Office of Thrift Supervision
Department of the Treasury
Chief Counsel
1700 G Street, N.W., Washington, DC 20552 • (202) 906-6251

October 1, 2002

Mr. Stan Ommen, President
State Farm Bank, F.S.B.
One State Farm Plaza
Bloomington, IL 61710-0001

Re: Preemption of California Minimum Payment Statute

Dear Mr. Ommen:

This responds to your inquiry to the Office of Thrift Supervision ("OTS") on behalf of State Farm Bank, F.S.B., Bloomington, Illinois ("Association"), a federal savings association. You ask OTS to confirm that federal law preempts the application to federal savings associations of legislation referred to as the California Minimum Payment Statute ("California Statute"). The California Statute purports to regulate lending practices of credit card issuers, including federal savings associations.

In the Home Owners' Loan Act ("HOLA"),[1] Congress conferred on OTS responsibility to provide for the safe and sound operation of federal savings associations such as the Association. To fulfill that responsibility, Congress granted OTS plenary and exclusive authority to regulate all aspects of the operations of federal savings associations. Exercising that authority, OTS has promulgated comprehensive regulations governing lending operations. Those regulations specifically occupy the field of regulating federal savings associations' lending practices. In addition, two OTS regulations directly preempt state laws purporting to regulate disclosures made by, or terms of credit offered by, federal savings associations. Accordingly, for the reasons discussed in more detail below, we confirm that HOLA and OTS regulations preempt the California Statute.[2]

[1] 12 U.S.C.A. § 1461 *et seq.* (West 2001).

[2] You indicate that this issue is currently being litigated in the United States District Court for the Eastern District of California in *American Bankers Association et al. v. Lockyer*, No. CIV.S-02-1138 FCD (JFM). We understand that on June 28, 2002, the court stayed the effectiveness of the statute pending further hearing on a motion for a preliminary injunction on November 8, 2002.

Background

The Association engages in credit card lending nationwide, including California. Federal law expressly authorizes a federal savings association to invest in, sell, or otherwise deal in loans made through credit cards or credit card accounts under HOLA § 5(c)(1)(T).[3] OTS regulation 560.30 codifies this authority. The regulation provides that federal savings associations may conduct credit card lending "subject to the limitations indicated and any such terms, conditions, or limitations as may be prescribed from time to time by OTS by policy directive, order, or regulation."[4]

The applicable "terms, conditions, or limitations" are expressed in detailed regulations that OTS has promulgated, through notice and comment rulemaking, governing the lending activities of federal savings associations.[5] OTS's Thrift Activities Handbook also contains detailed and authoritative guidance on how federal savings associations are to conduct their lending activities, including credit card lending.[6]

The California Statute,[7] however, also purports to regulate federal savings associations when issuing credit cards. Among its requirements, the California Statute requires credit card issuers to provide to cardholders a combination of warnings and estimates of the length of time necessary to pay off their balances and the total cost of credit if only the required minimum is repaid each month. Issuers are not required to make these disclosures in any billing cycle in which either the account agreement requires a minimum payment of at least 10% of the outstanding balance or finance charges are not imposed. Issuers must also refer cardholders to credit counseling under certain circumstances. In addition to these disclosure requirements, the California Statute also requires some issuers to maintain a toll-free number to provide payoff estimates during specified hours. The California Statute further provides that certain provisions will not apply if the federal Bankruptcy Reform Act of 2001, as proposed by H.R. No. 333 of the 107th Congress, is enacted and includes the provisions of Section 1301

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[3] 12 U.S.C.A. § 1464(c)(1)(T) (West 2001).

[4] 12 C.F.R. § 560.30 (2002).

[5] *See* 12 C.F.R. part 560 (2002) (Lending and Investment).

[6] OTS Thrift Activities Handbook § 218 (Jan. 1994). This handbook addresses all of the major areas of concern to examiners and supervisors regarding the safety and soundness of OTS-regulated institutions. The handbook includes specific examination objectives and procedures.

[7] The legislation, passed as California Assembly Bill No. 865, consists of three sections. Section 1 adds a new section 1748.13 to the California Civil Code. Section 2 addresses the interrelationship of the California Statute with federal legislation that may be enacted in the future. Section 3 indicates the various effective dates of the California Statute's provisions.

addressing Enhanced Disclosures Under an Open End Credit Plan as it read on July 17, 2001. As of the date of this opinion, that bill has not been enacted.

Discussion

The doctrine of federal preemption, rooted in the Supremacy Clause of the United States Constitution,[8] applies in three situations: (1) Congress may expressly preempt state law;[9] (2) congressional intent for federal preemption of state law may be inferred when federal law dominates or occupies a particular field;[10] and (3) state law is nullified to the extent that it conflicts with federal law, that is, when compliance with both state and federal law or regulations is a physical impossibility, or when compliance with state law stands as an obstacle to the accomplishment of the objectives of Congress.[11] Federal regulations have no less preemptive effect than federal statutes.[12]

HOLA §§ 4(a) and 5(a)[13] authorize OTS to provide for the safe and sound operation of federal savings associations. These federal statutory provisions grant OTS exclusive and plenary authority to regulate all aspects of the operations of federal savings associations including, under HOLA § 5(c), their lending activities.

Numerous federal courts, OTS, and its predecessor, the Federal Home Loan Bank Board ("FHLBB"), have found that HOLA § 5(a), and OTS and the FHLBB implementing regulations, preempt state laws that purport to regulate the "activities or operations" of federal savings associations because Congress conferred on OTS and the

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[8] U.S. Constitution, Article VI, cl. 2.

[9] *Pacific Gas and Electric Co. v. State Energy Resources and Development Comm'n*, 461 U.S. 190, 203-04 (1983); *Fidelity Federal Savings and Loan Ass'n v. de la Cuesta*, 458 U.S. 141, 152-53 (1982) ("*de la Cuesta*").

[10] *de la Cuesta*, 458 U.S. at 153. *See also Barnett Bank of Marion County, N.A. v. Nelson*, 517 U.S. 25, 31 (1996) ("*Barnett Bank*") ("A federal statute, for example, may create a scheme of federal regulation 'so pervasive as to make reasonable the inference that Congress left no room for the States to supplement it'").

[11] *de la Cuesta*, 458 U.S. at 153-156 and 159 and cases cited therein; *Barnett Bank*, 517 U.S. at 31-37 and cases cited therein. *See also Silkwood v. Kerr-McGee Corp.*, 464 U.S. 238, 248 (1984); *First Federal Savings and Loan Ass'n of Boston v. Greenwald*, 591 F.2d 417, 425 (1st Cir. 1979) ("*Greenwald*") (preempting Massachusetts law requiring payment of interest on tax escrow account that conflicted with a regulation of OTS's predecessor agency, the Federal Home Loan Bank Board ("FHLBB")); *Kupiec v. Republic Federal Savings and Loan Ass'n*, 512 F.2d 147, 150 ("*Kupiec*") (7th Cir. 1975) (preempting state common law right to inspect and copy membership list that conflicted with FHLBB model bylaw governing communication with members or depositors).

[12] *de la Cuesta*, 458 U.S. at 153-54.

[13] 12 U.S.C.A. §§ 1463(a) and 1464(a) (West 2001). OTS has analyzed these provisions in a number of Chief Counsel opinions. *See, e.g.*, OTS Op. Chief Counsel (Jan. 10, 2002); OTS Op. Chief Counsel (July 26, 1999); OTS Op. Chief Counsel (July 1, 1998); OTS Mem. Chief Counsel (Sept. 2, 1997).

FHLBB exclusive authority to regulate the operations of federal savings associations.[14] Federal courts also have found that FHLBB regulations preempted state law where the law in question was an obstacle to the achievement of the objectives of, and therefore conflicted with, federal regulations.[15]

In enacting HOLA, Congress required the FHLBB (and now the OTS) to provide for the organization, incorporation, examination, operation, and regulation of federal savings associations "giving primary consideration of the best practices of thrift institutions in the United States."[16] Consistent with this language, OTS has made clear in its lending regulations its intent to carry out this congressional objective by giving federal savings associations maximum flexibility to exercise their lending powers in accordance with a uniform federal scheme of regulation.[17] That uniform federal scheme occupies the field of regulation for lending activities. The comprehensiveness of the HOLA § 5(a) language demonstrates that Congress intended the federal scheme to be exclusive, leaving no room for state regulation, conflicting or complementary.

OTS occupies the field to enhance safety and soundness and enable federal savings associations to conduct their operations in accordance with best practices by efficiently delivering low-cost credit to the public free from undue regulatory duplication and burden.[18] Under § 560.2(a), federal savings associations may extend credit as authorized under federal law without regard to state laws purporting to regulate or

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[14] *See, e.g., Conference of Federal Savings and Loan Associations v. Stein*, 604 F. 2d 1256, 1260 (9th Cir. 1979) ("*Stein*") ("[T]he regulatory control of the [FHLBB] over federal savings and loan associations is so pervasive as to leave no room for state regulatory control . . . . The broad regulatory authority over the federal associations conferred upon the [FHLBB] by HOLA does wholly preempt the field of regulatory control over these associations."), *aff'd mem.*, 445 U.S. 921 (1980); *FHLBB v. Empie*, 628 F. Supp. 223, 225 (W.D. Okla. 1983) ("*Empie*") ("Congress intended the HOLA to preempt all state regulation over federally-chartered savings and loan institutions."), *aff'd on other grounds*, 778 F.2d 1447 (10th Cir. 1985); *People v. Coast Federal Savings and Loan Ass'n*, 98 F. Supp. 311, 316 (S.D. Cal. 1951) ("The FHLBB has adopted comprehensive rules and regulations governing the powers and operations of every Federal savings and loan association from its cradle to its corporate grave"). *See also* OTS Op. Chief Counsel (Jan. 18, 1996) (state reporting requirements preempted); OTS Op. Chief Counsel (Oct. 11, 1991) (state deposit taking requirements preempted); FHLBB Op. General Counsel (Apr. 28, 1987) (state lending and examination requirements preempted).

[15] *de la Cuesta*, 458 U.S. at 156 and 159 (quoting *Heinz v. Davidowitz*, 312 U.S. 52, 67 (1941)) (preempting state limitation on due on sale practices that conflicted with FHLBB regulation); *Empie*, 778 F.2d at 1453-54 (preempting state limitation on use of word "bank" in advertising that conflicted with FHLBB regulation); *Greenwald*, 591 F. 2d at 425 (preempting Massachusetts law requiring payment of interest on tax escrow account that conflicted with FHLBB regulation); *Kupiec*, 512 F.2d at 150 (preempting "common law" right to inspect and copy membership list that conflicted with FHLBB model bylaw governing communication between members or depositors).

[16] 12 U.S.C.A. § 1464(a) (West 2001).

[17] 12 C.F.R. § 560.2(a) (2002).

[18] *Id.*

otherwise affect their credit activities. As described above, the California Statute imposes a number of very specific disclosure and other requirements on credit card loans. The California Statute would regulate areas covered by § 560.2 and therefore does not apply to federal savings associations' credit card lending.

Moreover, two specific OTS regulations clearly and expressly preempt the types of requirements in the California Statute. First, OTS regulation 560.2(b)(9) preempts the California Statute's disclosure requirements. The regulation provides that state laws purporting to impose requirements on federal savings associations regarding "Disclosure and advertising, including laws requiring *specific statements, information, or other content to be included in* credit application forms, credit solicitations, *billing statements*, credit contracts, or other credit-related documents and laws" are preempted.[19] We note that a federal savings association's credit card lending activities are subject to the elaborate federal network of disclosure laws, including the Truth in Lending Act and Federal Reserve Board Regulation Z.[20]

Second, to the extent that the California Statute seeks to compel federal savings associations to forbear from collecting interest due or to set minimum payments above a state-determined threshold in order to avoid triggering the California Statute's requirements, it is preempted by OTS regulation 560.2(b)(4). That regulation provides, in relevant part, that state laws purporting to impose requirements on federal savings associations regarding the "terms of credit, including amortization of loans . . . [and] payments due" are preempted.[21]

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[19] 12 C.F.R. §§ 560.2(b)(9) (2002) (emphasis added).

[20] 15 U.S.C.A. § 1601 *et seq.* (West 1998 & Supp. 2001) and 12 C.F.R. part 225 (2002), respectively. We further note that OTS has a long-standing regulation prohibiting savings associations from using advertising or making representations that are inaccurate or that misrepresent the association's products, services, or contracts. 12 C.F.R. § 563.27 (2002); *see also* 12 U.S.C.A. § 1468a (West 2001).

[21] 12 C.F.R. §§ 560.2(b)(4) (2002). Since the California Statute is the type preempted under § 560.2(b)(4) and (b)(9), the analysis ends there and the law is preempted. *See* 61 Fed. Reg. 50,951, 50,966 (Sept. 30, 1996) (Final Rule: Lending and Investment).

OTS regulation 560.2(c), addressing deference to certain types of state laws, offers no relief from this preemption. That regulation states that certain traditional areas of state law and laws that further a vital state interest are generally not preempted unless (1) they have more than an incidental effect on federal savings association lending operations, or (2) they are contrary to the purposes expressed in OTS regulation 560.2(a) discussed above. The California Statute has more than an incidental effect on federal savings associations' lending operations because it imposes substantive requirements concerning disclosures and the terms of credit directly on the lending process. The California Statute is also contrary to the purposes expressed in OTS regulation 560.2(a) because it limits the flexibility of federal savings associations to exercise their lending powers under a uniform federal scheme of regulation.

Several OTS legal opinions have applied these regulations to determine that state laws imposing loan disclosure requirements are preempted for federal savings associations. Most notably, in 1996 OTS concluded that specific lending disclosures required by Indiana and Ohio consumer credit laws were preempted for federal savings associations' credit card loan programs.[22] Instead, federal savings associations are to comply with applicable federal disclosure requirements. As the opinion noted, this conclusion was consistent with the agency's longstanding position that state disclosure laws are preempted for federal savings associations.[23] Since 1996, OTS has continued to find such state laws to be preempted, including those regulating credit card disclosures.[24]

Likewise, Federal courts have also concluded that state laws imposing disclosure requirements are preempted for federal savings associations. These include two decisions of the Ninth Circuit Court of Appeals, including one decision issued just last month.[25]

The specific provisions of the California Statute also are preempted by OTS regulation 560.30, which permits federal savings associations to engage in credit card lending, restricted only by being subject to "the limitations indicated and any such terms, conditions, or limitations as may be prescribed from time to time by OTS by policy directive, order, or regulation." Neither § 560.30 nor any other OTS policy directive, order, or regulation imposes the requirements that the California Statute purports to impose on federal savings associations.

Further, the California Statute thwarts the more general congressional objective that OTS have exclusive responsibility for regulating the operations of federal savings associations "giving primary consideration of the best practices of thrift institutions in the United States.[26] Congress gave OTS, not the States, the task of determining the best

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[22] OTS Op. Chief Counsel (Dec. 24, 1996).

[23] *Id.* at 7 n.20 (citing OTS Op. Dep. Chief Counsel (Oct. 18, 1994) (state law requiring a savings association to provide copies of credit reports held by the savings association preempted); OTS Op. Chief Counsel (Jan. 3, 1991) (state law requiring disclosure of information on escrow accounts for mortgages preempted); FHLBB Op. Gen Counsel (Apr. 28, 1987) (state lending disclosure regulations preempted); FHLBB Op. Gen. Counsel (Nov. 12, 1985) (state truth in lending laws preempted)).

[24] *See* OTS Op. Counsels (Banking and Finance) (May 16, 2001) (state law requiring certain credit card disclosures and mandating loan contract terms preempted); OTS Op. Chief Counsel (Aug. 19, 1997) (state law requiring certain mortgage loan disclosures and mandating loan contract terms preempted).

[25] *See Lopez v. Washington Mutual Bank, FA*, 2002 WL 179294 (9th Cir. 2002) (account disclosure requirements of California Civil Procedure Code § 804.080 among those provisions preempted for federal savings associations); *Stein*, 604 F.2d at 1260 (antidiscrimination notice requirements of California Housing Financial Discrimination Act of 1977 among those provisions preempted for federal savings associations).

[26] 12 U.S.C.A. § 1464(a) (West 2001).

practices for thrift institutions and creating nationally uniform rules. Subjecting federal savings associations to the burdens of complying with a "hodgepodge of conflicting and overlapping state lending requirements" would undermine the federal objective of permitting federal savings associations to exercise their lending powers "under a single set of uniform federal laws and regulations. This [uniformity] furthers both the 'best practices' and safety and soundness objectives of the HOLA by enabling federal thrifts to deliver low-cost credit to the public free from undue regulatory duplication and burden."[27]

Finally, we note that to the extent the California Statute would require federal savings associations to maintain a toll-free telephone operation to provide payoff estimates, the requirement is preempted under OTS regulation 545.2.[28] The regulation expressly provides for OTS's exclusive authority to regulate all aspects of the operations of federal savings associations and preempt any state law purporting to address such operations. OTS's part 545 and part 555 regulations specifically regulate the various types of offices and telephone operations that a federal savings association may operate. The California Statute would impermissibly intrude on the establishment or nonestablishment of such operations and the terms such as hours and services offered.

In reaching the foregoing conclusions, we have relied on the factual representations made in the material you submitted to us as summarized herein. Our conclusions necessarily depend on the accuracy and completeness of those facts. Any material difference in facts or circumstances from those described herein could result in different conclusions.

If you have any questions regarding this matter, please feel free to contact Richard Bennett, Counsel (Banking & Finance) at (202) 906-7409.

Sincerely,

Carolyn J. Buck
Chief Counsel

cc: All Regional Directors
All Regional Counsel

[27] 61 Fed. Reg. at 50,965.

[28] 12 C.F.R. § 545.2 (2002).