
Attorney, Owen Marikan, Deputy City Attorney,
for Defendant City and County of San Francisco.

Marsha Jones Moutrie, City Attorney, Santa
Monica, California, By: Adam Radinsky, Deputy
City Attorney, Eda U. Suh, Deputy City Attorney,
for Defendant City of Santa Monica.

Office of the Comptroller of the of the Currency,
Washington, D.C., for Amicus Curiae.

BEFORE THE HONORABLE VAUGHN R.
WALKER, JUDGE.

{EXCERPT OF TRANSCRIPT} ORDER
GRANTING PRELIMINARY INJUNCTION

WALKER, J.

*1 THE COURT: THE PLAINTIFFS IN THESE
CASES ARE TWO NATIONALLY-CHARTERED
BANKS AND A CALIFORNIA BANK TRADE

ASSOCIATION. THE PLAINTIFFS
CHALLENGE TWO SIMILAR CITY
ORDINANCES FORBIDDING THE
ASSESSMENT OF FEES TO NONACCOUNT
HOLDERS USING BANK AUTOMATED
TELLER MACHINES.

ON OCTOBER 12, THE CITY COUNCIL IN
SANTA MONICA ADOPTED SECTION 4
.32.040 TO ITS MUNICIPAL CODE,
FORBIDDING BANK ATM'S FROM
CHARGING FEES FOR NONACCOUNT
HOLDERS USE OF ATM'S.

ON NOVEMBER 2, THE VOTERS IN THE
CITY AND COUNTY OF SAN FRANCISCO
PASSED A NEARLY IDENTICAL INITIATIVE,
PROPOSITION F, REQUIRING THE ADOPTION
OF THE SAME LAW INTO SAN FRANCISCO'S
MUNICIPAL CODE SECTION 648.1.

THESE ORDINANCES WERE ENACTED
WITH THE STATED GOALS OF PROTECTING
CONSUMERS AGAINST EXCESSIVE FEES
AND OF ENSURING COMPETITION AMONG
SMALLER BANKS AND CREDIT UNIONS.

ON NOVEMBER 3, PLAINTIFFS
COMMENCED THIS ACTION AGAINST THE
CITIES AND VARIOUS CITY OFFICIALS
ALLEGING THAT THE ORDINANCES AS
APPLIED TO NATIONALLY-CHARTERED
BANKS ARE PREEMPTED BY FEDERAL LAW
AND THAT THE DOCTRINE OF
SEVERABILITY PREVENTS ENFORCEMENT
OF THE ORDINANCES AGAINST STATE
CHARTERED BANKS ONCE THE
ORDINANCES ARE INVALIDATED AS TO
NATIONALLY-CHARTERED BANKS.

THE COURT GRANTED THE PLAINTIFFS'
MOTION FOR AN EXPEDITED HEARING ON
THEIR MOTION FOR PRELIMINARY
INJUNCTION. THE OFFICE OF THE
COMPTROLLER OF THE CURRENCY WAS
PERMITTED TO APPEAR AND HAS
APPEARED AS AMICUS CURIAE.

AS A PRELIMINARY MATTER, SANTA
MONICA ARGUES THAT IT IS
IMPERMISSIBLY JOINED IN THIS ACTION AS
A PARTY AND SHOULD BE SEVERED.
FEDERAL RULE OF CIVIL PROCEDURE 20

Not Reported in F.Supp.2d
(Cite as: 1999 WL 33429989 (N.D.Cal.))

GOVERNS PERMISSIVE JOINDER. SANTA MONICA SEEKS TO TRANSFER THE VENUE OF THE ACTION AGAINST IT TO THE CENTRAL DISTRICT OF CALIFORNIA. SANTA MONICA ARGUES THAT THE TWO ORDINANCES WERE SEPARATELY ENACTED AND THUS NOT PART OF THE SAME TRANSACTION OR OCCURRENCE.

THE TWO ORDINANCES UNDER CHALLENGE ARE SUBSTANTIALLY IDENTICAL AND ARE BEING CHALLENGED ON THE SAME LEGAL GROUNDS; THE CASE THUS POSES BASICALLY THE SAME QUESTION OF LAW FOR BOTH DEFENDANTS.

THE ENACTMENT OF THE TWO ORDINANCES WOULD APPEAR TO BE PART OF A SERIES OF LOCAL ENACTMENTS DESIGNED TO REGULATE OR PROHIBIT ATM FEES CHARGED BY THE OWNERS OR OPERATORS OF AT LEAST SOME ATMS. IN FACT, THE MEMORANDUM OF THE SANTA MONICA CITY ATTORNEY, DATED OCTOBER 5, 1999, ATTACHED AS EXHIBIT E TO SANTA MONICA'S MEMORANDUM, MAKES REFERENCE TO THE FACT THAT SEVERAL CALIFORNIA CITIES ARE CONSIDERING A BAN ON ATM SURCHARGES AND SPECIFICALLY REFERENCES THE SAN FRANCISCO PROPOSITION F WHICH IS CHALLENGED HERE IN THIS ACTION.

CONSIDERATION OF THE CHALLENGES TO THE ORDINANCES IN ONE ACTION WILL SERVE THE INTERESTS OF JUDICIAL ECONOMY AND CONSERVE THE PARTIES' RESOURCES. FURTHERMORE, THE DISPUTE INVOLVES PURELY LEGAL DETERMINATIONS. THERE ARE NO FACTUAL DISPUTES. IT IS UNLIKELY THAT THIS COURT'S RULING ON THIS MATTER WILL BE THE LAST JUDICIAL WORD ON THE SUBJECT AND CONSIDERATION OF THE PRESENT CHALLENGES WILL SIMPLY EXPEDITE PROMPT AND ORDERLY APPELLATE REVIEW OF THE SUBJECT. THERE IS MUCH TO BE GAINED BY ADJUDICATING THE TWO ORDINANCES IN ONE PROCEEDING.

*2 RULE 20 PERMITS JOINDER WHEN THE EVENT STEMS FROM THE SAME SERIES OF TRANSACTIONS OR OCCURRENCES AND WHEN THERE IS ANY QUESTION OF LAW OR FACT COMMON TO ALL DEFENDANTS. THE STANDARD OF RULE 20 HAS THEREFORE BEEN MET, AND SANTA MONICA'S MOTION UNDER RULE 20 IS DENIED.

NOW THE CHALLENGED ORDINANCES PROHIBIT THE CHARGING OF FEES FOR ATM SERVICES BY FINANCIAL INSTITUTIONS. OTHER INSTITUTIONS ARE NOT REGULATED BY THESE ORDINANCES AND PRESUMABLY CAN CONTINUE TO CHARGE FEES TO THEIR USERS.

THE ORDINANCES PROHIBIT ONLY ONE CLASS OF ATM CHARGES -- SURCHARGES LEVIED AGAINST NONACCOUNT HOLDER USERS OF THE MACHINES BY THE FINANCIAL INSTITUTION WHICH OPERATES THE MACHINE. FOREIGN FEES, THAT IS, CHARGES LEVIED BY AN ATM USER'S OWN BANK FOR USING ANOTHER BANK'S ATM REMAIN LAWFUL UNDER THE ORDINANCES. FURTHERMORE, BANK ATM OPERATORS ARE STILL PERMITTED TO CHARGE THE NONACCOUNT HOLDER'S BANK AN INTERCHANGE FEE FOR PROCESSING THE TRANSACTION. THE CHALLENGED LAWS ARE ENFORCEABLE BY PRIVATE RIGHTS OF ACTION AGAINST THE BANKS AND ANY INDIVIDUAL WHO IS CHARGED A FEE IN VIOLATION OF THE ORDINANCES MAY BRING SUCH A CIVIL ACTION.

SANTA MONICA'S ORDINANCE CONTAINS A SEVERABILITY CLAUSE; SAN FRANCISCO'S ORDINANCE DOES NOT. SANTA MONICA'S ORDINANCE BECAME EFFECTIVE ON NOVEMBER 11, SAN FRANCISCO'S ORDINANCE HAS NOT YET TAKEN EFFECT, BUT IS EXPECTED TO BECOME EFFECTIVE IN EARLY DECEMBER.

TO PREVAIL ON A MOTION FOR PRELIMINARY INJUNCTION, THE MOVING PARTY MUST SATISFY ONE OF TWO TESTS AVAILABLE IN THIS CIRCUIT. UNDER THE TRADITIONAL TEST, THE MOVING PARTY

Not Reported in F.Supp.2d
(Cite as: 1999 WL 33429989 (N.D.Cal.))

MUST DEMONSTRATE ONE. IRREPARABLE INJURY IF THE RELIEF IS DENIED, TWO. PROBABILITY OF SUCCESS ON THE MERITS, THREE, A BALANCE OF POTENTIAL HARM THAT FAVORS THE MOVING PARTY, AND FOUR, PUBLIC INTEREST THAT FAVORS THE INJUNCTION.

UNDER AN ALTERNATIVE TEST, THE MOVING PARTY CAN PREVAIL BY DEMONSTRATING EITHER, ONE, A COMBINATION OF PROBABLY SUCCESS ON THE MERITS AND THE POSSIBILITY OF IRREPARABLE INJURY IF THE RELIEF IS NOT GRANTED, OR TWO, THE EXISTENCE OF SERIOUS QUESTIONS GOING TO THE MERITS, AND A BALANCE OF HARDSHIPS THAT TIPS SHARPLY IN FAVOR OF THE MOVING PARTY. PLAINTIFFS APPEAR TO HAVE SATISFIED THE REQUIREMENTS UNDER BOTH STANDARDS.

THE ORDINANCES ARE LIKELY TO BE INVALIDATED AS PREEMPTED BY FEDERAL LAW AS APPLIED TO NATIONALLY-CHARTERED BANKS. NATIONALLY-CHARTERED BANKS SUCH AS PLAINTIFFS, BANK OF AMERICA AND WELLS FARGO, ARE HEAVILY REGULATED BY THE NATIONAL BANK ACT. THIS ACT AUTHORIZES NATIONALLY-CHARTERED BANKS TO EXERCISE ALL INCIDENTAL POWERS AS NECESSARY TO CARRY ON THE BUSINESS OF BANKING. THE PRIMARY REGULATOR OF BANKS CHARTERED UNDER THE ACT IS THE OFFICE OF THE COMPTROLLER OF THE CURRENCY. THAT OFFICE HAS THE DISCRETION TO AUTHORIZE ACTIVITIES BEYOND THOSE SPECIFICALLY ENUMERATED IN THE NATIONAL BANK ACT.

THE ORDINANCES IMPLICATE AN INCIDENTAL POWER ESSENTIAL TO THE BUSINESS OF BANKING. AN OFFICE OF THE COMPTROLLER OF THE CURRENCY REGULATION EXPRESSLY PERMITS ANY NATIONAL BANK TO CHARGE ITS CUSTOMERS NONINTEREST CHARGES AND FEES. THAT IS 12 CFR SECTION 7.4002(A).

*3 THE PROVISIONS OF THE NATIONAL BANK ACT STRONGLY SUGGEST THAT THE

ACT PREEMPTS THE FIELD OF REGULATION OF ATM USER FEES DISPLACING THE POWER OF THE MUNICIPAL DEFENDANTS TO SET FEES, OR AS WITH THE ORDINANCES UNDER REVIEW, TO PROHIBIT THE CHARGING OF THOSE FEES ALTOGETHER.

IN BANK ONE VERSUS GUTTAU, THE EIGHTH CIRCUIT COURT OF APPEALS REVERSED A DISTRICT COURT'S DENIAL OF A PRELIMINARY INJUNCTION SOUGHT BY A NATIONALLY-CHARTERED BANK TO PREVENT ENFORCEMENT OF AN IOWA STATUTE GOVERNING ATM'S IN THAT STATE. THE IOWA STATUTE PROHIBITED OWNERSHIP OF ATM BY OUT-OF-STATE FINANCIAL INSTITUTIONS AND IMPOSED CERTAIN OTHER SO-CALLED CONSUMER PROTECTION MEASURES REGULATING ADVERTISING AND HOURS OF OPERATION OF ATM'S.

THE COURT OF APPEALS NOTED THAT THE NATIONAL BANKING ACT GRANTS TO NATIONAL BANKS "ALL SUCH INCIDENTAL POWERS AS MAY BE NECESSARY TO CARRY ON THE BUSINESS OF BANKING," QUOTING FROM TITLE 12 UNITED STATES CODE SECTION 24(SEVENTH).

THE SUPREME COURT HAS OBSERVED THAT THE GRANT OF BOTH ENUMERATED AND INCIDENTAL POWERS ORDINARILY PREEMPT CONTRARY STATE LAW. STATE LAW WHICH STANDS AS OBSTACLE TO ACCOMPLISHMENT AND EXECUTION OF SUCH CONGRESSIONAL INTENT MAY BE FOUND PREEMPTED. THE EIGHTH CIRCUIT OBSERVED THAT THE 1996 AMENDMENTS TO THE NATIONAL BANK ACT MAKE CLEAR THAT ATM'S ARE NOT SUBJECT TO STATE REGULATIONS DEALING WITH BRANCHING AND LIKE MATTERS AND THUS WHATEVER REGULATORY AUTHORITY THE STATES RETAIN WITH RESPECT TO NATIONAL BANK BRANCHES, THE 1996 AMENDMENT CLEARLY EXPRESSES CONGRESS' INTENT THAT THAT AUTHORITY NO LONGER EXTENDS TO NATIONAL BANK ATM'S.

THE SUPREME COURT HAS MADE CLEAR

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THAT INTERPRETATIONS OF THE NATIONAL BANK ACT BY THE COMPTROLLER OF THE CURRENCY ARE ENTITLED TO GREAT WEIGHT. IN THIS CASE THE COMPTROLLER OF THE CURRENCY HAS MADE ABUNDANTLY CLEAR THAT HE CONSIDERS THE ORDINANCES AT BAR TO BE PREEMPTED BY THE NATIONAL BANK ACT.

THE MUNICIPAL DEFENDANTS IN THIS CASE REPEAT THE CONTENTION OF THE IOWA SUPERINTENDENT OF BANKING IN THE BANK ONE CASE THAT THE FEDERAL ELECTRONIC FUNDS TRANSFER ACT, NOT THE NATIONAL BANK ACT APPLIES, AND THAT STATE REGULATION OR PROHIBITION OF ATM FEES IS PERMISSIBLE UNDER THE ANTIPREEMPTION PROVISION OF THE ELECTRONIC FUNDS TRANSFER ACT.

DEFENDANTS' CONTENTION THAT THE ELECTRONIC FUNDS TRANSFER ACT TRUMPS THE NATIONAL BANK ACT IS PREDICATED ON THE ARGUMENT THAT THE ELECTRONIC FUNDS TRANSFER ACT IS THE MORE SPECIFIC OF THE TWO ENACTMENTS AND THE MORE RECENT, AND, THEREFORE, TAKES PRIORITY. THE EIGHTH CIRCUIT MADE SHORT SHRIFT OF THAT ARGUMENT IN BANK ONE, NOTING THAT THE ANTIPREEMPTION PROVISION OF THE EFTA IS SPECIFICALLY LIMITED TO THE PROVISIONS OF THE EFTA DOES NOT EXTEND TO ANY OTHER FEDERAL STATUTE AND DOES NOT GRANT THE STATES OR MUNICIPALITIES ANY ADDITIONAL AUTHORITY TO REGULATE NATIONAL BANKS THAT THE STATES WOULD OTHERWISE NOT POSSESS.

FURTHERMORE, EVEN IF THE EFTA SUPPLIED THE APPLICABLE FEDERAL LAW, IT IS DOUBTFUL THAT ATM FEE REGULATION OR PROHIBITION OF THE ORDINANCES AT BAR IS PERMISSIBLE UNDER THAT STATUTE. THAT SORT OF CONSUMER PROTECTION MEASURES OR THE KIND OF CONSUMER PROTECTION MEASURES THAT THE EFTA APPEARS TO CONTEMPLATE FOR THE STATES AND LOCALITIES RELATE TO ATM USER

SAFETY. SUCH AS LOCATION, INSTALLATION AND LIGHTING OF ATM AND, POSSIBLY, DISCLOSURE OF FEES AND OTHER TERMS AND CONDITIONS OF ELECTRONIC TRANSFERS. ATM FEE REGULATION OR PROHIBITION GOES TO THE ABILITY OF A NATIONAL BANK TO INSTALL AND OPERATE ATM'S AND CANNOT UNDER ANY REASONABLE STRETCH BE CONSIDERED A MEASURE NECESSARY TO PROTECT CONSUMERS. MOST LIKELY, STATE AND LOCAL ATM FEE REGULATION OR PROHIBITION WOULD DISCOURAGE OR IMPAIR THE PROVISION OF ATM SERVICES TO CONSUMERS, RATHER THAN FOSTER THE PROVISION OF SUCH SERVICES TO CONSUMERS.

*4 THESE AUTHORITIES ESTABLISH BEYOND QUESTION THAT THERE IS A SERIOUS QUESTION WHETHER THE ORDINANCES AT BAR ARE PREEMPTED BY FEDERAL LAW. INDEED, THE LAW IS SUFFICIENTLY CLEAR THAT IT WOULD APPEAR THAT PLAINTIFFS HAVE NOT MERELY RAISED SERIOUS QUESTIONS ABOUT THE VALIDITY OF THE ORDINANCES AT BAR, BUT HAVE IN FACT SATISFIED THE ALTERNATIVE ARTICULATION OF THE PRELIMINARY INJUNCTION TEST BY SHOWING A LIKELIHOOD OF SUCCESS ON THE MERITS.

IT IS ALSO CLEAR THAT THE PLAINTIFFS, HAVING RAISED SERIOUS QUESTIONS AS TO THE VALIDITY OF THE ORDINANCES, THE PLAINTIFFS ARE ENTITLED TO AN INJUNCTION IF THE BALANCE OF HARSHIPS TIP STRONGLY IN THEIR FAVOR.

ENFORCEMENT OF THE ORDINANCES PENDING RESOLUTION OF THE DISPUTE WOULD CAUSE PLAINTIFFS GREAT HARM BECAUSE THEY WILL NOT BE ABLE TO RECOVER THE FEES LOST DURING THE PERIOD OF THE INJUNCTION IF THEY ULTIMATELY PREVAIL ON THE MERITS. PLAINTIFFS WILL EITHER REPROGRAM THEIR ATM'S TO PROHIBIT WITHDRAWALS BY NONACCOUNT HOLDERS, AS HAS ALREADY BEEN DONE BY WELLS FARGO AND BANK OF AMERICA IN SANTA

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MONICA, OR WILL SIMPLY STOP CHARGING
NONACCOUNT HOLDERS THE FEES.

IN EITHER CASE, THOUSANDS OF DOLLARS
OF REVENUE WILL BE LOST EACH MONTH.
AND PLAINTIFFS HAVE NO FEASIBLE
MEANS OF LATER RECOVERING FEES FROM
INDIVIDUALS WHO USE THE MACHINES
WITHOUT PAYING THESE FEES. THERE IS
NO QUESTION THAT SUCH HARM IS
SIGNIFICANT.

THE CITIES CONTEND THAT THEY WILL
SUFFER HARDSHIP IN NOT EXECUTING
THEIR LAWS AND ENFORCING THE WILL OF
THE PEOPLE EITHER DIRECTLY OR
THROUGH THEIR ELECTED
REPRESENTATIVES. ADDITIONALLY,
RESIDENTS AND VISITORS TO THESE TWO
CITIES WILL, ACCORDING TO THE CITY,
SUFFER THE HARDSHIP OF PAYING
UNLAWFUL FEES IF THE ORDINANCES ARE
ENJOINED AND THEN ULTIMATELY
UPHELD.

HOWEVER, THE HARM THAT IS POINTED
TO BY THE CITIES CAN BE AVOIDED BY
REQUIRING THE BANKS TO ESCROW THE
FEES COLLECTED PENDING THE OUTCOME
OF THE DISPUTE. THE BANKS ARE
CAPABLE OF LATER REFUNDING THE FEES
TO THE ATM CUSTOMERS IF THE CITIES
EVENTUALLY PREVAIL. WHILE BOTH
PARTIES AGREE THAT SOME INDIVIDUALS
MAY NEVER BE LOCATED, THE BANKS'
SUGGESTION THAT THEY COULD DONATE
EXCESS FEES TO SOME FORM OF
CONSUMER FRAUD DETECTION
DEPARTMENT OF THE CITIES IS A
SATISFACTORY SOLUTION TO ANY
UNCLAIMED FEES THAT MAY BE LEFT
OVER.

THESE FACTS ESTABLISH THAT THE
BALANCE OF HARDSHIPS TIPS SHARPLY IN
PLAINTIFFS' FAVOR. THE PLAINTIFFS HAVE
THUS ESTABLISHED THAT A PRELIMINARY
INJUNCTION SHOULD ISSUE IN THEIR
FAVOR UNDER THE ALTERNATIVE TEST.
FURTHERMORE, THE IRREPARABLE INJURY
WHICH THE PLAINTIFFS HAVE
DEMONSTRATED FURNISHES THE FIRST
AND THIRD GROUNDS OF THE

TRADITIONAL FOUR-PART TEST FOR A
PRELIMINARY INJUNCTION. WITH RESPECT
TO THE PROBABILITY OF PLAINTIFFS'
SUCCESS ON THE MERITS AND THE PUBLIC
INTEREST FACTOR, PLAINTIFFS TOO HAVE
DEMONSTRATED THE EXISTENCE OF
THESE FACTORS. ALTHOUGH THERE IS
RELATIVELY LITTLE CASE LAW, THE
EIGHTH CIRCUIT DECISION IN BANK ONE
COGENTLY REASONED AND LIKELY TO BE
FOLLOWED BY THE OTHER CIRCUITS.
FURTHER, THE SUPREME COURT HAS
COUNSELED THE COURTS SHOULD PAY
HEED TO THE POSITION OF THE OFFICE OF
THE COMPTROLLER OF THE CURRENCY IN
SUCH MATTERS.

*5 THE PARTIES DISAGREE ABOUT
WHETHER THE INJUNCTION SHOULD
APPLY TO ALL BANKS OR TO ONLY
NATIONAL BANKS. IF THE LAW ARE
PREEMPTED, THEY ARE ONLY PREEMPTED
AS TO NATIONAL BANKS. SO THE ISSUE IS
WHETHER THE ORDINANCES SHOULD BE
SEVERED SO AS TO EXEMPT NATIONAL
BANKS AND REMAIN EFFECTIVE AGAINST
STATE CHARTERED BANKS. TO APPLY THE
SEVERABILITY DOCTRINE, THE
CONTESTED PROVISION MUST BE
GRAMMATICALLY, FUNCTIONALLY, AND
VOLITIONALLY SEPARABLE FROM THE
REMAINING PORTION OF THE ORDINANCE.
THE CITIES ARGUE THAT THE PROVISIONS
ARE FUNCTIONALLY SEVERABLE: THE
LAWS COULD FUNCTION IN THE PROPOSED
SEVERED FORM. IF THE PURPOSE OF THE
ORDINANCES IS TO FOSTER COMPETITION,
SEVERANCE WILL MOST LIKELY DEFEAT
THIS PURPOSE. BANNING THE
SURCHARGES BY THE LARGER,
NATIONALLY-CHARTERED BANKS WAS
THE KEY TO THE PURPOSE UNDERLYING
THESE ORDINANCES.

BOTH ORDINANCES CLAIM TO BAR FEES
IMPOSED BY FINANCIAL INSTITUTIONS.
THE BANKS CONTEND THAT SINCE THE
TERM "FINANCIAL INSTITUTION" IS
DEFINED TO INCLUDE BOTH NATIONAL
AND STATE CHARTERED BANKS, THE
ORDINANCES ARE NOT GRAMMATICALLY
SEPARABLE. AN ENACTMENT PASSES THE
GRAMMATICAL TEST WHERE THE

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LANGUAGE OF THE STATUTE IS MECHANICALLY SEVERABLE, THAT IS, WHERE THE VALID AND INVALID PARTS CAN BE SEPARATED BY PARAGRAPH, SENTENCE, PHRASE, OR EVEN SINGLE WORDS. BUT THERE IS NO PARAGRAPH, SENTENCE, CLAUSE, PHRASE, OR WORD THAT COULD BE SEVERED FROM THE LANGUAGE OF THE ORDINANCES AT BAR THAT WOULD YIELD A LAW WHICH APPLIED ONLY TO ONE CLASS OF BANK.

SAN FRANCISCO ARGUES THAT THE ORDINANCE CAN BE GRAMMATICALLY SEVERED BY REDEFINING THE MEANING OF FINANCIAL INSTITUTIONS TO INCLUDE ONLY STATE CHARTERED BANKS. BUT FOR THE COURT TO SEVER IN THIS CASE WOULD ENTAIL A WHOLESAL INTRUSION BY THE COURT INTO THE LEGISLATIVE PROCESSES OF THE CITY AND COUNTY OF SAN FRANCISCO. AN INVITATION OF THE CITY ATTORNEY FOR THE COURT TO DO SO IS SURPRISING UNDER THESE CIRCUMSTANCES.

FURTHERMORE, THE VOLITIONAL SEVERABILITY TEST IS NOT MET HERE. THE STATED PURPOSE OF THE SANTA MONICA ORDINANCE IS TO PROVIDE A MEANS OF ENSURING THE VIABILITY OF SMALL BANKS. TO ENFORCE THIS LAW AGAINST ONLY THAT CLASS OF BANKS WOULD INDEED THWART THE STATED PURPOSE OF THE LAW. THEREFORE, DESPITE SANTA MONICA'S SEVERABILITY CLAUSE, THE COURT FINDS THE ORDINANCE IS NOT SEVERABLE IN THIS FASHION.

THE SAN FRANCISCO ORDINANCE, OF COURSE, WAS ENACTED VIA VOTER INITIATIVE. IT IS, THEREFORE, HARDER TO DETERMINE THE VOLITIONAL INTENT OF ADOPTING THIS LEGISLATION. CERTAINLY MANY VOTERS WERE MOST CERTAINLY MOTIVATED BY THEIR SELF- INTEREST IN NOT HAVING TO PAY AN ATM USAGE FEE. THE ORDINANCE WAS PLACED ON THE BALLOT BY THE SAN FRANCISCO BOARD OF SUPERVISORS. THE PREAMBLE OF THE SAN FRANCISCO ORDINANCE EXPRESSES THE SAME CONCERNS ABOUT THE

ANTICOMPETITIVE EFFECT OF ATM SURCHARGES. AND IT APPEARS THAT THESE CONCERNS MOTIVATED THE BOARD OF SUPERVISORS TO DRAFT THE ORDINANCE. REGARDLESS, SINCE THE STATE CHARTERED BANKS ARE NOT GRAMMATICALLY SEPARABLE FROM THE NATIONAL BANKS, THE INJUNCTION MUST APPLY TO BOTH.

*6 ACCORDINGLY, THE COURT GRANTS THE MOTION OF THE PLAINTIFFS. AND AS PART OF THE INJUNCTION, THE BANKS ARE REQUIRED TO ESCROW AND TO KEEP RECORDS ON ALL ATM NONACCOUNT HOLDER FEES COLLECTED DURING THE PERIOD OF THIS LITIGATION.

IN ADDITION, THE BANKS WILL BE REQUIRED TO POST BOND. AND MR. BRUCE, I AM INCLINED TO REQUIRE POSTING OF A BOND IN THE AMOUNT OF \$50,000, WHICH WOULD APPEAR TO COVER THE BASIC LITIGATION COSTS THAT ARE INVOLVED.

ARE YOUR CLIENTS PREPARED TO POST A BOND IN THAT AMOUNT?

MR. BRUCE: THEY ARE, YOUR HONOR.
THE COURT: VERY WELL.

THEN THAT WILL BE THE ORDER. IS THERE ANYTHING FURTHER?

MR. RADINSKY: EXCUSE ME, YOUR HONOR.

I KNOW MR. BERNHARD HAS SOMETHING AS WELL.

THE CITY FILED EVIDENTIARY OBJECTIONS TO THE THREE DECLARATIONS FILED WITH THE BANKS' PAPERS. AND WE ADDITIONALLY WANT TO OBJECT ON THE RECORD TODAY TO THE DECLARATION OF MR. LYTEN (PHONETIC) ON THE GROUNDS THAT IT IS HEARSAY, SPECULATION AND LACKS FOUNDATION.

THE COURT: NONE OF THE MATTERS TO WHICH OBJECTION WERE MADE WERE RELIED UPON BY THE COURT.
MR. RADINSKY: VERY WELL.

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ANOTHER MATTER IS THE SAVINGS AND LOAN INSTITUTIONS AND CREDIT UNIONS, FOR EXAMPLE, IN BOTH OF THESE CITIES WANT A CLARIFICATION FROM YOUR HONOR ABOUT YOUR ORDER, WHETHER IT WOULD APPLY TO ALL FINANCIAL INSTITUTIONS OR JUST TO BANKS PER SE.

THE COURT: I DON'T BELIEVE THAT YOU CAN SEVER THESE PROVISIONS. AND I THINK THAT--IS THAT NOT CLEAR?

MR. RADINSKY: YOUR HONOR MENTIONED THE TERM "BANKS". THIS APPLIES TO ALL FINANCIAL INSTITUTIONS?

THE COURT: I DON'T BELIEVE THAT UNDER THE CIRCUMSTANCES FOR THE REASONS THAT I INDICATED THAT YOU CAN SEVER ONE KIND OF FINANCIAL INSTITUTION FROM THE OTHERS.

MR. RADINSKY: VERY WELL.

DOES YOUR HONOR'S ORDER ABOUT THE FUNDS BEING PLACED IN ESCROW, DOES THAT APPLY TO EVERY FINANCIAL INSTITUTION IN BOTH CITIES?

THE COURT: IT APPLIES TO THE PARTIES.

MR. RADINSKY: WELL, YOUR HONOR, THERE ARE MANY OTHER FINANCIAL INSTITUTIONS WHICH UNDER--AS I UNDERSTAND YOUR HONOR'S RULING, WILL HAVE THE BENEFIT OF YOUR RULING.

THE COURT: WHAT I AM ENJOINING IS ANY ENFORCEMENT ACTIONS BY THE CITY AND COUNTY OF SAN FRANCISCO AND BY SANTA MONICA IN THE MEANTIME WITH RESPECT TO THE SECURITY THAT IS BEING POSTED AND WITH RESPECT TO THE ORDER WITH RESPECT TO ESCROWING, THAT CAN ONLY APPLY TO THE PARTIES THAT ARE BEFORE ME.

MR. RADINSKY: ALTHOUGH THE INJUNCTION GOES BEYOND.

THE COURT: THE INJUNCTION GOES BEYOND THAT. THAT IS CORRECT. NOW IF YOU WISH TO SEEK RELIEF WITH RESPECT TO OTHERS, YOU CAN CERTAINLY DO SO. BUT I AM NOT IN A POSITION TO ENJOIN PARTIES THAT ARE NOT BEFORE THE COURT.

MR. RADINSKY: VERY WELL.

AS TO THE BOND UNDER RULE 65. YOUR HONOR, I WOULD SUBMIT THAT THE AMOUNT OF \$50,000 APPARENTLY JUST FOCUSES ON THE LITIGATION COST TO THE CITY ATTORNEYS OFFICES RATHER THAN TO THE POTENTIAL HARM OF THE PUBLIC OF THESE TWO CITIES.

THE COURT: THERE IS NO HARM THAT THE CITY SUFFER IN THEIR OWN CAPACITY, AND IF THE FUNDS ARE ESCROWED DURING THE PENDENCY OF THE LITIGATION, THEN IF THE CITIES ULTIMATELY PREVAIL, THOSE FUNDS CAN BE REMITTED TO THE USERS OF FEES, SO THERE IS NO HARM TO THOSE USERS DURING THE PENDENCY OF THE LITIGATION.

*7 MR. RADINSKY: WE WOULD OBJECT FOR THE RECORD. YOUR HONOR, THAT THAT ORDER WOULD VIOLATE RULE 65 AS NOT PROVIDING A SUFFICIENTLY SAFE MECHANISM FOR ASSURING PROPER PAYMENT.

ALSO THAT THEIR EVIDENCE SUBMITTED WITH BASICALLY THIS PROMISE THAT THEY WILL DO THEIR BEST AND THAT THEY WILL KEEP TRACK OF ALL THESE FEES. THAT IS INSUFFICIENT UNDER RULE 65 AND THAT WE NEED A CHANCE TO CONDUCT INVESTIGATION AND DISCOVERY INTO THE TRUTH OF THE PROCEDURES--

THE COURT: I ASSUME THE CASE IS GOING TO GO ON.

MR. RADINSKY: VERY WELL.

THE COURT: ALL RIGHT.

MR. BRUCE?

MR. BRUCE: YOUR HONOR, THANK YOU VERY MUCH.

ANTICIPATING THAT YOU MIGHT WANT TO PUT INTO YOUR ORDER SOME SPECIFIC LANGUAGE ABOUT THE REFUND MECHANISMS. WE HAVE A PROPOSED ORDER TO TENDER FOR YOUR CONSIDERATION. PERHAPS YOU HAVE ALREADY WRITTEN YOURS. WE HAVE GIVEN IT TO THE OTHER SIDE THIS AFTERNOON. AS TO--

THE COURT: WHY DON'T YOU SUBMIT THAT, AND I WILL TAKE A LOOK AT IT.

MR. BRUCE: YES.

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HOW MANY COPIES WOULD YOU LIKE?
THE COURT: HOW ABOUT THREE.
MR. BRUCE: THREE. HERE ARE THREE COPIES.

(DOCUMENTS HANDED TO COURT.)
MR. BRUCE: AS TO THE FORM OF THE INJUNCTION ORDER, OUR MOTION PAPERS AND PROPOSED ORDER WERE VERY SPECIFIC, AND THEY WERE SPECIFIC FOR A VERY SPECIFIC REASON.

THE ONLY WAY THAT ANY OF THE BANKS ARE PROTECTED BY YOUR HONOR'S ORDER IS TO ENSURE THAT THE ORDINANCES ARE NOT ALLOWED IN SANTA MONICA'S CASE TO REMAIN EFFECTIVE DURING THE COURSE OF LITIGATION, AND IN SAN FRANCISCO'S CASE, TO ENSURE THAT THE BOARD OF SUPERVISORS, WHICH HAS THE LAST MINISTERIAL ACT IN THE PROCESSES, NOT ALLOW TO APPROVE THE INITIATIVE AND SEND OUT, IF YOU WILL, INTO THE LAW OF SAN FRANCISCO. AN INJUNCTION THAT JUST OPERATED AGAINST THE ENFORCEMENT OF THE CITIES AND NOTHING MORE WOULD LEAVE U.S. EXPOSED TO THOUSANDS AND THOUSANDS OF LAWSUITS IN STATE COURT BY INDIVIDUALS WHO CAN GRAB THESE ENFORCEMENT MECHANISMS. SO I JUST FOCUS YOUR HONOR AGAIN ON THE--

THE COURT: I UNDERSTAND THAT. LET'S DEAL WITH THAT SITUATION, IF WE ENCOUNTER IT. I SAID LET'S DEAL WITH THAT SITUATION IF WE ENCOUNTER IT.

I THINK THE--I WILL TRUST THAT THE CITIES ARE NOT GOING TO TAKE ANY MEASURES TO ENFORCE THE ORDINANCE DURING THE PENDENCY OF THE PRELIMINARY INJUNCTION, AND WE'LL DEAL WITH ANY CIVIL ACTIONS THAT ARE BROUGHT DURING THE PENDENCY OF THE CASE IF THERE ARE ANY TO DEAL WITH.

MR. BRUCE: YOUR HONOR, IF I MAY BE HEARD ON THAT BECAUSE IT IS REALLY QUITE IMPORTANT.

AS TO SANTA MONICA, AS YOU KNOW, THEIRS BECAME EFFECTIVE ON NOVEMBER 11. AND UNLESS THIS COURT ORDERS THAT IT BE SUSPENDED PENDING

THE MERITS, AS WE ASK THE COURT TO DO, AND THAT IS JUST A MAINTENANCE OF THE STATUS QUO AT THE TIME OF THE SUIT, IT WOULD BE--OUR CLIENTS WOULD BE EXPOSED TO PUNITIVE DAMAGES OF 5,000 PER TRANSACTION AND SO-CALLED ACTUAL DAMAGES OF \$250 PER TRANSACTION IN SUITS THAT WOULD BE FILED IN STATE COURT BY INDIVIDUAL CITIZENS OF SANTA MONICA, OR FOR THAT MATTER, TOURISTS IN SANTA MONICA, AND THE SAME WOULD APPLY TO SAN FRANCISCO.

*8 THIS COURT WOULD THEN HAVE TO REACH OUT AND ENJOIN ALL OF THESE INDIVIDUALS WHO ARE--WHO WOULD FILE THESE LAWSUITS IN STATE COURT, OR EVEN MORE DRAMATICALLY, IF YOU WILL, WOULD HAVE TO SOMEHOW ENJOIN THE SMALL CLAIMS COURTS OF THE STATE OF CALIFORNIA FROM ENTERTAINING THESE SUITS. ABSENT THAT KIND OF INJUNCTIVE RELIEF, THE BANKS WOULD BE EXPOSED TO POTENTIALLY ENORMOUS LIABILITIES IF THEY DON'T COMPLY WITH THE ORDINANCES.

THE COURT: WELL--

MR. BRUCE: THAT IS WHY WE WERE SO CAREFUL TO ASK--

THE COURT: IT IS DIFFERENT, IS IT NOT, IN SAN FRANCISCO BECAUSE THE ORDINANCE HAS NOT BECOME EFFECTIVE?

MR. BRUCE: YES. SO LONG AS THE COURT IS CRYSTAL CLEAR ON THIS, THAT THERE IS AN INJUNCTION AGAINST THE CITY OF SAN FRANCISCO FROM ALLOWING THE ORDINANCE TO BECOME EFFECTIVE, THEN THAT IS FINE. BECAUSE WITH THAT INJUNCTION, THAT LAW WILL NEVER BE THERE FOR ANYONE TO INVOKE BECAUSE THE BOARD OF SUPERVISORS WILL NOT BE ABLE TO TAKE THAT LAST ACT.

AS TO SANTA MONICA--

THE COURT: LETS ASK MR. BERNHARD, IS THAT CLEAR?

MR. BERNHARD: THAT'S MY UNDERSTANDING OF THE COURTS ORDER.

THE COURT: VERY WELL.

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MR. BRUCE: THAT'S FINE.

AS TO SANTA MONICA, I'M AFRAID WE WOULD BE LEFT IN THE POSTURE OF REALLY AS A PRACTICAL MATTER HAVING TO COMPLY WITH IT DURING THE COURSE OF THE LITIGATION. IF THAT'S YOUR HONOR'S CHOICE. THEN, OF COURSE, THAT IS WITHIN YOUR DISCRETION IN SHAPING EQUITABLE RELIEF ON A PRELIMINARY BASIS.

BUT IT IS ALSO WITHIN YOUR HONOR'S POWER UNDER THE TANNER CASE. FOR EXAMPLE, AND OTHER CASES OF THE NINTH CIRCUIT THAT WE DIDN'T BRIEF BECAUSE THE ISSUE REALLY WASN'T RAISED BY THE OTHER SIDE, IT IS WITHIN YOUR HONOR'S POWER, PARTICULARLY IN A CASE OF CONSTITUTIONAL DIMENSION, WHICH THIS IS, TO RESTORE THE STATUS QUO BY ORDERING SANTA MONICA TO SUSPEND THE ORDINANCE. THEN YOU WOULD HAVE SOME KIND OF ACTION BY THE SANTA MONICA GOVERNMENT THAT WOULD SUSPEND THE ORDINANCE.

WITH THAT ORDER FROM THIS COURT DIRECTLY TO SANTA MONICA, NO SANTA MONICA CITIZEN COULD GO INTO THE STATE COURT AND START THESE LAWSUITS. SO I JUST WANTED TO DISCUSS--

THE COURT: LET'S HEAR MR. RADINSKY ON THIS.

MR. RADINSKY: THERE IS A PROBLEM HERE, YOUR HONOR. HE REFERS TO THE STATUS QUO. THE STATUS QUO IS THAT SINCE THEY WAITED MORE THAN THREE WEEKS TO FILE THEIR LAWSUIT AGAINST SANTA MONICA, THIS LAW WAS ALREADY ON THE BOOKS, AND ONLY A MATTER OF DAYS BEFORE IT BECAME EFFECTIVE.

AS YOU RECOGNIZED IN OUR LAST HEARING, THE CITY ATTORNEY'S OFFICE DOESN'T HAVE THE AUTHORITY TO UNDO A LEGISLATIVE ACT THAT HAS ALREADY SEEN ITS FINAL STEP. THAT LAW IS IN EFFECT, AND THEY CHOSE TO WAIT, SO THE STATUS QUO HERE IS THAT THE SURCHARGE BAN IS IN EFFECT IN SANTA

MONICA. AND HE IS ASKING FOR A CHANGE TO THE STATUS QUO.

I DON'T KNOW THERE IS A MECHANISM TO DO THAT. AS WE DISCUSSED LAST TIME, I DON'T HAVE THE AUTHORITY ON BEHALF OF MY OFFICE TO NULLIFY A LAW THAT OUR ELECTED REPRESENTATIVES HAVE PASSED WHICH HAS GONE PASSED ITS LAST STAGE.

*9 NOW, I UNDERSTAND YOU TO BE ENJOINING OUR OFFICE, FOR EXAMPLE, FROM PROSECUTING VIOLATIONS OR THE CITY FROM TAKING ANY AFFIRMATIVE STEPS TO ENFORCE THIS LAW, BUT THAT IS A FAR CRY FROM UNDOING THE LEGISLATIVE WILL THAT HAS ALREADY PASSED ITS FINAL HURDLE. AND I WOULD SUBMIT THAT'S EXTRAORDINARY RELIEF THEY'RE SEEKING, AND IT WOULD UPSET THE STATUS QUO.

MR. BRUCE: MAY I RESPOND?

THE COURT: YES.

MR. BRUCE: YOUR HONOR, THE WAY SANTA MONICA DID THIS, AND THERE IS NOTHING WRONG WITH WHAT SANTA MONICA DID PROCEDURALLY, AS I UNDERSTAND IT, AND I AM NOT A CALIFORNIAN. IT IS THE WAY MOST MUNICIPAL LAW WORKS. THAT THE CITY COUNCIL HAS A FIRST READING OF A PROPOSED MEASURE. AND THEY TAKE A VOTE ON IT.

THEY DID THAT A WEEK BEFORE OCTOBER THE 12TH. THEN, IN A WEEK PERIOD, THEY HAD A SECOND READING, AND IT WAS APPROVED FOUR TO THREE.

UNDER CALIFORNIA LAW, THAT IS THE LAST ACT. THERE IS NOTHING LEFT IN PROCESS. SO THAT 30 DAYS LATER, IT AUTOMATICALLY BECAME EFFECTIVE. UNLESS, UNLESS THERE WAS AN ORDER TO THE CITY COUNCIL ITSELF TO AN EFFECT RESCIND WHAT IT DID.

NOW, I MADE A JUDGMENT THAT WE WOULD NOT COME TO THIS COURT FOR A TEMPORARY RESTRAINING ORDER TO PREVENT THE CITY, TO PREVENT THE SANTA MONICA ORDINANCE FROM

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BECOMING EFFECTIVE BECAUSE A TEMPORARY RESTRAINING ORDER WOULD HAVE HAD TO HAVE AN AFFIRMATIVE RELIEF ELEMENT IN IT. AND I MADE THE JUDGMENT, IT MIGHT HAVE BEEN WRONG. THAT THIS COURT WOULD HAVE--YOU DO HAVE THE AUTHORITY ON THE PRELIMINARY INJUNCTION TO GIVE THAT AFFIRMATIVE RELIEF AND THERE WOULD BE A SHORT PERIOD OF TIME BETWEEN THE 11TH OF NOVEMBER AND TODAY'S THE 15TH, FOUR DAYS THERE WOULD HAVE TO BE COMPLIANCE, BUT THAT THE COURT DOES HAVE THE AUTHORITY TO ASK OR DIRECT THE CITY COUNCIL, OR THE CITY OF SANTA MONICA TO SUSPEND ITS ORDINANCE.

THE STATUS QUO IS, AND THIS IS THE TANNER CASE, 316 F.2D, 804 AT 808. 1963 DECISION OF THE NINTH CIRCUIT, THE STATUS QUO IS THE LAST UNCONTESTED STATUS THAT PRECEDED THE CONTROVERSY. OF COURSE, WE FILED OUR LAWSUIT. I FORGET HOW MANY DAYS, BUT SUBSTANTIALLY BEFORE THE EFFECTIVE DATE.

THIS COURT HAS FULL POWER, ESPECIALLY ON A CASE OF CONSTITUTIONAL DIMENSIONS, TO DIRECT THE CITY OF SANTA MONICA NOT TO RESCIND FOREVER BUT TO SUSPEND THE ORDINANCE DURING THE PERIOD OF THE PRELIMINARY INJUNCTION. IF THE COURT DOES THAT, THEN IT TOO WILL BE IN THE SAME POSTURE AS SAN FRANCISCO.

IF THE COURT DOESN'T DO THAT, THEN THE SANTA MONICA ORDINANCE FOR ALL PRACTICAL PURPOSES, WILL HAVE TO BE REGARDED BY THE BANKS AS IN EFFECT BECAUSE THEY COULDN'T STAND THE PROSPECT OF THAT \$5,000 PUNITIVE DAMAGES AND 250 PER TRANSACTION.

MR. RADINSKY: MAY I BE HEARD BRIEFLY, YOUR HONOR, ON WHAT HE RAISED.

AT THE LAST HEARING, COUNSEL FOR THE BANKS SPECIFICALLY SAID WHEN YOU ADDRESSED WHY THE DELAY ON SANTA MONICA, THEY SAID THAT THEY WOULD

QUOTE TAKE THEIR "LUMPS" UNQUOTE IN SANTA MONICA. AND ALSO REFERRED TO SANTA MONICA AS THE TAIL WAGGING THE DOG IN THIS CASE.

WHAT THEY WERE SAYING WAS THEY'RE REALLY NOT TOO CONCERNED ABOUT SANTA MONICA. THEY COULD HAVE FILED A LAWSUIT ALMOST A MONTH BEFORE THEY DID WHEN THE FIRST VOTE HAPPENED ON OCTOBER 5TH. THEY CHOSE NOT TO. THEY MADE A TACTICAL DECISION THAT WHEN THERE WAS STILL TIME FOR THE CITY COUNCIL TO TAKE ITS FINAL ACT, THEY COULD HAVE COME UP HERE OR MORE APPROPRIATELY DOWN THERE, WHICH IS WHERE WE ARE SUPPOSED TO BE, AND SOUGHT EMERGENCY RELIEF BEFORE THE FINAL ACT WAS TAKEN. THEY CHOSE NOT TO DO THAT. THEY CHOSE TO TAKE THEIR LUMPS AS MR. DARWIN SAID, AND THIS IS AN EXAMPLE OF THAT.

*10 YOUR HONOR, IF YOU DO WHAT HE IS ASKING, YOU WOULD BE UNDONG A LEGISLATIVE ACT THAT HAS ALREADY BEEN DONE.

THE COURT: LETS BOTH BE PRACTICAL AND ALSO LETS TAKE A LOOK AT THE LAW. I AM GOING TO ASK MR. BRUCE AND HIS COLLEAGUES TO PUT TOGETHER A BRIEF MEMORANDUM ON THIS SUBJECT INFORMING ME OF THAT TANNER CASE THAT YOU REFERRED TO AND ANY OTHER AUTHORITIES THAT YOU BELIEVE ARE APPLICABLE. AND GIVE MR. RADINSKY AN OPPORTUNITY TO RESPOND.

AND ALSO TO BE PRACTICAL ABOUT IT, IT MAKES A GREAT DEAL OF SENSE TO PLACE BOTH DEFENDANTS ON THE SAME POSTURE IN TERMS OF THE ENFORCEMENT OF THE ORDINANCE, AND ALSO TO HAVE THE SITUATION IN BOTH CITIES THE SAME.

SO, I MUST SAY I AM INCLINED TO GRANT RELIEF WHICH WOULD ACCOMPLISH THAT. BUT I WILL BE GUIDED BY WHATEVER ADDITIONAL GUIDANCE YOU CAN GIVE ME IN A MEMORANDUM.

Not Reported in F.Supp.2d
(Cite as: 1999 WL 33429989 (N.D.Cal.))

HOW LONG WOULD YOU NEED TO PREPARE THAT MEMORANDUM?

MR. BRUCE: WELL, I WOULD LIKE AT LEAST UNTIL, TODAY IS MONDAY. COULD WE HAVE UNTIL WEDNESDAY. YOUR HONOR?

THE COURT: THAT WOULD BE FINE.

MR. RADINSKY, CAN YOU GET IN A RESPONSE BY NEXT MONDAY?

THAT WILL BE ONE WEEK FROM TODAY.

MR. RADINSKY: YES, YOUR HONOR, WE CAN DO THAT.

THE COURT: ALL RIGHT. AS I UNDERSTAND IT, THE BANKS ARE NOT CHARGING FEES IN SANTA MONICA AT THE PRESENT TIME?

MR. BRUCE: THE BANKS ARE COMPLYING WITH THE--

THE COURT: SO, THAT CAN CONTINUE FOR ANOTHER WEEK, AT LEAST ANOTHER WEEK UNTIL WE SEE WHAT THE LAW IS--

MR. RADINSKY: CAN I HAVE A WEEK AFTER THEIR BRIEF? WE HAVE BEEN DOING EVERYTHING SO RUSHED, I'M GETTING USED TO IT, BUT WE WOULD LIKE--

THE COURT: THIS IS A NARROW POINT, MR. RADINSKY. IT IS A NARROW POINT AND WE OUGHT TO SETTLE THE TERMS OF THE INJUNCTION AS SOON AS POSSIBLE.

MR. BRUCE: THANK YOU, YOUR HONOR.

THE COURT: ALL RIGHT? ANYTHING FURTHER?

MR. BERNHARD: THERE IS, YOUR HONOR, VERY BRIEFLY.

FIRST--TWO THINGS. FIRST THE PROPOSED ORDER THAT PLAINTIFFS HAVE SUBMITTED. THIS ORDER DOESN'T APPEAR TO INCLUDE THE CALIFORNIA BANKING ASSOCIATION, VERY ACTIVE PLAINTIFFS AND PARTICIPANTS IN THIS LITIGATION.

AS THE COURT ALREADY NOTED, IT ONLY IMPOSED OBLIGATIONS ON THE PARTIES BEFORE IT AND CBA IS BEFORE YOU. THIS ORDER--I AM REFERRING SPECIFICALLY TO PAGE 3, ITEM 3 ABOUT THE ESCROW AND THE FUNDS, THAT SHOULD APPLY TO THE

CALIFORNIA BANK ASSOCIATION AS WELL.

THE COURT: I DON'T KNOW THAT THE--DOES THE BANK ASSOCIATION--

MR. BERNHARD: THEY ARE IN THIS COURT. THEY SAY, BECAUSE THEY HAVE OVER 280--

THE COURT: I UNDERSTAND. BUT THEY ARE NOT A DEPOSITORY INSTITUTION, ARE THEY?

MR. BERNHARD: THEY REPRESENT 280 MEMBERS.

THE COURT: MR. KASS?

MR. KASS: AS YOUR HONOR POINTS OUT, WE ARE HERE ON A REPRESENTATIONAL CAPACITY ONLY, AND THE VARIOUS MEMBER BANKS ARE NOT THE PARTIES TO THIS AS YOUR HONOR MENTIONED EARLIER.

IT WOULD BE DIFFICULT TO--I DON'T SEE HOW WE CAN MAKE THEM SUBJECT TO THAT PROVISION. SO I DON'T--THAT BEING SAID, I DON'T SEE THAT THERE IS GOING TO BE ANY PROBLEM WITH THEM DOING EXACTLY WHAT THE BANKS THAT ARE PARTIES TO THIS ACTION ARE DOING, WHICH IS THE RESPONSIBLE THING TO DO.

*11 THE COURT: LET'S SEE IF WE CAN AVOID THE PROBLEM. ARE YOU IN A POSITION ON BEHALF OF YOUR MEMBERS TO REPRESENT THAT THEY WILL FOLLOW THE SAME ESCROW PROCEDURES AS BANK OF AMERICA AND WELLS FARGO?

MR. KASS: WHAT I AM IN A POSITION TO REPRESENT AT THIS POINT IS THAT I THINK IT WOULD BE REASONABLE TO INSTRUCT THAT ANY FINANCIAL INSTITUTION THAT IS A MEMBER OF CBA THAT INTENDS TO A VAIL ITSELF OF THE INJUNCTIVE RELIEF THAT THIS COURT IS ORDERING, DOES SO CONDITIONED ON COMPLYING WITH THE SAME INSTRUCTIONS THAT YOU ARE MAKING WITH RESPECT TO THE PLAINTIFF BANKS.

THE COURT: IS THAT SATISFACTORY, MR. BERNHARD?

MR. BERNHARD: I AM NOT SURE. I AM NOT SURE IF I UNDERSTAND EXACTLY WHAT IT MEANS.

WHAT I AM CERTAIN OF IS THAT MR.

Not Reported in F.Supp.2d
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CHENOWETH, OFFICIAL OF CBA
SUBMITTED A DECLARATION, AND HE
ALSO, I BELIEVE, SAID THAT THEY COULD
ESCROW FUNDS. AND WE WOULD LIKE HIM
TO LIVE UP TO THAT PROMISE.

THE COURT: WELL, I AM RELUCTANT,
WOULD BE MORE THAN RELUCTANT TO
ENJOIN PARTIES THAT ARE NOT BEFORE
ME.

CBA IS NOT A DEPOSITORY INSTITUTION. I
AM RATHER INCLINED TO THINK THAT IT
MIGHT BE A USEFUL WAY TO BEGIN THIS
LITIGATION, SINCE WE ARE STILL AT A
VERY EARLY STAGE, TO ASK YOU, MR.
BERNHARD TO TALK TO MR. KASS AND SEE
IF THERE ISN'T A PRACTICAL SOLUTION TO
YOUR CONCERNS.

MR. BERNHARD: I WOULD BE HAPPY TO
DO THAT.

THE COURT: ANYTHING FURTHER?

MR. BERNHARD: I HAVE ONE LAST
MATTER, YOUR HONOR. AT THIS TIME,
DEFENDANTS ASK THE COURT TO STAY
ITS ORDER FOR 30 DAYS TO PERMIT
DEFENDANTS AN OPPORTUNITY TO
OBTAIN RELIEF.

THE COURT: MR. BRUCE?

MR. BRUCE: THIS IS A STAY PENDING
APPEAL?

THE COURT: STAY PENDING APPEAL.

MR. BERNHARD: IT'S FOR A STAY
PENDING APPLICATION FOR RELIEF.

MR. BRUCE: YES.

MR. BERNHARD:--TO THE NINTH CIRCUIT.

MR. BRUCE: YOUR HONOR, WE FULLY
EXPECT THEM TO GO TO THE COURT OF
APPEALS, AS YOUR HONOR INDICATED IN
YOUR DECISION.

A STAY OF 30 DAYS COULD, I AM NOT
SAYING SAN FRANCISCO WOULD DO THIS.
BUT IT COULD PUT THE BOARD OF
SUPERVISORS IN A POSITION THAT THEY
WOULD GO AHEAD AND ALLOW THE SAN
FRANCISCO ORDINANCE TO BECOME
EFFECTIVE, BECAUSE 30 DAYS FROM
TODAY IS DECEMBER THE 15TH. AND
LEFT--THAT WOULD BE VERY UNWISE, I
THINK, FOR THEM TO DO THAT, AND
MAYBE MR. BERNHARD CAN GIVE U.S.
SOME COMFORT IN TERMS OF AN
ASSURANCE THAT DURING THAT STAY

PERIOD, SAN FRANCISCO WILL NOT ALLOW
ITS ORDINANCE TO BECOME EFFECTIVE.

THE COURT: WELL, IF I DENY THE STAY.

MR. BERNHARD HAS HIS RECORD.

MR. BRUCE: IF YOU DENY THE STAY, WE
OBVIOUSLY HAVE NO PROBLEM WITH
THAT.

THE COURT: MR. BERNHARD HAS HIS
RECORD.

MR. BRUCE: YES, THANK YOU.

THE COURT: I THINK I WILL UNDER THE
CIRCUMSTANCES SINCE WE ARE GOING
TO BE SETTLING THE EXACT TERMS OF
THE ORDER WITH RESPECT TO ALL OF
THESE MATTERS WE HAVE DISCUSSED IN
THE NEXT FEW DAYS, AN EFFECTIVE
STAY IS NOT APPROPRIATE, BUT YOU
HAVE MADE YOUR RECORD AND
REQUESTED THE COURT TO STAY, AND
THAT HAS BEEN DENIED.

MR. BERNHARD: THANK YOU, YOUR
HONOR.

*12 THE COURT: ALL RIGHT? ANYTHING
FURTHER?

MR. BRUCE: NO, YOUR HONOR.

THE COURT: VERY WELL. THANK YOU,
COUNSEL.

1999 WL 33429989 (N.D.Cal.)

END OF DOCUMENT

FILED

APR 3 2003

CLERK, U.S. DISTRICT COURT
EASTERN DISTRICT OF CALIFORNIA
BY _____
FOR THE EASTERN DISTRICT OF CALIFORNIA

WELLS FARGO BANK, N.A., and)
WELLS FARGO HOME MORTGAGE, INC.,)

Plaintiffs,)

v.)

CIV. NO. S-03-0157 GEB JFM

DEMETRIOS A. BOUTRIS, in his)
official capacity as Commissioner)
of the California Department of)
Corporations,)

Defendant.)

QUICKEN LOANS INC, a Michigan)
corporation,)

Plaintiff,)

v.)

CIV. NO. S-03-0256 GEB JFM ✓

DEMETRIOS A. BOUTRIS, in his)
official capacity as Commissioner)
of the California Department of)
Corporations,)

Defendant.)

NATIONAL CITY BANK OF INDIANA, and)
NATIONAL CITY MORTGAGE CO.,)

Plaintiffs,)

v.)

CIV. NO. S-03-0655 LKK DAD

DEMETRIOS A. BOUTRIS, in his)
official capacity as Commissioner)
of the California Department of)
Corporations,)

Defendant.)

RELATED CASE ORDER

Examination of the above-entitled actions reveals that
the actions are related within the meaning of Local Rule 83-123(a).

1 The actions are based on the same or similar claims, similar questions
2 of fact and the same question of law. Accordingly, the assignment of
3 the matters to the same judge and magistrate judge is likely to effect
4 a substantial savings of judicial effort and is also likely to be
5 convenient for the parties.

6 The parties should be aware that relating the cases under
7 Local Rule 83-123 merely has the result that the actions are assigned
8 to the same judge and magistrate judge; no consolidation of the
9 actions is effected. Under the regular practice of this court,
10 related cases are generally assigned to the judge and magistrate judge
11 to whom the first filed action was assigned.

12 IT IS THEREFORE ORDERED that the action denominated CIV. NO.
13 S-03-0655 LKK DAD be, and the same hereby is, reassigned to Judge
14 Garland E. Burrell, Jr., and Magistrate Judge John F. Moulds for all
15 further proceedings, and any dates currently set in this reassigned
16 case only are hereby VACATED. The parties are referred to the
17 attached Order Setting Status (Pretrial Scheduling) Conference.
18 Henceforth, the caption on documents filed in the reassigned case
19 shall be shown as CIV. NO. S-03-0655 GEB JFM.

20 IT IS FURTHER ORDERED that the Clerk of the Court make
21 appropriate adjustment in the assignment of civil cases to compensate
22 for this reassignment.

23 IT IS SO ORDERED.

24 DATED: April 2, 2003

25
26 /s/ GARLAND E. BURRELL, JR.
United States District Judge
27
28

FILED

April 4, 2003

CLERK, US DISTRICT COURT
EASTERN DISTRICT OF
CALIFORNIA

S Kirkpatrick

DEPUTY CLERK

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF CALIFORNIA

NATIONAL CITY BANK OF
INDIANA,

Plaintiff,

V.

DEMETRIOS A BOUTRIS,

Defendants.

CIV. NO. S-03-655 GEB JFM

ORDER SETTING STATUS

(PRETRIAL SCHEDULING)

CONFERENCE

This action has been assigned to Judge Garland E. Burrell, Jr. Pursuant to the provisions of Federal Rule of Civil Procedure 16, IT IS ORDERED that:

1. A status (pretrial scheduling) conference is set for August 11, 2003 at 9:00 a.m., before Judge Burrell in Courtroom #10 of the above-entitled court;

2. All parties to the action shall appear by counsel (or in person if acting without counsel; however, pursuant to Local Rule 83-183, a corporate party or other entity may not appear in propria persona and must appear through counsel);

3. Concurrently with the service of process, or as soon thereafter as possible, plaintiff(s) shall serve upon each of the parties named herein, and upon all parties subsequently joined by plaintiff, a copy of this order, and shall file with the Clerk of Court a certificate reflecting such service. Any party who impleads a third party defendant shall serve upon that party a copy of this order, and shall file with the Clerk of Court a certificate reflecting such service;

1 4. In the event this action was originally filed in a
2 state court and was thereafter removed to this court, the removing
3 party or parties shall, immediately following such removal, serve
4 upon each of the other parties named herein and upon all parties
5 subsequently joined, a copy of this order and shall file with the
6 Clerk of Court a certificate reflecting such service;

7 5. At least twenty-one (21) calendar days before the
8 scheduling conference is held, the parties shall confer and develop
9 a proposed discovery plan, as required by Fed. R. Civ. P. 26(f);

10 6. The parties shall file a Joint Status Report with the
11 court not later than fourteen days prior to the scheduling
12 conference.¹ The report shall briefly set forth the views of each
13 party on the following matters:

- 14 a) Status of service of process on parties not yet
15 served;
- 16 b) Possible joinder of additional parties;²
- 17 c) Anticipated amendment of pleadings;
- 18 d) The basis for jurisdiction and venue;
- 19 e) Anticipated motions with suggested dates;
- 20 f) Anticipated and outstanding discovery;³
- 21 g) A written report outlining the proposed discovery
22 plan required by Fed. R. Civ. P. 26(f). The
23 discovery plan shall indicate the parties' views and
24 proposals concerning:

25 ¹ The failure of one or more of the parties to participate in
26 the preparation of the Joint Status Report does not excuse the other
27 parties from their obligation to timely file a status report in
28 accordance with this Order. In the event a party fails to participate
as ordered, the party timely submitting the status report shall
include a declaration explaining why it was unable to obtain the
cooperation of the other party or parties.

29 ² Plaintiff(s) shall indicate in the Joint Status Report a
date by when the identities of any "Doe" defendants are expected to be
discovered. Failure to set forth specific information regarding the
time Plaintiff(s) needs to identify any "Doe" defendants will be
deemed an abandonment of any claims against such defendants, and a
dismissal order will follow.

30 ³ Fed. R. Civ. P. 26 requires, absent a contrary stipulation,
initial disclosures to be made as provided in that Rule. Any
objection to the initial disclosures and the basis therefor must be
included in the joint status report.

1 (1) what changes should be made in the timing,
2 form, or requirement for disclosures under Rule
3 26(a), including a statement as to when
disclosures under subdivision (a)(1) were made
or will be made;

4 (2) the subjects on which discovery may be
5 needed, when discovery should be completed, and
6 whether discovery should be conducted in phases
or be limited to or focused upon particular
issues; and

7 (3) what changes should be made in the
8 limitations on discovery imposed under the
Federal Rules of Civil Procedure or the Local
Rules, and what other limitations should be
9 imposed;

- 10 h) Scheduling of future proceedings, including
11 suggested timing of the disclosure of expert
12 witnesses and information required by Rule 26(a)(2),
completion dates for discovery and law and motion,
and dates for final pretrial conference and trial;⁴
- 13 i) Estimate of trial time;
- 14 j) Appropriateness of special procedures such as
15 reference to a special master or agreement to try
the matter before a magistrate pursuant to 28 U.S.C.
16 § 636(c);
- 17 k) Modification of standard pretrial procedures because
of the simplicity or complexity of the case;
- 18 l) Whether the case is related to any other case
19 pending in this district, including the bankruptcy
courts of this district;
- 20 m) Prospects for settlement, including whether a
21 settlement conference should be scheduled and
whether the parties will stipulate to the trial
22 judge acting as settlement judge;
- 23 n) Any other matter that may be conducive to the just
24 and expeditious disposition of the case.

25 ⁴ In completing this portion of the status report, the parties
26 are advised that Judge Burrell's typical pretrial scheduling
27 procedures require: 1) that initial expert disclosures be made 150
28 days prior to the completion of discovery; 2) that rebuttal expert
disclosures be made 120 days prior to the completion of discovery; 3)
that discovery be completed 90 days prior to the final pretrial
conference; 4) that law and motion is cut off 60 days before the final
pretrial conference; and 5) that the final pretrial conference will be
held 90 days before the trial.

1 7. Following the status conference, a formal order will
2 be issued regarding future proceedings in the case. Requests to
3 modify or vacate any date set forth in the order are not favored
4 and will not be granted absent good cause.

5 8. The parties are advised that failure to file a joint
6 status report in accordance with this order may result in the
7 imposition of sanctions.

8 9. The parties are required to immediately notify the
9 courtroom deputy and chambers of any settlement or other
10 disposition of the case. L.R. 16-160. In addition to notifying
11 chambers orally, the parties shall file a notice of settlement in
12 the Clerk's Office within three (3) days which sets forth a date by
13 which dispositional documents will be filed.

14 10. Motions shall be filed in accordance with Local Rule
15 78-230(b). Opposition papers shall be filed in accordance with
16 Local Rule 78-230(c). Any party that does not oppose the granting
17 of the motion shall file a statement of non-opposition as required
18 by Local Rule 78-230(c). The failure to file an opposition or
19 statement of non-opposition in accordance with Local Rule 78-230(c)
20 may be deemed consent to the granting of the motion and the Court
21 may dispose of the motion summarily. Brydges v. Lewis, 18 F.3d
22 651, 652-53 (9th Cir. 1994).

23
24 IT IS SO ORDERED

25
26 DATE: April 4, 2003

27
28 GARLAND E. BURRELL, JR.
UNITED STATES DISTRICT JUDGE

by: S Kirkpatrick
Deputy Clerk

United States District Court
for the
Eastern District of California
April 4, 2003

* * CERTIFICATE OF SERVICE * *

2:03-cv-00157

2:03-cv-00256
2:03-cv-00655

Wells Fargo Bank NA

v.

Dept of Corporations

I, the undersigned, hereby certify that I am an employee in the Office of the Clerk, U.S. District Court, Eastern District of California.

That on April 4, 2003, I SERVED a true and correct copy(ies) of the attached, by placing said copy(ies) in a postage paid envelope addressed to the person(s) hereinafter listed, by depositing said envelope in the U.S. Mail, by placing said copy(ies) into an inter-office delivery receptacle located in the Clerk's office, or, pursuant to prior authorization by counsel, via facsimile.

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Severson and Werson
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Suite 2600
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SF/GEB

AR/LKK

CF/JFM

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BY: Deputy Clerk

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