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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.

1 California Financial Lenders Law, Cal. Fin. Code § 22000 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 ¹ 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 ² 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...)

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

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."³ (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 ³ 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. . . ."

1 protect national banks against intrusive regulation by the States."

2 Bank of America v. City and County of San Francisco, 309 F.3d 551, 561

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
buying and selling exchange, coin, and bullion; by
loaning money on personal security; and by
obtaining, issuing, and circulating notes. . . .

10 12 U.S.C. § 24(Seventh). The United States Supreme Court stated that
11 the National Bank Act has charged the Comptroller with the supervision
12 of the Act, and that the Comptroller bears "primary responsibility for
13 surveillance of 'the business of banking' authorized by § 24

14 (Seventh)." Nationsbank of North Carolina, N.A. v. Variable Annuity

15 Life Ins. Co., 513 U.S. 251, 256 (1995); see 12 U.S.C. § 1, 26-27,

16 481. The United States Supreme Court held that the "'business of

17 banking' is not limited to the enumerated powers in § 24 Seventh and
18 that the Comptroller therefore has discretion to authorize activities

19 beyond those specifically enumerated. The exercise of the

20 Comptroller's discretion, however, must be kept within reasonable

21 bounds." NationsBank of North Carolina, N.A., 513 U.S. at 258 n.2.

22 The OCC-promulgated regulation regarding the exercise of
23 visitorial powers over national banks provides:

24 Only the OCC or an authorized representative of
25 the OCC may exercise visitorial powers with
26 respect to national banks except as provided in
27 paragraph (b) of this section. State officials
28 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

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

4 12 C.F.R. § 7.4000.

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

17 Operating Subsidiaries

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

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

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

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

20 Acquisition of Controlling Stock Interest in Subsidiary Operations
21 Corporation, 31 Fed. Reg. 11,459 at 11,459-60 (Aug. 31, 1966).

22 Plaintiffs and the OCC also argue that the Gramm-Leach-
23 Bliley Act ("GLBA") acknowledges national banks' authority to conduct
24 banking business through operating subsidiaries. See 12 U.S.C. § 24a.
25 The GLBA defines a financial subsidiary as something "other than a
26 subsidiary that . . . engages solely in activities that national banks
27 are permitted to engage in directly and are conducted subject to the
28 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:

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

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

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

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

16 During the March 10 hearing, OCC pointed to the Third
17 Circuit decision in Nat'l State Bank, Elizabeth, N.J. v. Long, 630
18 F.2d 981 (3d Cir. 1980), as support for its position that the OCC has
19 exclusive visitorial powers over WFHMI whether or not the enforcement
20 of California law is involved. Long reveals, "Questions about the
21 applicability of state legislation to national banks must be
22 distinguished from the related inquiry of who is responsible for
23 enforcing national bank compliance." Long, 630 F.2d at 987-88. In
24 light of the respect that is to be given to the OCC's construction of
25 the National Bank Act articulated in its brief and its interpretive
26 letter where it opines it has exclusive visitorial power over WFHMI as
27 a subsidiary of a national bank, Plaintiffs are likely to prevail on
28 the merits of their claim that the OCC's recognition of WFHMI'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

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
23 succeed on the merits of this action but are
24 impeded in their business activities by the
25 Commissioner's actions to stop WFHMI from
26 continuing its business operations in California
27 for some period of time before they obtain a
28 favorable final decision from this Court.

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

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

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 visitorial powers over Plaintiffs or from otherwise
 26 preventing WFHMI from operating in California; however, the portion of

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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

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6 ~~GARLAND E. BURRELL, JR.~~
7 UNITED STATES DISTRICT JUDGE
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