

The Dodd–Frank Act's Expansion of State Authority to Protect Consumers of Financial Services

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| | |
|---|------------|
| I. INTRODUCTION | 895 |
| II. FEDERAL BANKING AGENCIES FAILED TO PROTECT CONSUMERS DURING THE HOUSING BOOM AND PREVENTED THE STATES FROM DOING SO | 897 |
| <i>A. The FRB Failed to Exercise Its Authority under HOEPA to Stop Predatory Lending</i> | <i>898</i> |
| <i>B. The FRB Failed to Regulate Nonprime Lenders That Were Subsidiaries of Bank Holding Companies</i> | <i>900</i> |
| <i>C. Federal Banking Agencies Issued Weak and Inadequate Guidance on Nonprime Mortgages</i> | <i>901</i> |
| <i>D. Federal Regulators Failed to Stop Predatory Lending Because of Their Belief in Deregulation and “Pushback” from the Financial Services Industry</i> | <i>903</i> |
| 1. <i>The FRB, the OTS and the OCC Followed Deregulatory Policies During the Nonprime Lending Boom</i> | <i>903</i> |
| 2. <i>The Financial Services Industry Strongly Resisted Efforts by Federal Regulators to Restrict Nonprime Mortgage Lending</i> | <i>907</i> |
| <i>E. The OTS and the OCC Preempted Initiatives by the States to Stop Predatory Lending, Thereby Aggravating the Severity of the Financial Crisis</i> | <i>909</i> |
| 1. <i>Many States Adopted Laws and Brought Enforcement Actions to Stop Predatory Lending.....</i> | <i>909</i> |
| 2. <i>The OTS and the OCC Preempted State APL Laws and State Enforcement Efforts.....</i> | <i>910</i> |
| 3. <i>The Industry-Based Funding for the OTS and OCC Created a Conflict of Interest Between Their Supervisory Duties and Their Budgetary Concerns</i> | <i>915</i> |
| 4. <i>OTS and OCC Preemption Helped Federal Thrifts and National Banks to Establish Leading Positions as Subprime and Alt-A Mortgage Lenders.....</i> | <i>916</i> |
| 5. <i>The OTS, the OCC, and the FRB Failed to Prevent the Failures of Several Major Financial Institutions That Were Heavily Engaged in Originating and Securitizing Nonprime Mortgages</i> | <i>918</i> |

| | |
|---|-----|
| III. TITLE X OF DODD–FRANK GRANTS SUPPLEMENTAL LAWMAKING AND LAW ENFORCEMENT POWERS TO THE STATES AND IMPOSES SIGNIFICANT RESTRICTIONS ON THE OCC’S AUTHORITY TO PREEMPT STATE LAWS | 920 |
| <i>A. Title X Establishes a Federal “Floor” of Protection for Consumers of Financial Services</i> | 920 |
| <i>B. Title X Empowers the States to Adopt Laws Providing Additional Protection to Consumers of Financial Services</i> | 922 |
| <i>C. Title X Enables State Attorneys General to Enforce the CFP Act and the CFPB’s Regulations</i> | 924 |
| <i>D. Dodd–Frank Limits the Preemptive Authority of the OCC with Respect to National Banks and Federal Thrifts</i> | 925 |
| 1. <i>Dodd–Frank Establishes New Preemption Standards That Govern the Application of State Consumer Financial Laws to National Banks and Federal Thrifts</i> | 925 |
| 2. <i>Dodd–Frank’s New Standards Significantly Limit the OCC’s Authority to Preempt State Consumer Financial Laws</i> | 926 |
| <i>a. Under Dodd–Frank, the OCC May Preempt a State Consumer Financial Law Only If That Law Prevents or Significantly Interferes With a National Bank’s Exercise of Its Powers</i> | 927 |
| <i>b. Dodd–Frank Requires the OCC to Act on a Case-by-Case Basis, to Show Substantial Evidence for Its Preemptive Determinations, and to Publish and Review Its Determinations Periodically</i> | 931 |
| <i>c. Dodd–Frank Confirms that the NBA Is Governed by Conflict Preemption Rules, and that OCC Preemption Determinations Are Not Entitled to Chevron Deference</i> | 932 |
| <i>d. Dodd–Frank Denies Preemptive Immunity to Most Subsidiaries, Affiliates and Agents of National Banks</i> | 934 |
| 3. <i>Dodd–Frank Requires the OCC to Rescind or Modify Its Existing Preemption Rules Except for the Regulation Governing the Charging of “Interest” under 12 U.S.C. § 85</i> | 935 |
| <i>a. The OCC’s Preemption Test Conflicts with the Barnett Bank Preemption Standard Incorporated by Dodd–Frank</i> | 936 |
| <i>b. The OCC’s Blanket Preemption Rules Are No Longer Valid in View of Dodd–Frank’s Mandate for “Case-by-Case” Determinations Supported by “Substantial Evidence”</i> | 938 |
| <i>c. The OCC’s Preemptive Rule for Operating Subsidiaries Conflicts with Dodd–Frank</i> | 938 |
| <i>d. The OCC’s Existing Preemption Rules Must Conform to Dodd–Frank by July 21, 2011</i> | 939 |
| 4. <i>Dodd–Frank Affirms the Authority of State AGs to Enforce Applicable Laws Against National Banks</i> | 941 |

| | |
|---|-----|
| 5. <i>Dodd–Frank Establishes Preemption Standards under HOLA That Are Equivalent to Those Embodied in the NBA</i> | 942 |
| 6. <i>Dodd–Frank Does Not Address State Laws of General Application, But Those Laws Should Presumptively Apply to National Banks under Existing Judicial Precedents</i> | 944 |
| IV. TITLE X OF DODD–FRANK CREATES A REGIME OF INTERACTIVE FEDERALISM THAT WILL PROVIDE BETTER SAFEGUARDS FOR CONSUMERS OF FINANCIAL SERVICES..... | 948 |
| <i>A. Title X Will Promote Beneficial Cooperation, Competition, and Innovation by CFPB and State Officials</i> | 949 |
| <i>B. Title X Reduces the Risk that CFPB Might Be Captured by the Financial Services Industry</i> | 951 |
| V. CONCLUSION | 954 |

I. INTRODUCTION

On July 21, 2010, President Barack Obama signed into law the Dodd–Frank Wall Street Reform and Consumer Protection Act (Dodd–Frank).¹ The statute’s preamble states that one of Dodd–Frank’s purposes is “to protect consumers from abusive financial services practices.”² When President Obama signed Dodd–Frank into law, he declared that the statute would create “the strongest consumer financial protections in history.”³

In order to implement and enforce Dodd–Frank’s new protections for consumers, Congress created the Bureau of Consumer Financial Protection (CFPB) as an “independent bureau” within the Federal Reserve System (Fed).⁴ President Obama explained that CFPB will operate as “a new consumer watchdog with just one job: looking out for people—not big banks, not lenders, not investment houses—looking out for people as they interact with the financial system.”⁵ Similarly, the Senate committee report on Dodd–Frank explained that CFPB’s mission is to “help protect consumers from unfair, deceptive, and abusive acts that so often trap them in unaffordable financial products.”⁶

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1. Dodd–Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

2. *Id.* at Preamble (describing the purposes of Dodd–Frank).

3. President Barack H. Obama, Remarks on Signing the Dodd–Frank Wall Street Reform and Consumer Protection Act (July 21, 2010), available at <http://whitehouse.gov/the-press-office/remarks-president-signing-dodd-frank-wall-street-reform-and-consumer-protection-act> [hereinafter Presidential Dodd–Frank Signing Statement].

4. Dodd–Frank § 1011(a), see also H.R. REP. NO. 111-517, at 874 (2010) (Conf. Rep.), reprinted in 2010 U.S.C.C.A.N. 722, 730.

5. Presidential Dodd–Frank Signing Statement, *supra* note 3.

6. S. REP. NO. 111-176, at 11 (2010).

Thus, Congress gave CFPB “the Herculean task of regulating the financial services industry to protect consumers.”⁷ Congress sought to increase CFPB’s “accountability” for that mission by delegating to CFPB the combined authority of seven federal agencies that were previously responsible for protecting consumers of financial services.⁸ Congress determined that a single federal authority dedicated to protecting consumers of financial services was needed in light of “the spectacular failure of the [federal] prudential regulators to protect average American homeowners from risky, unaffordable” mortgages during the housing boom that led to the financial crisis of 2007 to 2009.⁹ As stated in the Senate report, and as further explained in Part II of this Article, federal banking agencies “routinely sacrificed consumer protection” while adopting policies that promoted the “short-term profitability” of large banks, nonbank mortgage lenders and Wall Street securities firms.¹⁰ The Senate report concluded that “the failure by the prudential regulators to give sufficient consideration to consumer protection . . . helped bring the financial system down.”¹¹

To provide additional safeguards to consumers, Dodd–Frank enables the states to supplement CFPB’s rulemaking and enforcement efforts. Congress realized that many states attempted to stop abusive mortgage lending practices during the housing boom by adopting and enforcing state laws.¹² However, “rather than supporting these anti-predatory lending laws, federal regulators preempted them.”¹³ As explained in the Senate report and as further discussed in Part II.E of this Article, two federal banking agencies—the Office of the Comptroller of the Currency (OCC) and the Office of Thrift Supervision (OTS)—“actively created an environment where abusive mortgage lending could flourish without State control.”¹⁴

To correct the problems created by federal preemption, Dodd–Frank enlarges both the lawmaking and law enforcement functions of the states in the area of consumer financial protection. As described in Part III of this article, Title X of Dodd–Frank empowers CFPB to issue regulations that establish a federal “floor” of consumer protection and authorizes the states to adopt additional substantive rules that provide greater safeguards to consumers. Dodd–Frank also allows state officials to enforce the statutory provisions of Title X as well as CFPB’s regulations and applicable state laws. The Senate report endorsed these grants of enhanced authority to the states, noting that “States are much closer to [financial] abuses and are able to move more quickly when necessary to address them.”¹⁵

Moreover, Dodd–Frank abolishes the OTS, limits the preemptive authority of the OCC, and clarifies the states’ authority to apply and enforce their consumer financial protection laws against national banks and federally-chartered savings associations

7. Rachel E. Barkow, *Insulating Agencies: Avoiding Capture Through Institutional Design*, 89 TEX. L. REV. 15, 18 (2010).

8. S. REP. NO. 111-176, at 11 (2010).

9. *Id.* at 15.

10. *Id.* (quoting congressional testimony of Patricia McCoy on Mar. 3, 2009).

11. *Id.* at 166.

12. *Id.* at 16; *see also infra* Part II.E.1 (describing passage of anti-predatory lending laws by 30 states and the District of Columbia).

13. S. REP. NO. 111-176, at 16 (2010).

14. *Id.* at 17.

15. *Id.* at 174.

(federal thrifts). Under the new preemption standards established by Title X of Dodd–Frank, (i) state consumer financial laws will apply to national banks and federal thrifts unless they prevent or significantly interfere with the exercise of national bank powers; (ii) the OCC will have authority to preempt state laws only on a case-by-case basis and only if its preemption determinations are supported by substantial evidence; (iii) state laws will generally apply to the subsidiaries, affiliates and agents of national banks and federal thrifts; and (iv) state attorneys general will have authority to enforce applicable laws—including non-preempted state laws and CFPB’s regulations—against national banks and federal thrifts through judicial enforcement proceedings.

Part IV of this Article situates Title X of Dodd–Frank within contemporary debates about the proper role of state lawmaking and state enforcement in the area of consumer protection. By enabling states to construct additional safety measures on top of the federal “floor” of consumer financial protections, Title X of Dodd–Frank affirms the longstanding role of states as “laboratories of regulatory experimentation” in identifying emerging threats to consumer welfare and designing new legal rules to counteract those threats.¹⁶ In addition, the supplemental enforcement powers granted to states under Title X enables state officials to act as “normative entrepreneurs” in protecting their citizens from unfair, deceptive, or abusive financial practices in circumstances where CFPB or other federal agencies might fail to act.¹⁷ Finally, the independent lawmaking and law enforcement roles delegated to the states by Title X provide important safeguards against the potential risk that CFPB could be “captured” over time by the financial services industry.¹⁸

II. FEDERAL BANKING AGENCIES FAILED TO PROTECT CONSUMERS DURING THE HOUSING BOOM AND PREVENTED THE STATES FROM DOING SO

Regulatory inaction and preemption by federal banking agencies played a significant role in allowing abusive nonprime lending to grow and spread during the past decade. Nonprime lenders originated almost 10 million subprime and Alt-A mortgage loans between 2003 and 2007, and by 2008 about \$2 trillion of such loans were outstanding.¹⁹

16. Barkow, *supra* note 7, at 75–76; *see also* William W. Buzbee, *Asymmetrical Regulation: Risk, Preemption, and the Floor/Ceiling Distinction*, 82 N.Y.U. L. REV. 1547, 1554–56, 1586–89 (2007) (explaining the advantages of federal statutory schemes that establish a “floor” of minimum federal standards but allow individual states to experiment by adopting more protective measures); S. REP. NO. 111-176, at 174–75 (“If States were not allowed to take the initiative to enact laws providing greater protection for consumers, the Federal Government would lose an important source of information and reason to adjust [federal] standards over time.”). *Cf.* *New State Ice Co. v. Liebman*, 285 U.S. 262, 311 (1932) (Brandeis, J., dissenting) (“It is one of the happy incidents of the federal system that a single courageous State may, if its citizens choose, serve as a laboratory; and try novel social and economic experiments without risk to the rest of the country.”).

17. *See* Adam J. Levitin, *Hydraulic Regulation: Regulating Credit Markets Upstream*, 26 YALE J. ON REG. 143, 199–200 (2009) (describing political motivations that cause state officials to act as “normative entrepreneurs” in adopting new policies to protect consumers).

18. Barkow, *supra* note 7, at 53–57, 75–76; *see also* Buzbee, *supra* note 16, at 1609–11 (describing risks of regulatory capture); Levitin, *supra* note 17, at 199–206 (explaining why state enforcement of consumer protection laws could help to prevent regulatory capture).

19. Arthur E. Wilmarth, Jr., *The Dark Side of Universal Banking: Financial Conglomerates and the Origins of the Subprime Lending Crisis*, 41 CONN. L. REV. 963, 1015–17, 1027 (2009). The term “nonprime mortgages” includes “subprime” and “Alt-A” mortgages. Subprime mortgages were marketed to borrowers who

Unfortunately, the Federal Reserve Board (FRB) failed to exercise its authority under the Home Ownership and Equity Protection Act (HOEPA)²⁰ to prevent unfair and deceptive acts and practices in residential mortgage lending. The FRB also failed to stop abusive lending practices by nonbank mortgage lenders that were subsidiaries of bank holding companies.²¹

In contrast, the states did try to stop predatory lending. As discussed below, 30 states and the District of Columbia adopted anti-predatory lending (APL) laws between 1999 and 2007.²² However, the OCC and the OTS issued regulations that preempted state APL laws. Those rules barred states from applying their APL laws to national banks and federal thrifts, as well as their mortgage lending subsidiaries and agents. In addition, the OCC and the OTS failed to take effective action to stop abusive nonprime lending practices by national banks, federal thrifts, and affiliated entities.

Federal regulatory inaction and federal preemption encouraged federally-chartered depository institutions and their affiliates to become leading participants in nonprime mortgage lending. Ultimately, the regulatory failures of the FRB, the OCC, and the OTS contributed to defaults and foreclosures on millions of nonprime loans. By December 2010, lenders had foreclosed on about 5 million homes, and 4 million additional foreclosures were expected to occur in 2011 and 2012.²³ In addition, reckless lending by federally-chartered depository institutions and their affiliates led to the failures or government bailouts of several of the largest national banks and federal thrifts, including Citigroup, Wachovia, Washington Mutual, National City and IndyMac.

A. The FRB Failed to Exercise Its Authority under HOEPA to Stop Predatory Lending

In 1994, Congress passed HOEPA to prevent abusive lending practices in certain segments of the residential mortgage market.²⁴ Most of HOEPA's requirements are directed at "high-cost" mortgage refinancing loans; accordingly, those requirements do not apply to purchase mortgages, reverse mortgages, and home equity lines of credit.²⁵ However, one section of HOEPA authorizes the FRB to issue regulations and orders to "prohibit acts or practices in connection with . . . mortgage loans that the [FRB] finds to be unfair, deceptive, or designed to evade the provisions of this section."²⁶ Under that provision, HOEPA gives the FRB broad authority to stop unfair and deceptive lending practices by *all* types of federally-chartered and state-chartered lenders with respect to *all* types of mortgages.²⁷

had poor credit histories (including low credit scores and/or recent bankruptcies) as well as inadequate savings to make substantial down payments. In contrast, Alt-A loans were typically made to borrowers who had less serious credit problems or who were unable or unwilling to provide full documentation of their income or assets. *Id.* at 1015–16, 1016 n.256.

20. Home Ownership and Equity Protection Act, Pub. L. No. 103-325, §§ 151–58, 108 Stat. 2190, 2190–98 (1994) (codified as amended at various provisions of 15 U.S.C.).

21. See *infra* Parts II.A, II.B (describing the FRB's regulatory shortcomings)

22. See *infra* notes 112–16 and accompanying text (discussing state APL laws).

23. CONGRESSIONAL OVERSIGHT PANEL, DECEMBER OVERSIGHT REPORT: A REVIEW OF TREASURY'S FORECLOSURE PREVENTION PROGRAMS 10 (Dec. 14, 2010).

24. KATHLEEN C. ENGEL & PATRICIA A. MCCOY, THE SUBPRIME VIRUS 194–95 (2011).

25. *Id.*

26. 15 U.S.C. § 1639(l)(2) (1980).

27. ENGEL & MCCOY, *supra* note 24, at 195; Oren Bar-Gill & Elizabeth Warren, *Making Credit Safer*,

As required by HOEPA, the FRB held a series of public hearings on predatory lending between 1997 and 2000.²⁸ Following those hearings, members of the FRB’s staff proposed that the FRB adopt new rules under HOEPA.²⁹ The proposed rules would have prohibited all lenders from making mortgage loans based solely on the value of the collateral and without properly documenting the borrowers’ ability to repay the loans.³⁰ However, FRB Chairman Alan Greenspan and other members of the FRB’s Board of Governors rejected the staff proposals.³¹ Instead, the FRB adopted a regulation that slightly expanded the definition of “high-cost” loans and thereby modestly enlarged the scope of HOEPA’s regulatory regime for mortgage refinancing loans.³² As a practical matter, the FRB’s 2001 regulation covered “only about 1% of subprime loans” because subprime lenders changed the terms of their loans to avoid the FRB’s revised definition for application of HOEPA.³³

The FRB did not adopt another regulation under HOEPA until July 2008, when it issued comprehensive rules to ban unfair and deceptive practices with respect to a much broader category of “higher-priced mortgage loans.”³⁴ However, the Fed’s 2008 rules—which finally required lenders to verify borrowers’ ability to repay higher-priced loans—were issued “a year after the subprime market had shut down.”³⁵ Accordingly, the 2008 rules were “too little and too late” to play any role in preventing the predatory nonprime lending that led to the financial crisis.³⁶

At a hearing held by the Financial Crisis Inquiry Commission (FCIC) in September 2010, Commissioner John Thompson asked FDIC Chairman Sheila Bair, “[I]f you had one bullet that you could fire as a regulator that would have mitigated or . . . prevented this financial calamity, what would that have been?”³⁷ Chairman Bair replied: “I absolutely would have been over at the [FRB] writing rules, prescribing mortgage lending standards across the board for everybody, bank and nonbank, that you cannot make a mortgage unless you have documented income that the borrower can repay the

157 U. PA. L. REV. 1, 89 (2008).

28. FIN. CRISIS INQUIRY COMM’N, THE FINANCIAL CRISIS INQUIRY REPORT 76–77, 93 (2011) [hereinafter FCIC REPORT], available at <http://www.gpoaccess.gov/ecic/fcic.pdf>.

29. *Id.* at 93.

30. *Id.*

31. *Id.* at 93–94.

32. ENGEL & MCCOY, *supra* note 24, at 195.

33. FCIC REPORT, *supra* note 28, at 94; *see also* ENGEL & MCCOY, *supra* note 24, at 195 (describing very limited impact of the FRB’s 2001 regulation).

34. Truth in Lending, 73 Fed. Reg. 44,522 (July 30, 2008).

35. FCIC REPORT, *supra* note 28, at 22, 95; *see also* S. REP. NO. 111-176, at 16 (2010) (stating that the Fed’s 2008 rules were issued “long after the marketplace had shut down the availability of subprime and exotic mortgage credit”).

36. Patricia A. McCoy et al., *Systemic Risk Through Securitization: The Result of Deregulation and Regulatory Failure*, 41 CONN. L. REV. 1327, 1347 (2009); *see also* Sudeep Reddy, *Currents: Fed Faces Grilling on Consumer-Protection Lapses*, WALL ST. J., Dec. 2, 2009, at A22 (reporting that “many lawmakers and consumer advocates” viewed the Fed’s 2008 rules as “too little too late” because the Fed’s “ban on deceptive subprime-mortgage practices, came only after the financial crisis exposed vast regulatory holes and a sea of loans to homeowners who can’t meet their payments”).

37. *Too Big to Fail: Expectations and Impact of Extraordinary Government Intervention and the Role of Systemic Risk in the Financial Crisis: Hearing Before Fin. Crisis Inquiry Comm’n*, 112th Cong. 190–91 (2010), available at http://fcic-static.law.stanford.edu/cdn_media/fcic-testimony/2010-0902-transcript.pdf.

loan.”³⁸ Chairman Bair’s reply highlighted the significance of the FRB’s failure to exercise its authority to stop predatory lending under HOEPA.

B. The FRB Failed to Regulate Nonprime Lenders That Were Subsidiaries of Bank Holding Companies

The Bank Holding Company Act of 1956 (BHC Act) empowers the FRB to regulate nonbank subsidiaries of bank holding companies (BHCs).³⁹ Nevertheless, the FRB chose not to exercise its authority to regulate nonbank mortgage lending subsidiaries of BHCs between 1998 and 2007. As a result, the FRB failed to stop lending abuses by several major nonprime lenders that were affiliated with BHCs.

In January 1998, the FRB “formalized its long-standing policy of ‘not routinely conducting consumer compliance examinations of nonbank subsidiaries of [BHCs].’”⁴⁰ Some FRB officials and staff members subsequently tried to change this no-supervision policy for mortgage lending subsidiaries after they saw growing evidence of mortgage lending abuses.⁴¹ In 2000, members of the Fed’s consumer division staff proposed that the FRB undertake a pilot program to investigate predatory lending practices at selected nonbank subsidiaries of BHCs.⁴² Former FRB Governor Edward Gramlich, who served on the Board of Governors between 1999 and 2005, urged FRB Chairman Greenspan to implement the pilot program.⁴³ However, Chairman Greenspan rejected the proposal.⁴⁴

The FRB adhered to its no-supervision policy for nonbank mortgage lending subsidiaries of BHCs despite two reports issued by the GAO in 1999 and 2004, which criticized the FRB’s “lack of regulatory oversight” over such entities.⁴⁵ Chairman Greenspan later argued that the FRB “lacked sufficient resources” to regulate the nonbank subsidiaries and claimed that inadequate FRB supervision would have given a misleading “Good Housekeeping” seal of approval to such firms.⁴⁶ As a result of its no-supervision policy, the FRB failed to regulate BHC subsidiaries that were responsible for

38. *Id.* at 191; *see also* FCIC REPORT, *supra* note 28, at 94 (quoting reply by Chairman Bair). I served as a consultant to the FCIC during 2010.

39. *See* 12 U.S.C. §§ 1813(q)(D), 1843, 1844(c)(2)(B) (2006). Under a 1999 statute, the FRB was required to defer to the primary regulators of functionally-regulated subsidiaries of BHCs, such as banks, securities broker-dealers, and insurance companies. McCoy et al., *supra* note 36, at 1345–46. However, nonbank mortgage lenders were not functionally-regulated subsidiaries and were therefore fully subject to the FRB’s supervisory and enforcement authority. 12 U.S.C. §§ 1813(q)(2)(F), 1818, 1843(c); *see also* ENGEL & MCCOY, *supra* note 24, at 199 (“It doesn’t appear that [the 1999 statute] was what motivated the Fed’s refusal to examine [BHC] subsidiaries. In fact, the evidence suggests that the Fed’s failure to conduct routine examinations of subsidiaries during the subprime boom was a matter of discretion, not a dictate of the law.”).

40. FCIC REPORT, *supra* note 28, at 77 (quoting FRB Division of Consumer and Community Affairs, Consumer Affairs Letter CA 98-1, dated Jan. 20, 1998).

41. *Id.* at 94.

42. *Id.*

43. Greg Ip, *Did Greenspan Add to Subprime Woes? Gramlich Says Ex-Colleague Blocked Crackdown on Predatory Lenders Despite Growing Concerns*, WALL ST. J., Jun. 9, 2007, at B1.

44. *Id.*; FCIC REPORT, *supra* note 28, at 94–95.

45. FCIC REPORT, *supra* note 28, at 77, 95.

46. *Id.* at 95 (summarizing Mr. Greenspan’s interview with the FCIC); *see also* Binyamin Applebaum, *Fed Held Back as Evidence Mounted on Subprime Loan Abuses*, WASH. POST, Sept. 27, 2009, at A1 (characterizing the FRB’s approach as a “hands-off policy”); Edmund L. Andrews, *Fed and Regulators Shrugged as Subprime Crisis Spread*, N.Y. TIMES, Dec. 18, 2007, at A1 (noting Mr. Greenspan’s defense of his actions).

a substantial portion of subprime and Alt-A lending during the housing boom.⁴⁷

Between 1999 and 2007, several leading BHCs acquired nonprime mortgage lenders and used those nonbank subsidiaries to establish leading positions in the subprime and Alt-A mortgage markets. National City, a large Midwestern bank, purchased First Franklin in 1999.⁴⁸ Citigroup bought Associates First Capital in 2000⁴⁹ and Argent (an affiliate of Ameriquest) in 2007.⁵⁰ JP Morgan Chase acquired Advanta in 2001,⁵¹ and HSBC purchased Household in 2002.⁵² Countrywide, the nation’s largest mortgage lender, acquired a national bank and became a BHC in 2001.⁵³ Countrywide also established a securitization unit and expanded aggressively into subprime and Alt-A lending.⁵⁴ Despite the growing significance of nonprime lending by BHC subsidiaries, the FRB took only one public enforcement action against a nonbank subsidiary of a BHC.⁵⁵ In a 2004 order, the FRB levied a fine of \$70 million against CitiFinancial (the subprime mortgage lending subsidiary of Citigroup) for numerous lending violations.⁵⁶

The FRB did not change its no-supervision policy for nonbank subsidiaries of BHCs until July 2007, when it began a pilot program to examine subprime lending subsidiaries of several BHCs.⁵⁷ In September 2009, the FRB finally reversed its 1998 policy statement and announced a new policy to examine all nonbank subsidiaries of BHCs for compliance with consumer lending laws.⁵⁸ Again, the Fed’s policy change came far too late to prevent the financial crisis.

C. Federal Banking Agencies Issued Weak and Inadequate Guidance on Nonprime Mortgages

Instead of issuing binding rules to stop abusive nonprime lending, the FRB joined with other federal banking agencies in issuing statements of “guidance” on nonprime adjustable-rate mortgages (ARMs). In October 2006, federal regulators issued guidance on “nontraditional” mortgages, including “pick-a-pay” option ARMs and mortgages issued with little or no documentation of the borrowers’ income or assets.⁵⁹ Regulators

47. ENGEL & MCCOY, *supra* note 24, at 198–203 (noting that nonbank subsidiaries of BHCs “made 17.7%—almost one-fifth—of higher-priced [mortgage] loans in 2007”).

48. Wilmarth, *supra* note 19, at 1018.

49. *Id.* at 1017.

50. *Id.* at 1018; ENGEL & MCCOY, *supra* note 24, at 170.

51. Wilmarth, *supra* note 19, at 1017.

52. *Id.* at 1017–18.

53. *Id.* at 1018.

54. ENGEL & MCCOY, *supra* note 24, at 200–02; Wilmarth, *supra* note 19, at 1018; FCIC REPORT, *supra* note 28, at 107–08.

55. ENGEL & MCCOY, *supra* note 24, at 198–203.

56. *Id.* at 202–03; see also Binyamin Appelbaum, *As Subprime Lending Crisis Unfolded, Watchdog Fed Didn’t Bother Barking*, WASH. POST, Sept. 27, 2009, at A1 (reporting that the fine imposed on CitiFinancial represented “the Fed’s only public enforcement action against a lending affiliate”).

57. FCIC REPORT, *supra* note 28, at 95.

58. R. Christian Bruce, *Regulatory Reform: Fed to Broaden Consumer Protection Role Across Nonbank Subsidiaries of Bank Firms*, 93 BANKING REP. (BNA) 497 (Sept. 22, 2009) (citing FRB Letter CA 09-8, dated Sept. 14, 2009, issued by the Fed’s Division of Consumer and Community Affairs).

59. Interagency Guidance on Nontraditional Mortgage Product Risks, 71 Fed. Reg. 58,609, 58,609 (Oct. 4, 2006); see also FCIC REPORT, *supra* note 28, at 20–22, 172–73 (discussing issuance of federal guidance for

issued the 2006 guidance after they discovered alarming concentrations of nontraditional mortgages at major national banks and federal thrifts.⁶⁰

The federal banking agencies also issued guidance on “hybrid” subprime ARMs in July 2007.⁶¹ The 2006 and 2007 statements of guidance advised depository institutions that they should (i) underwrite each nonprime ARM based on the fully-amortized rate instead of the introductory “teaser” rate, and (ii) verify the borrower’s ability to repay the loan from sources other than the foreclosure value of the borrower’s collateral.⁶² However, both statements of guidance were presented merely as advice on good practices, were not directly enforceable by the agencies, and did not give injured borrowers any right to file lawsuits if lenders failed to follow the guidance.⁶³ For example, when regulators issued the 2006 guidance, Comptroller of the Currency John Dugan emphasized that the guidance “is *not* a ban on the use of nontraditional mortgage products” and “does *not* impose a limit on the number of nontraditional mortgages that an institution may hold.”⁶⁴

Federal regulators claimed that they enforced their statements of guidance and other consumer protection laws through bank examinations and “informal” enforcement measures such as voluntary agreements with supervised institutions.⁶⁵ For example, in October 2006, OCC Chief Counsel Julie L. Williams told a financial services group that the OCC “‘rarely’ brings an enforcement case, and uses prudential regulation almost exclusively.”⁶⁶ In a subsequent interview, Ms. Williams confirmed that the OCC’s

“nontraditional mortgages”). In a typical “pick-a-pay” option ARM, the borrower was permitted, during an introductory period of three to five years, to make either (i) interest-only monthly payments, or (ii) minimum monthly payments that were even lower than the accrued interest, in which case the unpaid interest was added to the loan balance. However, the borrower was normally required to make much higher monthly payments when either (A) the introductory period ended, or (B) the loan balance increased to 110% of 120% of the original principal amount. ENGEL & MCCOY, *supra* note 24, at 34; Wilmarth, *supra* note 19, at 1022 n.300.

60. FCIC REPORT, *supra* note 28, at 20 (stating that, during an interagency investigation in 2005, regulators found that nontraditional loans accounted for 59% of mortgage originations at Countrywide, 58% at Wells Fargo, 51% at National City, 31% at Washington Mutual, 26.5% at CitiFinancial, and 18.3% at Bank of America).

61. Statement on Subprime Mortgage Lending, 72 Fed. Reg. 37,569, 37,569 (July 10, 2007). “Hybrid” subprime ARMs were mortgages that allowed borrowers to pay a low “teaser” interest rate for an introductory period of two or three years and then required borrowers to pay much higher interest rates in subsequent years. ENGEL & MCCOY, *supra* note 24, at 34; FCIC REPORT, *supra* note 28, at 104–06.

62. See Interagency Guidance on Nontraditional Mortgage Product Risk, 71 Fed. Reg. at 58,611; Statement on Subprime Mortgage Lending, 72 Fed. Reg. at 37,571–73.

63. ENGEL & MCCOY, *supra* note 24, at 165–66. A federal banking agency “may”—but is not required to—require a depository institution to submit an “acceptable plan” if the institution fails to comply with guidance on lending practices. 12 U.S.C. § 1831p-1(e)(1)(A)(ii) (2006). However, the federal agency may not bring a formal enforcement proceeding based solely on an institution’s failure to comply with guidance. ENGEL & MCCOY, *supra* note 24, at 165–66.

64. ENGEL & MCCOY, *supra* note 24, at 165–66 (quoting speech by Mr. Dugan). For discussions of the inadequacy of regulatory guidance, see McCoy et al., *supra* note 36, at 1346–47, 1350–56 (explaining that the federal agencies’ nonbinding guidance failed to persuade leading national banks and federal thrifts to correct unsound mortgage lending practices); Andrews, *supra* note 46, at A1 (noting that, by the time regulators published the 2007 guidance for subprime lending, “more than 30 subprime lenders had gone out of business”).

65. ENGEL & MCCOY, *supra* note 24, at 164–65, 168–69.

66. Rachel McTague, *Regulatory Reform: Pitt, Wilson: Unified Regulatory Structure Needed for U.S. Financial Services Industries*, 87 BANKING REP. (BNA) 682, 682–83 (Nov. 6, 2006) (summarizing comments made by Ms. Williams at a meeting held by a commission on capital markets that was sponsored by the U.S.

preferred approach for protecting consumers was “not public,” and that the OCC did not “do press releases” for most of its consumer compliance efforts.⁶⁷

Because the federal agencies’ bank examinations and other informal supervisory procedures were “highly confidential,” the public could not determine whether regulated institutions actually complied with the 2006 and 2007 interagency statements of guidance.⁶⁸ As discussed below, several of the largest federally-chartered mortgage lenders failed or received federal assistance after engaging in abusive and unsound lending practices that violated both the 2006 and 2007 guidance.⁶⁹ The destructive behavior of those institutions indicated that their managers viewed the interagency statements of guidance as “mere ‘suggestions’” that they could ignore.⁷⁰

D. Federal Regulators Failed to Stop Predatory Lending Because of Their Belief in Deregulation and “Pushback” from the Financial Services Industry

Two factors help to explain why federal regulators failed to stop predatory nonprime lending practices. First, senior federal banking officials doubted the effectiveness of regulation and strongly preferred market-based solutions. Second, financial institutions strongly opposed any attempts by banking agencies to impose restrictions on high-risk mortgage lending.

1. The FRB, the OTS and the OCC Followed Deregulatory Policies During the Nonprime Lending Boom

As shown above, the FRB failed to take measures that could have stopped abusive nonprime lending practices between 1994 and 2008.⁷¹ FRB Chairman Alan Greenspan, who led the FRB from 1987 to 2006, played a decisive role in the FRB’s decisions to refrain from adopting strong rules under HOEPA and to forbear from supervising nonbank mortgage lending subsidiaries of BHCs.⁷² In a 2002 speech, Chairman Greenspan expressed his general view that regulators should seek to minimize any interference with innovation and competition in the financial markets:

Competition, of course, is the facilitator of innovation. And creative destruction, the process by which less-productive capital is displaced with innovative cutting-edge technologies, is the driving force of wealth creation.

Chamber of Commerce).

67. Stephanie Mencimer, *No Account: The Nefarious Bureaucrat Who’s Helping Banks Rip You Off*, NEW REPUBLIC, Aug. 27, 2007, at 14, available at <http://www.tnr.com/article/no-account-O> (quoting from interview with Ms. Williams).

68. McCoy et al., *supra* note 36, at 1350–51; Arthur E. Wilmarth, Jr., *Written Testimony on the Credit Card Industry Before the Subcommittee on Financial Institutions and Consumer Credit of the House Committee on Financial Services* 13–14 (George Washington Univ. Law Sch. Pub. Law & Legal Theory, Working Paper No. 517, 2007) [hereinafter Wilmarth *Written Testimony*], available at <http://ssrn.com/abstract=1729840>.

69. McCoy et al., *supra* note 36, at 1351–56; see also *infra* Part II.E.5 (discussing failures or near failures of large national banks and federal thrifts that engaged in reckless subprime and Alt-A lending).

70. McCoy et al., *supra* note 36, at 1346–47, 1355–57; see also ENGEL & MCCOY, *supra* note 24, at 165 (contending that the 2006 and 2007 guidelines “allowed for slack regulation and permitted lenders to argue that compliance was optional”).

71. See *supra* Parts II.A, II.B, II.C (discussing the FRB’s regulatory failures).

72. See *supra* notes 28–58 and accompanying text (discussing the FRB’s policy decisions).

Thus, from the perspective of aggregate wealth creation, the more competition the better.

....

While regulation must change as financial structures do, such regulatory change must be kept to a minimum to avoid fostering uncertainty among innovators and investors. Moreover, shifting regulatory schemes unavoidably leave obsolescent regulations in their wake

. . . Those of us who support market capitalism in its more-competitive forms might argue that unfettered markets create a degree of wealth that fosters a more civilized existence. I have always found that insight compelling.⁷³

Thus, there was “no truer believer in the ideology of free markets, financial innovation, and deregulation” than Mr. Greenspan.⁷⁴ He doubted whether most government regulation was beneficial, and he championed Joseph Schumpeter’s view that market innovation generated rising standards of living through a process of “creative destruction” that eliminated obsolete businesses and technologies.⁷⁵ In keeping with his deregulatory philosophy, Mr. Greenspan maintained that market discipline and private risk management produced better results than government regulation over the longer term.⁷⁶

FRB officials later confirmed that Mr. Greenspan’s opposition to new regulatory initiatives reflected a broader “mindset” in the Federal Reserve System that favored deregulation during the period leading up to the financial crisis. As FRB General Counsel Scott Alvarez explained, “The mind-set was that there should be no regulation; that the market should take care of policing, unless there already is an identified problem.”⁷⁷ Similarly, in 2009, the Federal Reserve Bank of New York prepared a “lessons learned” report, which acknowledged that federal regulators placed too much faith in the assumption that “markets will always self-correct.”⁷⁸ The report also admitted that the FRB’s belief in “the self-correcting property of markets inhibited supervisors from

73. Alan Greenspan, Chairman, Fed. Reserve Bd., International Financial Risk Management Address before the Council of Foreign Relations (Nov. 19, 2001), *available at* <http://www.federalreserve.gov/boarddocs/speeches/2002/20021119/default.htm>.

74. SIMON JOHNSON & JAMES KWAK, 13 BANKERS: THE WALL STREET TAKEOVER AND THE NEXT FINANCIAL MELTDOWN 100 (2010).

75. ENGEL & MCCOY, *supra* note 24, at 190–91.

76. *Id.* at 191–92. For example, Mr. Greenspan declared in 1997 that “the real question is not whether a market should be regulated. Rather the real question is whether government intervention strengthens or weakens private regulation.” FCIC REPORT, *supra* note 28, at 53–54 (quoting speech by Mr. Greenspan on Feb. 21, 1997). Similarly, Mr. Greenspan proclaimed in 2004 that “regulations that are inconsistent with market realities cannot be sustained indefinitely,” and he praised improvements in private risk management as “hold[ing] out the hope of a safer and stronger banking system contributing to a more stable economy.” Alan Greenspan, Chairman, Fed. Reserve Bd., Banking Address before the American Bankers Association Annual Convention (Oct. 5, 2004), *available at* <http://www.federalreserve.gov/boarddocs/speeches/2004/20041005/default.htm>.

77. FCIC REPORT, *supra* note 28, at 96 (quoting FCIC interview with Mr. Alvarez); *see also* JOHNSON & KWAK, *supra* note 74, at 103 (stating that “Greenspan dominated the Fed during his tenure, and his views became close to dogma on the Board of Governors”).

78. FCIC REPORT, *supra* note 28, at 171 (quoting FED. RESERVE BANK OF NEW YORK, DRAFT, REPORT ON SYSTEMIC RISK AND SUPERVISION 2 (2009)).

imposing prescriptive views on banks.”⁷⁹

Senior officials at the OTS and OCC followed a similar policy of “light touch” regulation during the decade leading up to the financial crisis.⁸⁰ The OTS followed a policy of aggressive deregulation and enthusiastically supported the interests of federal thrifts, which it viewed as the agency’s clients. In 2004, OTS Director James Gilleran affirmed that “[o]ur goal is to allow thrifts to operate with a wide breadth of freedom from regulatory intrusion.”⁸¹ John Reich, who succeeded Mr. Gilleran as OTS Director in 2005, described regulatory relief as his “favorite topic” and “something near and dear to my heart.”⁸²

Eugene Ludwig, who served as Comptroller of the Currency from 1993 to 1998, later explained that the OCC and other federal agencies believed that “a lighter hand at regulation was the appropriate way to regulate.”⁸³ In a speech delivered in May 2005, Acting Comptroller of the Currency, Julie Williams, declared that the OCC’s officials were “advocates on the national stage [for] measures designed to make regulation more efficient, *and* less costly, less intrusive, less complex, and less demanding on [bankers] and [their] resources.”⁸⁴ She added that the OCC’s approach to supervision “is a spacious framework, designed to accommodate change.”⁸⁵ In September 2007, John Dugan, who served as Comptroller from 2005 to 2010, testified at a congressional hearing that the OCC was strongly opposed to legislative or regulatory restrictions on financial “innovations” because “there are many different kinds of innovations that have led to positive things and sorting out which ones are the most positive and somewhat less positive is generally not something that the Federal Government is good at doing.”⁸⁶

Consistent with the OTS’s deregulatory philosophy, the OTS did not issue any formal regulations to stop predatory lending practices.⁸⁷ The OTS also opposed the interagency guidance on nontraditional lending and delayed its adoption for almost a year.⁸⁸ When the guidance was finally issued in September 2006, OTS Director Reich “described the guidance as ‘extremely controversial’ and not something that OTS ‘would have issued on [its] own.’”⁸⁹ Moreover, the OTS brought only “five to six” formal enforcement actions against federal thrifts for “unfair and deceptive practices” between

79. *Id.*

80. ENGEL & MCCOY, *supra* note 24, at 173; McCoy et al., *supra* note 36, at 1353.

81. Binyamin Appelbaum & Ellen Nakashima, *Banking Regulator Played Advocate Over Enforcer: Agency Let Lenders Grow Out of Control, Then Fail*, WASH. POST, Nov. 23, 2008, at A1.

82. ENGEL & MCCOY, *supra* note 24, at 176 (quoting from two speeches by Mr. Reich in 2006); *see also id.* at 183 (stating that “[e]ven in spring 2007, with the subprime market in flames, Reich . . . vowed ‘to pursue additional regulatory relief, to develop support for eliminating as many additional items of regulation as is possible’” and he “went so far as to call greater regulation ‘extremist behavior’”) (quoting speech by Mr. Reich in 2007).

83. FCIC REPORT, *supra* note 28, at 171 (quoting from an interview with Mr. Ludwig).

84. Julie L. Williams, Acting Comptroller of the Currency, Remarks before an OCC Bankers Outreach Meeting 3 (May 27, 2005), available at <http://www.occ.treas.gov/news-issuances/speeches/2005/pub-speech-2005-53.pdf>.

85. *Id.* at 5.

86. ENGEL & MCCOY, *supra* note 24, at 173 (quoting Mr. Dugan’s congressional testimony in Sept. 2007).

87. McCoy et al., *supra* note 36, at 1350.

88. FCIC REPORT, *supra* note 28, at 172–73; Appelbaum & Nakashima, *supra* note 81.

89. ENGEL & MCCOY, *supra* note 24, at 176 (quoting from speech by Mr. Reich in Oct. 2006).

2000 and 2008.⁹⁰

The OCC's record of protecting consumers was only marginally better than the OTS's lamentable performance. The OCC adopted just two substantive rules that were aimed at predatory lending. The first rule prohibited national banks from committing unfair and deceptive acts and practices in mortgage lending,⁹¹ and the second rule barred national banks from making mortgages without regard to the borrower's ability to repay the loan.⁹² However, the OCC greatly weakened the impact of the first rule by stating that it did not have authority to issue regulations proscribing specific practices as unfair or deceptive.⁹³ The OCC also watered down the second rule by stating that national banks could use "any reasonable method to determine a borrower's ability to repay, including . . . credit history, or other relevant factors."⁹⁴ The OCC's statement that national banks could use "credit history, or other relevant factors" to determine a borrower's ability to pay allowed national banks to use "such dubious practices as qualifying borrowers solely based on their credit scores for low-doc or no-doc loans."⁹⁵ As a result, "through 2007, large national banks continued to make large quantities of low- and no-documentation loans and subprime ARMs that were solely underwritten to the introductory [teaser] rate."⁹⁶

Like the OTS, the OCC initiated only a small number of public enforcement actions to protect consumers during the nonprime lending boom. Between 1995 and the outbreak of the financial crisis in 2007, the OCC issued only 13 public enforcement orders against national banks for violations of consumer protection laws.⁹⁷ Most of the OCC's orders were issued against small national banks, and none of the orders were issued against the top eight largest banks, even though large banks were the subject of most of the consumer complaints filed with the OCC.⁹⁸

90. Eric Nalder, *Mortgage System Crumbled While Regulators Josted*, SEATTLE POST-INTELLIGENCER, Oct. 11, 2008, at A1.

91. Bank Activities and Operations; Real Estate Lending and Appraisals, 69 Fed. Reg. 1904, 1916–17 (Jan. 13, 2004) (adopting prohibition codified at 12 C.F.R. §§ 7.4008(c), 34.3(c) (2010)).

92. *Id.* (adopting prohibition codified at 12 C.F.R. §§ 7.4008(b), 34.3(b) (2010)); see also ENGEL & MCCOY, *supra* note 24, at 168 (discussing the OCC's rules).

93. Bank Activities and Operations; Real Estate Lending and Appraisals, 69 Fed. Reg. at 1913 n.55 (stating that "we lack the authority . . . to specify by regulation that particular practices, such as loan 'flipping' or 'equity stripping,' are unfair or deceptive. . . . [T]he OCC does not have rulemaking authority to define specific practices as unfair or deceptive."); see also Arthur E. Wilmarth, Jr., *The OCC's Preemption Rules Exceed the Agency's Authority and Present a Serious Threat to the Dual Banking System and Consumer Protection*, 23 ANN. REV. BANKING & FIN. L. 225, 307 (2004) (contending that the OCC's rule was "greatly weakened" by the agency's disclaimer of any authority to identify specific lending practices as "unfair or deceptive").

94. Bank Activities and Operations; Real Estate Lending and Appraisals, 69 Fed. Reg. at 1916, 1917 (adopting 12 C.F.R. §§ 7.4008(b), 34.3(b) (2010)).

95. ENGEL & MCCOY, *supra* note 24, at 168.

96. McCoy et al., *supra* note 36, at 1353.

97. Wilmarth *Written Testimony*, *supra* note 68, at 14–15; see also Mencimer, *supra* note 67 (reporting that from 2000 to 2007 "the OCC . . . brought just 11 consumer enforcement actions").

98. Wilmarth *Written Testimony*, *supra* note 68, at 14–15; see also *id.* at 18 ("During 2004, ten large banks accounted for four-fifths of all complaints received by the OCC's Consumer Assistance Group.").

2. The Financial Services Industry Strongly Resisted Efforts by Federal Regulators to Restrict Nonprime Mortgage Lending

In addition to the self-imposed obstacles created by deregulatory policies, federal banking regulators encountered intense resistance from the financial services industry whenever they tried to persuade banks to reduce their involvement in high-risk lending. During a congressional hearing in March 2008, FRB Vice Chairman Donald Kohn acknowledged that advice offered by regulators in favor of more conservative lending policies was “a very hard sell to the banks” during the credit boom that led up to the financial crisis.⁹⁹ Similarly, Roger Cole, who served as the FRB’s Director of Bank Supervision from 2006 to 2009, told the FCIC that FRB officials encountered significant “pushback” when they urged bank executives to follow more conservative risk management policies.¹⁰⁰

Banks, thrifts, and nonbank mortgage lenders strongly opposed even the weak and nonbinding regulatory guidance that federal regulators issued in 2006 and 2007 with regard to nontraditional mortgages and hybrid subprime ARMs.¹⁰¹ When the FRB and other federal regulators proposed the nontraditional guidance in late 2005, FRB officials “got tremendous pushback from the industry as well as Congress as well as . . . internally . . . [b]ecause it was stifling innovation, potentially, and it was denying the American dream [of homeownership] to many people.”¹⁰² The American Bankers Association (ABA) asserted that the proposed guidance “overstate[d] the risk of nontraditional mortgages,”¹⁰³ while the Financial Services Roundtable declared that it was “not aware of any empirical evidence that supports the need for further consumer protection standards.”¹⁰⁴ Similarly, when federal regulators proposed the guidance on hybrid subprime ARMs in early 2007, trade associations representing banks, thrifts, and

99. *Bank Supervision: Senators Grill Financial Regulators on Failure to Supervise Banks During Mortgage Crisis*, 90 BANKING REP. (BNA) 435 (Mar. 10, 2008) (quoting Mr. Kohn’s testimony during a hearing before the Senate Banking Committee on Mar. 4, 2008).

100. Mr. Cole noted that

[A] lot of that pushback was given credence . . . by the fact that [firms]—like Citigroup were earning \$4 to \$5 billion per quarter When that kind of money is flowing [in] quarter after quarter after quarter, and their capital ratios are way above the minimums, it’s very hard to challenge.

FCIC REPORT, *supra* note 28, at 307 (quoting from interview with Mr. Cole). Similarly, Richard Spillenkothen, who served as the FRB’s Director of Bank Supervision between 1991 and 2006, explained that the FRB’s prevailing deregulatory philosophy made it very difficult for supervisory officials to impose limits on large financial institutions until they began to report losses: “Supervisors understood that forceful and proactive supervision, especially early intervention *before* management weaknesses were reflected in poor financial performance, might be viewed as i) overly-intrusive, burdensome, and heavy-handed, ii) an undesirable constraint on credit availability, or iii) inconsistent with the Fed’s public posture.” *Id.* at 54 (quoting memorandum by Mr. Spillenkothen) (emphasis added).

101. See *supra* notes 59–70 and accompanying text (discussing 2006 and 2007 guidance).

102. FCIC REPORT, *supra* note 28, at 173 (quoting from interview with Richard Siddique, former head of credit risk for the FRB’s Division of Banking Supervision and Regulation); see also *id.* at 21 (quoting from interview with former FRB Governor Susan Bies, and also quoting Mr. Siddique’s statement that “[t]he ideological turf war lasted more than a year, while the number of nontraditional loans kept growing and growing”).

103. *Id.* (quoting the ABA’s letter of Mar. 29, 2006).

104. *Id.* (quoting the Financial Services Roundtable’s letter of Mar. 29, 2006).

other mortgage lenders argued that the guidance “may restrict credit to many consumers in high-cost areas and deny credit to many deserving low-income, minority, and first-time homebuyers.”¹⁰⁵ The determined opposition of the financial services industry and the deregulatory philosophy of senior regulatory officials combined to block federal banking agencies from taking effective and timely action to stop unsound nonprime lending.¹⁰⁶

The inability of federal regulators to restrain nonprime lending during the housing boom was part of a larger pattern of “regulatory capture,” which caused federal agencies to subordinate consumer protection and other public interests to the overriding policy goal of increasing the profits of major financial institutions.¹⁰⁷ As I pointed out in a recent article:

[R]epeated regulatory failures during past financial crises reflect a ‘political economy of regulation’ in which regulators face significant political and practical challenges that undermine their efforts to discipline [large, complex financial institutions (LCFIs)]. . . . [A]nalysts have pointed to strong evidence of ‘capture’ of financial regulatory agencies by LCFIs during the two decades leading up to the financial crisis, due to factors such as (1) large political contributions made by LCFIs, (2) an intellectual and policy environment favoring deregulation, and (3) a continuous interchange of senior personnel between the largest financial institutions and the top echelons of the financial regulatory agencies.¹⁰⁸

Similarly, Simon Johnson and James Kwak have observed that “regulatory capture is most effective when regulators share the worldview and the preferences of the industry they supervise.”¹⁰⁹ They contend that “the revolving door” for officials moving between the large financial institutions and top government positions created a “confluence of perspectives and opinions between Wall Street and Washington,” in which “Wall Street’s positions became the conventional wisdom in Washington.”¹¹⁰ They further maintain that a symbiotic relationship between financial leaders and senior regulators produced “group-think,” in which (i) “the federal government deferred to the interests of Wall Street repeatedly in the 1990s and 2000s,” and (ii) any officials who disagreed with Wall Street “were marginalized as people who simply did not understand the bright new world of modern finance.”¹¹¹

105. Joe Adler, *Agencies Propose Hybrid Clampdown: Critics Fret over Credit Access*, AM. BANKER, Mar. 5, 2007, at 1 (quoting press release from the Mortgage Bankers Association); see also Cheyenne Hopkins, *Bankers Find Plenty Not to Like in Loan Guidance*, AM. BANKER, May 10, 2007, at 5 (quoting letter from the ABA, stating that the proposed guidance could restrict “credit options to creditworthy borrowers who otherwise would benefit from the flexibility afforded by our banks and savings associations”).

106. JOHNSON & KWAK, *supra* note 74, at 121–50; FCIC REPORT, *supra* note 28, at 20–24, 93–96, 307–08.

107. JOHNSON & KWAK, *supra* note 74, at 82–109, 118–44, 147–50; Bar-Gill & Warren, *supra* note 27, at 85–95; Levitin, *supra* note 17, at 148–61; S. REP. NO. 111-176, at 9–17 (2010).

108. Arthur E. Wilmarth, Jr., *The Dodd–Frank Act: A Flawed and Inadequate Response to the Too-Big-to-Fail Problem*, 89 OR. L. REV. 951, 1011 (2011) (footnotes omitted).

109. JOHNSON & KWAK, *supra* note 74, at 93.

110. *Id.* at 93–97 (quotes at 97).

111. *Id.* at 97; see also *id.* at 103 (describing how then-IMF Chief Economist Raghuram Rajan “was met with a torrent of attacks by Greenspan’s defenders,” including then FRB Vice Chairman Donald Kohn and former Treasury Secretary Lawrence Summers, when “Rajan presented a paper [in August 2005] asking in prophetic tones about whether deregulation and innovation had increased rather than decreased risk in the

E. The OTS and the OCC Preempted Initiatives by the States to Stop Predatory Lending, Thereby Aggravating the Severity of the Financial Crisis

In contrast to the half-hearted measures taken by federal regulators, many states passed laws and brought enforcement actions to combat predatory lending. However, the OCC and the OTS responded to those initiatives by preempting the states’ authority to enforce state consumer protection laws against national banks, federal thrifts, and their subsidiaries and agents. The preemption campaigns of the OCC and the OTS seriously undermined the states’ efforts to protect consumers from abusive nonprime lending practices.

1. Many States Adopted Laws and Brought Enforcement Actions to Stop Predatory Lending

Many states responded to growing evidence of predatory lending by enacting anti-predatory lending (APL) laws—often called “mini-HOEPA” laws—and by taking vigorous enforcement actions against subprime lenders.¹¹² North Carolina passed the first “mini-HOEPA” law in 1999.¹¹³ North Carolina’s statute covered a much broader spectrum of subprime loans than the FRB’s rules under HOEPA.¹¹⁴ North Carolina’s law prohibited prepayment penalties for mortgage loans under \$150,000, forbade patterns of repeated refinancing known as loan “flipping,” and barred lenders from financing single-premium credit insurance as part of the mortgage.¹¹⁵ A number of other states soon copied North Carolina’s approach. By the end of 2007, 30 states and the District of Columbia had adopted APL laws designed to combat various types of mortgage lending abuses.¹¹⁶

Two recent studies determined that state APL laws were effective in reducing the number of mortgage loans with predatory features. The first study found that state APL laws significantly reduced the percentage of mortgages with prepayment penalties, balloon payments, hybrid ARM terms, interest-only ARM terms, and reduced-documentation requirements, all of which were associated with predatory or unsound

financial system”); *id.* at 7–9, 135–36 (explaining that (i) Brooksley Born, then chair of the Commodity Futures Trading Commission (CFTC), “provoked furious opposition” when the CFTC issued a concept paper in May 1998, proposing a study of whether to strengthen the regulation of over-the-counter derivatives; and (ii) Ms. Born’s opponents—including FRB chairman Greenspan, Treasury Secretary Robert Rubin, Treasury Deputy Secretary Lawrence Summers and SEC chairman Arthur Levitt—persuaded Congress to pass legislation barring the CFTC from acting on its proposal).

112. FCIC REPORT, *supra* note 28, at 96–97; Arthur E. Wilmarth, Jr., *Cuomo v. Clearing House: The Supreme Court Responds to the Subprime Financial Crisis and Delivers a Major Victory for the Dual Banking System and Consumer Protection* 21–22 (George Washington Univ. Law Sch. Public Law & Legal Theory, Working Paper No. 479, 2010), available at <http://ssrn.com/abstract=1499216>. I have served as a consultant to state financial regulators over the past three decades.

113. FCIC REPORT, *supra* note 28, at 96.

114. *Id.*

115. *Id.*

116. Raphael W. Bostic et al., *Mortgage Product Substitution and State Anti-Predatory Lending Laws: Better Loans and Better Borrowers?* 7 n.2 (Univ. Pa. Inst. & Econ., Research Paper No. 09-27, 2009), available at <http://ssrn.com/abstract=1460871>; Lei Ding et al., *The Impact of State Anti-Predatory Lending Laws on the Foreclosure Crisis 4* (June 30, 2010) (unpublished manuscript), available at <http://ssrn.com/abstract=1632915>.

loans.¹¹⁷ The second study determined that borrowers in states with APL laws were substantially less likely to receive mortgages with risky terms (including prepayment penalties) and also had a significantly lower rate of default on their loans.¹¹⁸ The authors concluded that “[t]his study provides strong evidence that state regulation of subprime mortgages can serve as an important tool in the landscape of mortgage market regulation and consumer protection.”¹¹⁹

In addition to passing APL laws, states launched thousands of enforcement actions against abusive lending practices, including more than 3600 enforcement actions in both 2003 and 2006.¹²⁰ State enforcement efforts produced several consent orders that required nonbank mortgage lenders to pay large penalties, including a settlement that required Household to pay \$484 million, an agreement that forced Ameriquest to pay \$325 million, a settlement that compelled First Alliance to pay more than \$50 million, and a consent order that required Countrywide to pay \$150 million and provide more than \$8 billion in mortgage modifications to borrowers.¹²¹ However, as discussed in the next Part, state laws and state enforcement actions were not able to eradicate predatory lending because the OTS and the OCC preempted the states’ ability to act against federal thrifts, national banks, and their subsidiaries and agents.

2. The OTS and the OCC Preempted State APL Laws and State Enforcement Efforts

In 1996, the OTS issued a regulation governing the real estate lending activities of federal thrifts.¹²² The regulation declared that “OTS hereby occupies the entire field of lending regulation for federal savings associations.”¹²³ Thus, the regulation was designed to preempt all state laws that affected the terms and conditions of real estate loans made by federal thrifts.¹²⁴ The OTS issued another regulation in 1996 that gave operating subsidiaries of federal thrifts the same preemptive immunity from state laws as the parent thrifts enjoyed under the OTS rules.¹²⁵ The 1996 rules enabled federal thrifts and their subsidiaries to make residential mortgage loans without complying with state consumer protection laws.¹²⁶

117. Bostic et al., *supra* note 116, at 24.

118. Ding et al., *supra* note 116, at 18–20.

119. *Id.* at 14–20.

120. Wilmarth, *supra* note 93, at 316 (summarizing House of Representatives committee document indicating that during 2003 state officials “performed more than 20,000 investigations in response to consumer complaints about abusive lending practices, and those investigations produced more than 4000 enforcement actions”); Nalder, *supra* note 90 (reporting that state officials “took 3694 enforcement actions against mortgage lenders and brokers in 2006 alone”).

121. Testimony of Illinois Attorney General Lisa Madigan before the FCIC, Jan. 14, 2010, at 4–6, available at <http://www.fcic.gov/hearings/pdfs/2010-0114-Madigan.pdf> [hereinafter Madigan FCIC Testimony]; Wilmarth, *supra* note 93, at 316; Nalder, *supra* note 90.

122. Lending and Investment, 61 Fed. Reg. 50,951 (Sept. 30, 1996).

123. *Id.* at 50,972 (codified at 12 C.F.R. § 560.2(a) (2008)).

124. See Wilmarth, *supra* note 93, at 284–85 (discussing 12 C.F.R. § 560.2).

125. See *WFS Fin., Inc. v. Dean*, 79 F. Supp. 2d 1024, 1028 (W.D. Wis. 1999) (upholding 1996 OTS regulation extending preemption to operating subsidiaries of federal thrifts).

126. McCoy et al., *supra* note 36, at 1348–49. The OTS regulation permitted certain state laws of general applicability, including contract and tort laws, to apply to federal thrifts if such laws had only an “incidental” effect on the lending operations of federal thrifts. Wilmarth, *supra* note 93, at 285.

After the states began to adopt APL laws, the OTS issued a series of orders declaring that state APL laws were preempted by OTS regulations and, therefore, did not apply to federal thrifts and their operating subsidiaries. For example, the OTS Chief Counsel issued four opinion letters in 2003, declaring that OTS regulations preempted mini-HOEPA laws passed by Georgia, New York, New Jersey, and New Mexico.¹²⁷ In the New Mexico opinion, the OTS Chief Counsel declared that the OTS’s regulations preempted numerous provisions of the New Mexico statute, including New Mexico’s prohibitions against balloon payments, negative amortization, prepayment penalties, loan flipping, and lending without regard to the borrower’s ability to repay.¹²⁸ The OTS also issued orders exempting agents of federal thrifts from their duty to comply with state laws.¹²⁹ Thus, the OTS shielded federal thrifts and their subsidiaries and agents from complying with state APL laws.

The OCC soon joined the OTS’s efforts to bar the states from taking any action to restrict nonprime lending by federally-chartered depository institutions. In August 2003, the OCC issued an order declaring that Georgia’s mini-HOEPA statute, the Georgia Fair Lending Act (GFLA) did not apply to national banks and their operating subsidiaries.¹³⁰ At the same time, the OCC proposed sweeping preemption rules that would apply across-the-board to all state laws that interfered with or placed conditions on the ability of national banks to exercise their federally-granted powers as defined by the OCC.¹³¹ In January 2004, the OCC adopted the proposed blanket preemption rules, which were substantially identical to the OTS’s 1996 regulations.¹³² Like the OTS’s regulations, the OCC’s 2004 preemptive rules shielded both national banks and their operating subsidiaries from the application of most state consumer protection laws.¹³³

Also in January 2004, the OCC adopted a separate but related preemption rule. That

127. Letter from Carolyn J. Buck, Chief Counsel, Office of Thrift Supervision, Dep’t of Treasury (Jan. 21, 2003), available at http://www.ots.treas.gov/_files/56301.pdf (concluding that federal law preempted the Georgia Fair Lending Act); Letter from Carolyn J. Buck, Chief Counsel, Office of Thrift Supervision, Dep’t of Treasury (Jan. 30, 2003), available at http://www.ots.treas.gov/_files/56302.pdf (concluding that federal law preempted the New York Predatory Lending Law); Letter from Carolyn J. Buck, Chief Counsel, Office of Thrift Supervision, Dep’t of Treasury (July 22, 2003), available at http://www.ots.treas.gov/_files/56305.pdf (concluding that federal law preempted the New Jersey Predatory Lending Act); Letter from Carolyn J. Buck, Chief Counsel, Office of Thrift Supervision, Dep’t of Treasury (Sept. 2, 2003), available at http://www.ots.treas.gov/_files/56306.pdf (concluding that federal law preempted the New Mexico Home Loan Protection Act).

128. Letter from Carolyn J. Buck, Chief Counsel, Office of Thrift Supervision, Dep’t of Treasury (Sept. 2, 2003), available at http://www.ots.treas.gov/_files/56306.pdf (noting that “[m]any of [New Mexico’s] statutory provisions] are the same as, or similar to, provisions of these other states’ predatory lending laws”).

129. See *State Farm Bank, FSB v. Reardon*, 539 F.3d 336, 349 (6th Cir. 2008) (upholding an OTS order that permitted agents of a federal thrift to offer mortgage loans in Ohio without complying with Ohio’s laws governing mortgage brokers).

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

131. Bank Activities and Operations; Real Estate Lending and Appraisals, 68 Fed. Reg. 46,119 (Aug. 5, 2003) (to be codified at 12 C.F.R. pt. 7, 34).

132. Bank Activities and Operations; Real Estate Lending and Appraisals, 69 Fed. Reg. 1904 (Jan. 13, 2004). For a description of the OCC’s 2004 rules and their similarity to the OTS’s rules, see Wilmarth, *supra* note 93, at 227–36, 298–99.

133. See Bar-Gill & Warren, *supra* note 27, at 81–82, 92 (concluding that the “regulation cancels out much state-level consumer protection law”); McCoy et al., *supra* note 36, at 1349–50 (discussing the broad preemptive impact of the OCC rule); Wilmarth, *supra* note 93, at 233–36 (same).

rule preempted the authority of the states to bring any type of enforcement action (whether administrative or judicial) against national banks, even with respect to state laws that the OCC did not preempt.¹³⁴ In combination, the OCC's 2004 rules: (i) exempted national banks from compliance with most state consumer protection laws, and (ii) prevented the states from enforcing other state laws that still applied to national banks.¹³⁵ In May 2004, the OCC took a further step and declared that the GFLA's regulation of mortgage brokers was preempted with respect to any brokers who arranged loans that were funded at closing by national banks or their subsidiaries.¹³⁶ That ruling effectively canceled the states' ability to regulate mortgage brokers who worked with national banks or their subsidiaries.

In addition to issuing its preemption rules, the OCC supported lawsuits brought by national banks to preempt state laws and state enforcement actions.¹³⁷ For example, during protracted litigation over the issue of whether national banks could charge late payment fees on credit card loans extended to residents of other states, the OCC issued a regulation in 1996 that authorized national banks to disregard conflicting state usury laws.¹³⁸ The Court granted deference to the OCC's regulation,¹³⁹ while noting that (i) the regulation was "prompted by litigation, including this very suit,"¹⁴⁰ and (ii) the OCC also "participated as an *amicus curiae* on the side of the banks."¹⁴¹ During oral argument, Chief Justice Rehnquist provoked laughter in the courtroom when he remarked to counsel for the United States that "I've been on the Court 23 or 24 years and heard a number of these cases. And I've never heard of a case in which the [OCC] ruled against the banks."¹⁴²

134. Bank Activities and Operations, 69 Fed. Reg. 1895 (Jan. 13, 2004) (to be codified at 12 C.F.R. pt. 7). For a description of this rule, see Wilmarth, *supra* note 93, at 228–29.

135. See McCoy et al., *supra* note 36, at 1349–50 (discussing impact of the preemptive rules issued by the OTS and OCC); see also Bar-Gill & Warren, *supra* note 27, at 81–82, 92 (same).

136. See Wilmarth, *supra* note 112, at 22 n.105 (citing OCC Interpretive Letter No. 1002, May 13, 2004, from Comptroller of the Currency John D. Hawke, Jr. to Georgia Banking Commissioner David G. Sorrell).

137. See Wilmarth, *supra* note 93, at 289–92 (explaining that "the OCC and national banks have used a coordinated litigation strategy to expand the preemptive reach of the [National Bank Act]"). An informal survey determined that the OCC filed amicus briefs in sixty court cases between 1994 and 2006, and that the OCC supported the positions taken by national banks in all but two of those cases. Mencimer, *supra* note 67 (describing results of survey).

138. *Smiley v. Citibank (South Dakota), N.A.*, 517 U.S. 735, 739–41 (1996) (discussing the OCC's adoption of 12 C.F.R. § 7.4001(a)). Under 12 U.S.C. § 85, a national bank that is "located" in one state may charge "interest" permitted by the laws of that state on loans made to residents of other states, notwithstanding the usury laws of those other states. The OCC's regulation at issue in *Smiley* allowed national banks to treat late payment fees and certain other charges as "interest" for purposes of § 85. *Id.* at 740; see also Wilmarth *Written Testimony*, *supra* note 68, at 7–8 (discussing the ability of national banks, under 12 U.S.C. § 85, to "export" interest rates on loans made to residents of other states).

139. *Smiley*, 517 U.S. at 739–47 (granting deference to the OCC's regulation under *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984)).

140. *Id.* at 741.

141. *Id.* at 740.

142. Transcript of Oral Argument at 16–17, *Smiley v. Citibank*, No.95-860, 1996 WL 220402 (U.S. Apr. 24, 1996). When Chief Justice Rehnquist asked counsel for the United States whether he knew of any rulings by the OCC against national banks, the only example provided by counsel was that the OCC's regulation at issue in *Smiley* allowed national banks to treat some—but not all—loan-related fees and charges as "interest" that could be "exported" to borrowers across state lines under 12 U.S.C. § 85. *Id.* at 17 (response by Irving L.

Subsequently, the OCC issued opinion letters and filed amicus briefs in support of three large national banks—Wachovia, Wells Fargo, and National City—that filed lawsuits to preempt efforts by several states to regulate the mortgage lending subsidiaries of national banks.¹⁴³ Those lawsuits produced court decisions upholding preemption of the challenged state laws.¹⁴⁴ However, as discussed below, Wachovia and National City subsequently suffered heavy losses from their nonprime lending activities and both institutions ultimately agreed to sell themselves to other banks in federally-assisted transactions in order to avoid failure.¹⁴⁵

In June 2005, the OCC joined with the Clearing House Association (an association of the largest national banks) in filing lawsuits to prevent New York Attorney General Eliot Spitzer from investigating national banks for alleged violations of New York’s fair lending statute.¹⁴⁶ The OCC conceded that New York’s antidiscrimination law applied to national banks, but the OCC claimed sole and exclusive authority to decide whether that law should be enforced against national banks.¹⁴⁷ With the OCC’s support, the national banks persuaded a federal district court to enjoin Mr. Spitzer’s investigation and that injunction was not lifted until the U.S. Supreme Court reversed the lower court’s decision in June 2009.¹⁴⁸ Once again, the OCC’s preemptive actions frustrated a state’s efforts to protect its citizens from abusive lending practices.

A 2008 investigative report by two journalists concluded that the OCC’s preemptive measures contributed to the severity of the financial crisis by “stifling . . . prescient state enforcers and legislators” who tried to prevent irresponsible lending.¹⁴⁹ Another journalist similarly observed:

For more than a decade, the O.C.C. has beaten back state attorney generals who have tried to enforce state consumer laws against national banks, arguing that federal laws pre-empt those of the states: the O.C.C. has stopped Georgia from enforcing predatory lending laws, intervened in New York’s effort to investigate discriminatory lending and opposed a campaign by New England states to curb gift card fees.

Gornstein, noting that “the banks would like to have all of [the charges] treated as interest so that they could be exported”). I am indebted to Alan Morrison, who attended the oral argument in *Smiley*, for alerting me to Chief Justice Rehnquist’s remarks and the laughter in the courtroom that followed.

143. See *Watters v. Wachovia Bank, N.A.*, 550 U.S. 1 (2007) (holding that federal law preempted the application of state mortgage lending laws to operating subsidiaries of national banks); *Nat’l City Bank of Ind. v. Turnbaugh*, 463 F.3d 325 (4th Cir. 2006), *cert. denied*, 550 U.S. 913 (2007) (same); *Wells Fargo Bank, N.A. v. Bourtris*, 419 F.3d 949 (9th Cir. 2005) (same); *Wachovia Bank, N.A. v. Burke*, 414 F.3d 305 (2d Cir. 2005), *cert. denied*, 550 U.S. 913 (2007) (same).

144. See *supra* note 143 (listing four preemption cases in which the OCC supported large national banks).

145. See *infra* notes 195–96 and accompanying text (referring to forced sales of Wachovia and National City).

146. Wilmarth, *supra* note 112, at 4–5.

147. *Id.* at 5.

148. See *id.* at 5–6, 11–12 (describing legal and factual background leading to the Supreme Court’s decision in *Cuomo v. Clearing House Ass’n, L.L.C.*, 129 S. Ct. 2710 (2009)).

149. Robert Berner & Brian Grow, *They Warned Us: The Watchdogs Who Saw the Subprime Disaster Coming—and How They Were Thwarted by the Banks and Washington*, BUS. WEEK, Oct. 20, 2008, at 36, 38, available at, <http://legacy.sabrew.info/contest/2008/entries/5334END/The%20Watchdogs%20Who%20Warned%20Us.pdf>.

...

CRITICS maintain that the O.C.C.'s campaign against the states weakened crucial consumer protections and ultimately exacerbated the impact of the financial crisis.¹⁵⁰

In written testimony presented to the FCIC in January 2010, Illinois Attorney General Lisa Madigan maintained that “[s]tate enforcement efforts have been progressively hamstrung by the dual forces of federal preemption and a lack of oversight at the federal level.”¹⁵¹ Attorney General Madigan contended that OCC and OTS preemption had three adverse effects on the states’ ability to enact and enforce consumer protection laws. First, “when state attorneys general come upon lending abuses by federally chartered lenders, we first have to determine whether we can afford to expend our limited resources fighting a protracted preemption battle.”¹⁵² Second, “most of the remaining mortgage lenders are now sheltering under the protections of federal charters.”¹⁵³ For example, Attorney General Madigan pointed out that Countrywide moved all of its mortgage lending operations into its federal thrift subsidiary in 2007 in order to obtain the protection of federal preemption against future state investigations and enforcement proceedings.¹⁵⁴ Third, federal preemption made it more difficult for states to enact protective legislation, because “[w]hen we introduced legislation, mortgage brokers and other state licensees were quick to respond with the ‘level playing field’ argument, demanding that they should be subject to the same lax standards as federal charters.”¹⁵⁵

The preemptive actions of the OCC and OTS prevented state officials from responding to predatory lending problems with the same effectiveness they displayed in exposing a series of scandals on Wall Street between 2002 and 2006. During those years, state authorities took the lead in prosecuting securities firms (including securities affiliates of major banks) for (i) pressuring their research analysts to produce biased reports to investors, (ii) engaging in corrupt practices related to initial public offerings, and (iii) permitting hedge funds to carry out abusive market timing and late trading strategies that exploited mutual funds sponsored by securities firms.¹⁵⁶ After initial resistance, the Securities and Exchange Commission (SEC) eventually cooperated with

150. Andrew Martin, *Does This Bank Watchdog Have a Bite?*, N.Y. TIMES, Mar. 28, 2010, at BU.

151. Madigan FCIC Testimony, *supra* note 121, at 9.

152. *Id.* at 11.

153. *Id.*; see also *infra* note 183 and accompanying text (citing examples of nonbank subprime lenders that sold themselves to national banks to gain preemptive immunity from state enforcement).

154. Madigan FCIC Testimony, *supra* note 121, at 6 (noting that, in 2008, Illinois and several other states obtained a large settlement requiring Countrywide to take remedial actions for past violations of state consumer protection laws; however, the states were not able to secure “mandatory injunctive provisions governing [Countrywide’s] future lending practices” because Countrywide transferred its mortgage lending operations to its subsidiary federal thrift).

155. *Id.* at 11; see also ENGEL & MCCOY, *supra* note 24, at 162 (noting that “in response to the OCC and OTS preemption rules, state banks and thrifts lobbied regulators for the same hands-off treatment so they would have competitive parity with their federally chartered counterparts”).

156. See Renee M. Jones, *Dynamic Federalism: Competition, Cooperation and Securities Enforcement*, 11 CONN. INS. L. J. 107, 117–21 (2005) (discussing recent scandals); Wilmarth, *supra* note 93, at 348–52; Wilmarth, *supra* note 19, at 1000–02 (commenting on how the OCC’s rules undermine the enforcement of consumer protection laws).

the states’ enforcement measures against Wall Street firms.¹⁵⁷ In contrast, as shown above, the determined preemption campaigns of the OTS and the OCC frustrated the efforts of the states to combat abusive nonprime lending.¹⁵⁸

3. *The Industry-Based Funding for the OTS and OCC Created a Conflict of Interest Between Their Supervisory Duties and Their Budgetary Concerns*

The preemption initiatives of the OTS and the OCC served the financial self-interest of both agencies.¹⁵⁹ The budgets of the OCC and the OTS were funded almost entirely by assessments paid by national banks and federal thrifts.¹⁶⁰ Both agencies therefore had powerful budgetary incentives to persuade depository institutions to operate under national bank and federal thrift charters.¹⁶¹

During the period leading up to the financial crisis, the OTS and the OCC actively competed for chartering rights with state officials who regulated state-chartered banks and state-chartered thrifts.¹⁶² In a newspaper interview in 2002, Comptroller of the Currency John D. Hawke, Jr. acknowledged that “the potential loss of regulatory market share [to the state banking system] ‘was a matter of concern to us.’”¹⁶³ Similarly, in 2007 OTS Director John Reich described Washington Mutual, the largest thrift institution, as “my largest constituent” in an email message.¹⁶⁴

Preemption “gave the OCC and OTS a powerful extra lure to entice lenders to their charters, in the form of relief from state anti-predatory lending laws.”¹⁶⁵ The OTS’s sweeping preemption rules, along with its nationwide branching regulations, persuaded most state-chartered thrifts to convert to federal charters between 1975 and 2003.¹⁶⁶ Similarly, the OCC’s preemption initiatives were intended to induce large, multistate

157. Jones, *supra* note 156, at 118–21; Stefania A. Di Trolio, *Public Choice Theory, Federalism and the Sunny Side to Blue Sky Laws*, 30 WM. MITCHELL L. REV. 1279, 1281, 1305–07; Wilmarth, *supra* note 93, at 348–52.

158. See *supra* notes 122–55 and accompanying text (discussing impact of the OTS’s and OCC’s preemptive rules).

159. ENGEL & MCCOY, *supra* note 24, at 158–61.

160. The Dodd–Frank Act abolishes the OTS and transfers its functions to the other federal banking regulators, effective on July 21, 2011. The OCC will inherit the OTS’s responsibility for regulating federal thrifts, while the FDIC will assume responsibility for regulating state-chartered thrifts and the FRB will take over responsibility for regulating thrift holding companies. See H.R. REP. NO. 111-517, at 866 (2010) (Conf. Rep.), reprinted in 2010 U.S.C.C.A.N. 722, 723, available at <http://www.gpo.gov/fdsys/pkg/CRPT-111hrpt517/pdf/CRPT-111hrpt517.pdf>; Cheyenne Hopkins, *On Foreign Soil, Acting OTS Head Criticizes Reform*, AM. BANKER, Nov. 18, 2010, at 7; Cheyenne Hopkins, *Under New Management, Thrifts Must Get in Line*, AM. BANKER, Feb. 4, 2011, at 1.

161. Bar-Gill & Warren, *supra* note 27, at 93–94; ENGEL & MCCOY, *supra* note 24, at 158–61; Wilmarth, *supra* note 93, at 276–77; Wilmarth, *supra* note 112, at 20, 23.

162. ENGEL & MCCOY, *supra* note 24, at 158–61; Wilmarth, *supra* note 93, at 274–86.

163. Jess Bravin & Paul Beckett, *Friendly Watchdog: Federal Regulator Often Helps Banks Fighting Consumers*, WALL ST. J., Jan. 28, 2002, at A1 (summarizing and quoting from an interview with Mr. Hawke).

164. Binyamin Appelbaum, *Onetime Cop, Out of Business*, N.Y. TIMES, July 14, 2010, at B1.

165. ENGEL & MCCOY, *supra* note 24, at 159.

166. Wilmarth, *supra* note 93, at 280–87 (contending that “[t]he most likely reason for the disintegration of the state-chartered thrift system is the aggressive preemption campaign that the [Federal Home Loan Bank Board (FHLBB)] began in the late 1970s and the OTS continued after assuming the FHLBB’s functions in 1989”).

banks to convert from state charters to national bank charters.¹⁶⁷ In a 2002 speech, Comptroller Hawke declared that “national banks’ immunity from state law is a significant benefit of the national charter—a benefit that the OCC has fought hard over the years to preserve.”¹⁶⁸ He further claimed that “[t]he ability of national banks to conduct a multistate business subject to a single, uniform set of federal laws, under the supervision of a single regulator, free from visitorial powers of various state authorities, is a major advantage of the national charter.”¹⁶⁹

The OCC’s subsequent issuance of broad preemption rules in 2004 had the desired effect. By 2005, three major banks with more than \$1 trillion of assets had converted from state charters to national charters to take advantage of the OCC’s rules.¹⁷⁰ Those conversions provided a significant financial benefit to the OCC, as they produced a 15% increase in the OCC’s annual budget.¹⁷¹ The OTS and OCC preemption rules continued to encourage state thrift and state banks to convert to federal charters until the outbreak of the financial crisis in 2007.¹⁷²

4. OTS and OCC Preemption Helped Federal Thrifts and National Banks to Establish Leading Positions as Subprime and Alt-A Mortgage Lenders

OTS preemption helped federal thrifts to establish a major presence in the subprime and Alt-A mortgage markets during the late 1990s and early 2000s. In 1999, Washington Mutual (WaMu), the largest federal thrift, acquired Long Beach, a major subprime lender.¹⁷³ Two other large federal thrifts, IndyMac and Downey Federal, also rapidly expanded their nonprime lending operations.¹⁷⁴ In addition, three major securities firms—Merrill Lynch, Lehman Brothers, and Morgan Stanley—each acquired a federal thrift,¹⁷⁵ as did AIG, a big insurance company,¹⁷⁶ and H&R Block, a large tax preparation firm.¹⁷⁷ All eight of the foregoing companies were subject to OTS regulation

167. S. REP. NO. 111-176, at 16 (2010) (“At a hearing on the OCC’s preemption rule, Comptroller Hawke acknowledged, in response to questioning from Senator Sarbanes, that one reason Hawke issued the preemption rule was to attract additional charters, which helps to bolster the budget of the OCC.”); *see also* Wilmarth, *supra* note 93, at 275 (observing that “the OCC evidently concluded that an aggressive preemption campaign—promising freedom from state regulation— . . . will persuade large, multistate banks to operate under national charters”).

168. John D. Hawke, Jr., Comptroller of the Currency, Remarks Before the Women in Housing and Finance 2 (Feb. 12, 2002), *available at* <http://www.occ.gov/static/news-issuances/speeches/2002/pub-speech-2002-10.pdf>.

169. *Id.* In a contemporaneous interview, Comptroller Hawke confirmed that preemption “is one of the advantages of the national charter, and I’m not the least bit ashamed to promote it.” Bravin & Beckett, *supra* note 163 (quoting from interview with Mr. Hawke).

170. Bar-Gill & Warren, *supra* note 27, at 81–83, 92–94 (describing conversions of JP Morgan Chase, HSBC, and Bank of Montreal from state to national charters in response to the OCC’s adoption of its 2004 preemption rules).

171. *Id.* at 94.

172. ENGEL & MCCOY, *supra* note 24, at 161.

173. Wilmarth, *supra* note 19, at 1017.

174. ENGEL & MCCOY, *supra* note 24, at 176–80.

175. Wilmarth, *supra* note 19, at 977–78.

176. ENGEL & MCCOY, *supra* note 24, at 221–23.

177. *Id.* at 26.

due to their status as federal thrifts or owners of federal thrifts.¹⁷⁸ The OTS exercised primary supervision over federal thrifts, and the OTS also exercised consolidated supervision over all holding companies that owned federal thrifts, including financial conglomerates whose principal subsidiaries were securities broker-dealers or insurance companies.¹⁷⁹

Similarly, large national banks expanded aggressively into subprime and Alt-A lending and took full advantage of the preemptive shield offered by the OCC. Citigroup acquired Associates First Capital in 2000 and purchased Argent (an affiliate of Ameriquest) in 2007.¹⁸⁰ Similarly, National City, a leading Midwestern bank, bought First Franklin in 1999, while Chase purchased Advanta in 2001, and HSBC acquired Household in 2002.¹⁸¹ In addition, Countrywide, the largest mortgage lender, acquired a national bank in 2001 and operated as a bank holding company until it converted its bank charter to a federal thrift charter in early 2007.¹⁸² In several instances, nonbank subprime lenders sold themselves to national banks or federal thrifts, after they were sued by state regulators, in order to obtain the immunity from state regulation offered by the OCC’s or OTS’s preemptive shield.¹⁸³

The Center for Public Integrity (CPI) published a study in May 2009, which compiled a list of the top 25 subprime lenders from 2005 through 2007.¹⁸⁴ CPI’s data showed that the top 25 subprime lenders and their affiliates accounted for 72% of all subprime loans made between 2005 and 2007.¹⁸⁵

According to CPI’s study, at the peak of the subprime lending boom between 2005 and 2007, the following 6 companies that owned federal thrifts ranked among the top 20 subprime lenders in the nation: Merrill Lynch, WaMu, H&R Block, Lehman Brothers,

178. FCIC REPORT, *supra* note 28, at 150–51, 178, 306, 350–51; McCoy et al., *supra* note 36, at 1352–53, 1365–66; Wilmarth, *supra* note 112, at 26–27.

179. U.S. Government Accountability Office, *Financial Market Regulation: Agencies Engaged in Consolidated Supervision Can Strengthen Performance Measurement and Collaboration*, GAO-07-154 (Mar. 2007), at 9–14, 20–22, 25–29 [hereinafter GAO Consolidated Supervision Report (2007)].

180. FCIC REPORT, *supra* note 28, at 92, 164; Wilmarth, *supra* note 19, at 1017–18.

181. Wilmarth, *supra* note 19, at 1017–18.

182. *Id.* at 1018; ENGEL & MCCOY, *supra* note 24, at 200–02.

183. Wilmarth, *supra* note 112, at 22–23 (citing the sales of Household to HSBC, Ameriquest (Argent) to Citigroup, and Okoboji Mortgage to Wells Fargo). In addition, Providian, a major subprime credit card lender, sold most of its assets to JP Morgan Chase and WaMu after settling a state enforcement action. Dan Richman, *New Acquisition for WaMu: Providian Deal Aims to Speed Firm’s Credit Card Program*, SEATTLE POST-INTELLIGENCER, June 7, 2005, at C1; *see also* Madigan FCIC Testimony, *supra* note 121, at 6 (discussing Countrywide’s transfer of its mortgage lending operations to its federal thrift subsidiary in order to take advantage of the OTS’s preemption rules).

184. David Donald, *Who’s Behind the Financial Meltdown?*, *Methodology*, CENTER FOR PUB. INTEGRITY, http://www.publicintegrity.org/investigations/economic_meltdown/about_this_project/methodology/ (last visited Apr. 13, 2011). The CPI’s study was based on methodology and supporting data developed by Chris Mayer of the Columbia Business School and Karen Pence, a FRB economist. The CPI’s study drew on data from (i) reports filed by banks, thrifts and other mortgage lenders under the Home Mortgage Disclosure Act (“HMDA”), (ii) data on subprime lenders compiled by HUD, and (iii) data collected by private-sector sources for use in the real estate industry. *Id.*

185. Jonn Dunbar & David Donald, *Who’s Behind the Financial Meltdown?*, Article on *The Roots of the Financial Crisis: Who Is to Blame?*, CENTER FOR PUB. INTEGRITY, http://www.publicintegrity.org/investigations/economic_meltdown/articles/entry/1286/ (last visited Apr. 13, 2011) (listing the top subprime lenders in “The Subprime 25”).

IndyMac, and AIG.¹⁸⁶ In addition, Countrywide, the nation's largest subprime lender, switched the charter of its subsidiary depository institution from a national bank to a federal thrift in early 2007.¹⁸⁷

Several major national banks were also affiliated with leading subprime lenders. According to CPI's study, during the peak of the subprime lending boom from 2005 to 2007, 7 of the nation's top 20 subprime lenders—Countrywide (until early 2007), National City, Wells Fargo, HSBC, JP Morgan Chase, Citigroup, and Wachovia—were companies that owned national banks.¹⁸⁸

In sum, CPI's study showed that 12 of the 20 largest subprime lenders from 2005 to 2007 were companies that owned either national banks or federal thrifts.¹⁸⁹ During the same period, those 12 lenders accounted for almost 60% of the subprime loans made by the top 25 subprime lenders and for more than 40% of the subprime loans made by all subprime lenders.¹⁹⁰ A second study, prepared by the National Consumer Law Center (NCLC), found that national banks, federal thrifts, and their operating subsidiaries originated 31.5% of all subprime mortgages, 40.1% of all Alt-A mortgages, and 51% of all payment-option and interest-only ARMs in 2006, the high point of the housing boom.¹⁹¹ Thus, national banks, federal thrifts, and their affiliates were responsible for a large share of the nonprime lending that occurred during the housing boom.

5. The OTS, the OCC, and the FRB Failed to Prevent the Failures of Several Major Financial Institutions That Were Heavily Engaged in Originating and Securitizing Nonprime Mortgages

The failures and government bailouts of several major companies that owned national banks or federal thrifts revealed (i) the deep involvement of large federal thrifts and national banks in the origination and securitization of nonprime mortgages, and (ii) serious regulatory failures by the OTS, the OCC and the FRB. The OTS committed numerous regulatory lapses, and Congress ultimately decided, in enacting Dodd–Frank, to abolish the OTS and transfer its functions to other federal regulators.¹⁹² The OTS's regulatory failures contributed to (A) the failures of IndyMac, Lehman Brothers, and

186. *Id.*

187. *Id.*; see also ENGEL & MCCOY, *supra* note 24, at 159–60, 201–02 (describing Countrywide's status as a top subprime lender and its charter conversion); FCIC REPORT, *supra* note 28, at 107–08, 172–74 (same).

188. Dunbar & Donald, *supra* note 185.

189. *Id.* While 14 owners of federally-chartered depository institutions were listed among the top subprime lenders, there was an overlap in the case of two subprime lenders, because (i) Countrywide was a national bank until early 2007 and a federal thrift thereafter, until it was acquired by Bank of America in early 2008, and (ii) First Franklin was owned by National City until late 2006 and was then owned by Merrill Lynch until 2008. *Id.*

190. *Id.* (showing that lenders affiliated with national banks and federal thrifts accounted for \$567 billion of the \$972 billion of subprime loans originated by the top 25 subprime lenders between 2005 and 2007; also noting that the top 25 subprime lenders accounted for 72% of all subprime loans during that period).

191. *Preemption and Regulatory Reform: Restore the States' Traditional Role as "First Responder"*, NAT'L CONSUMER L. CTR. 11–13 (2009), available at <http://www.nclc.org/images/pdf/preemption/restore-the-role-of-states-2009.pdf>. The NCLC study was based on loan data provided by *Inside Mortgage Finance*, a leading mortgage industry publication. *Id.* at 11–13 tbls. 1–3.

192. S. REP. NO. 111-176, at 25–26 (2010); H.R. REP. NO. 111-517, at 866 (2010) (Conf. Rep.), reprinted in 2010 U.S.C.C.A.N. 722, 723; see also *supra* note 160 (discussing Dodd–Frank's transfer of the OTS's responsibilities to the OCC, the FRB, and the FDIC).

WaMu, (B) the collapse of AIG, which triggered a massive federal bailout, and (C) the near-failure of Merrill Lynch, which resulted in an emergency takeover by Bank of America—a transaction that in turn inflicted major losses on Bank of America and forced that bank to obtain extraordinary assistance from the federal government.¹⁹³

The OCC, the FRB, and the OTS bore joint responsibility for the near-failure of Countrywide, which sold itself in an emergency deal to Bank of America and subsequently inflicted additional losses on its acquirer.¹⁹⁴ The FRB and the OCC were also cited for failures of regulatory oversight that led to (i) the near-failure and costly federal bailout of Citigroup, (ii) the failure and forced sale of Wachovia to Wells Fargo in a federally-assisted transaction, and (iii) the near-collapse and forced sale of National City to PNC in another federally-assisted deal.¹⁹⁵ The failures and governmentally-assisted rescues of the foregoing institutions made it “painfully obvious” that federally-supervised thrifts and banks “were deeply implicated in the origination and securitization of bad mortgage loans, whether through the banks themselves or their nonbank affiliates.”¹⁹⁶

A recent study by Kathleen Engel and Patricia McCoy concluded that federal preemption contributed to unsound lending and higher rates of mortgage defaults among federally-chartered depository institutions.¹⁹⁷ Their study analyzed delinquency rates on residential mortgage loans made by four categories of depository institutions between 2006 and 2008.¹⁹⁸ The authors found that loans made by federal thrifts had the highest delinquency rate, while loans made by national banks had the second highest delinquency rate.¹⁹⁹ In contrast, loans made by state-chartered thrifts and state-chartered banks—which were not protected by federal preemption—had substantially lower delinquency rates (with state banks recording the lowest rates).²⁰⁰ The authors concluded: “Thus, at least when we compare depository institutions, federal preemption was associated with *higher* default rates, not lower ones, from 2006 through 2008. Those were the years when loan underwriting was at its worst and the credit markets experienced a meltdown.”²⁰¹

193. ENGEL & MCCOY, *supra* note 24, at 176–79, 222–23; Wilmarth, *supra* note 112, at 29–30; FCIC REPORT, *supra* note 28, at 88, 151–52, 177–78, 200–04, 257–59, 305–06, 346, 350–51, 365–66, 382–85; Appelbaum & Nakashima, *supra* note 81.

194. ENGEL & MCCOY, *supra* note 24, at 170, 200–02; FCIC REPORT, *supra* note 28, at 107–08, 173–74, 248–50; Steve Mufson, *A Fateful Step for a Banking Giant*, WASH. POST, Dec. 5, 2010, at G1; James R. Hagerty & Joann S. Lublin, *Countrywide Deal Driven by Crackdown Fear*, WALL ST. J., Jan. 29, 2008, at A3.

195. ENGEL & MCCOY, *supra* note 24, at 169–71, 202–03; FCIC REPORT, *supra* note 28, at 195–200, 263, 302–05, 366–71, 379–82; Wilmarth, *supra* note 19, at 978–79, 984–85.

196. ENGEL & MCCOY, *supra* note 24, at 204; *see also* FCIC REPORT, *supra* note 28, at 308 (concluding that “the banking supervisors failed to adequately and proactively identify and police the weaknesses of the banks and thrifts,” and noting that “[l]arge commercial banks and thrifts, such as Wachovia and IndyMac . . . had significant exposure to risky mortgage assets”).

197. ENGEL & MCCOY, *supra* note 24, at 159–63.

198. *Id.* at 163.

199. *Id.*

200. *Id.*

201. *Id.*

III. TITLE X OF DODD–FRANK GRANTS SUPPLEMENTAL LAWMAKING AND LAW ENFORCEMENT POWERS TO THE STATES AND IMPOSES SIGNIFICANT RESTRICTIONS ON THE OCC’S AUTHORITY TO PREEMPT STATE LAWS

Congress designated Title X of Dodd–Frank as the “Consumer Financial Protection Act of 2010” (CFP Act).²⁰² As described in Part III.A, Title X authorizes CFPB to issue regulations and to bring enforcement actions to protect consumers of financial services. However, Title X does not give CFPB exclusive authority over the field of consumer financial protection. Instead, as discussed in Parts III.B and III.C, the CFP Act empowers the states to provide supplemental safeguards to consumers through both lawmaking and law enforcement activities. Moreover, as explained in Part III.D, Title X imposes significant limitations on the OCC’s ability to preempt the application of state consumer financial laws to national banks and federal thrifts.

A. Title X Establishes a Federal “Floor” of Protection for Consumers of Financial Services

Title X of Dodd–Frank establishes CFPB as an “independent bureau” within the Fed and assigns to CFPB the mission of “regulat[ing] the offering and provision of consumer financial services under the Federal consumer financial laws.”²⁰³ CFPB is responsible for implementing and enforcing “federal consumer financial laws,” which include “nearly every existing federal consumer financial statute, as well as new consumer financial protection mandates prescribed by the [CFP] Act.”²⁰⁴ Title X protects the independence of the CFPB by (i) prohibiting the Fed from interfering with CFPB’s policymaking and enforcement functions,²⁰⁵ and (ii) requiring the Fed to provide approximately \$500 million each year to fund CFPB’s operations.²⁰⁶

202. Dodd–Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 1001, 124 Stat. 1376, 1955 (2010).

203. *Id.* § 1011(a). For a helpful overview of CFPB’s authority under Title X, see Michael B. Mierzewski et al., *The Dodd–Frank Act Establishes the Bureau of Consumer Financial Protection as the Primary Regulator of Consumer Financial Products and Services*, 127 BANKING L.J. 722 (2010).

204. Mierzewski et al., *supra* note 203, at 724–25; *see also* Dodd–Frank § 1021(a) (providing that CFPB’s purpose is to “implement and, where applicable, enforce Federal consumer financial law” to ensure that markets for consumer financial products and services are accessible to consumers and are also “fair, transparent, and competitive”); *Id.* § 1002(14) (defining “Federal consumer financial law” to include Title X of Dodd–Frank, 18 federal consumer protection statutes that are enumerated in Section 1002(12), and certain other laws).

205. Dodd–Frank prohibits the Federal Reserve Board (FRB) from (i) intervening in any CFPB proceeding; (ii) appointing, directing or removing any CFPB officer or employee; (iii) combining the CFPB or any of its functions with any other unit of the FRB; or (iv) approving or reviewing any rule or order of the CFPB or any legislative recommendation or testimony of the Director or any other officer of CFPB. *Id.* § 1012(c). Thus, Dodd–Frank “makes clear that the [CFPB] is to function without any interference by the [FRB].” S. REP. NO. 111-176, at 161 (2010). The provisions protecting CFPB’s independence are “modeled on similar statutes governing the [OCC],” an autonomous bureau located with the Treasury Department. *Id.*

206. Dodd–Frank requires the Fed to provide funds for CFPB’s operations in an amount determined by CFPB’s Director to be “reasonably necessary” to carry out the CFPB’s authorities in view of other funding available to the CFPB, up to the following maximum limits: (i) 10% of the Fed’s total operating expenses in fiscal year 2011, (ii) 11% of such expenses in fiscal year 2012, and (iii) 12% of such expenses in each subsequent fiscal year. Dodd–Frank § 1017(a). Congress concluded that “the assurance of adequate funding [from the Fed], independent of the Congressional appropriations process, is absolutely essential to the

The Director of CFPB is appointed by the President for a five-year term, with the Senate’s advice and consent, and is removable only for good cause.²⁰⁷ Title X authorizes the Director to issue rules, orders, and provide guidance “to administer and carry out the purposes and objectives of the Federal consumer financial laws, and to prevent evasions thereof.”²⁰⁸ In particular, the Director may issue rules and bring enforcement proceedings to prevent persons subject to Title X from engaging in “unfair, deceptive, or abusive acts or practices (UDAAP) in connection with consumer financial products or services.”²⁰⁹ The Director may also issue regulations to ensure that “the features of any consumer financial product or service . . . are fully, accurately, and, effectively disclosed to consumers in a manner that permits consumers to understand the costs, benefits, and risks associated with the product or service.”²¹⁰ CFPB’s regulations are subject to potential override by the Financial Stability Oversight Council (FSOC) if the FSOC determines that any CFPB regulation threatens the safety and soundness of the U.S. banking system or the stability of the U.S. financial system.²¹¹ In addition to the prohibitions created by CFPB’s rules, Section 1036 of Dodd–Frank imposes a general statutory ban on the use of UDAAP by covered providers of financial products or services.²¹²

Title X authorizes CFPB to examine depository institutions with total assets of more than \$10 billion (as well as their affiliates) and all nondepository providers of consumer financial services to determine their compliance with consumer financial protection laws.²¹³ Title X also enables CFPB to take a variety of actions to stop violations of (i) the CFP Act and the CFPB’s regulations thereunder (including statutory and regulatory prohibitions against UDAAP), or (ii) any of the 18 federal consumer financial laws

independent operations of any financial regulator.” S. REP. NO. 111-176, at 163 (2010). Dodd–Frank will require the Fed to provide approximately \$500 million of funding to CFPB in fiscal year 2013 and subsequent years. *Id.* at 164 (graph).

207. Dodd–Frank § 1011(b)–(c).

208. *Id.* § 1022(b)(1).

209. *Id.* § 1031(a)–(b). For a recent analysis of the potential scope of CFPB’s authority to adopt rules prohibiting UDAAP, see Carey Alexander, *Abusive: Dodd–Frank Section 1031 and the Continuing Struggle to Protect Consumers* 13–35 (St. John’s Leg. Stud. Res. Paper No. 10-193, Dec. 2010), available at <http://ssrn.com/abstract=1719600>.

210. Dodd–Frank § 1032(a).

211. The FSOC has authority to set aside any CFPB regulation if the FSOC determines by a vote of two-thirds of its members that the regulation would “put the safety and soundness of the United States banking system or the stability of the financial system of the United States at risk.” *Id.* § 1023(a). The FSOC has 10 voting members (including the heads of nine federal financial agencies and an independent member with insurance experience) and five non-voting members. *Id.* § 111(b). In order to initiate the FSOC’s review of a CFPB regulation, a member of the FSOC must petition the FSOC to set aside the regulation. *Id.* § 1023(a)–(b). It is not clear whether a non-voting member of the FSOC is qualified to file or vote on such a petition.

212. *Id.* § 1036(a)(1)(B). As discussed below, Title X’s statutory ban on UDAAP may be enforced against state-chartered or state-licensed providers of financial services by state attorneys general as well as the CFPB. See *infra* notes 235–36 and accompanying text.

213. Depository institutions with total assets of \$10 billion or less will be examined by federal banking agencies to assess their compliance with consumer financial protection laws. Mierzewski et al., *supra* note 203, at 731–32. CFPB has authority (i) to obtain reports from smaller depository institutions, (ii) to include one of CFPB’s examiners on the examination teams for such depository institutions, and (iii) to provide input to the primary regulations of such institutions with regard to the scope and conduct of examinations, the contents of examination reports and examination ratings. Dodd–Frank § 1026.

enumerated in Section 1002(12) of Dodd–Frank.²¹⁴ CFPB’s powers to prevent violations of such laws include (i) undertaking investigations and performing administrative discovery, (ii) initiating administrative enforcement proceedings (including actions for cease-and-desist orders), (iii) filing judicial enforcement actions, and (iv) making referrals of criminal charges to the Department of Justice.²¹⁵ The CFPB may use administrative or judicial enforcement proceedings to obtain a wide range of legal and equitable remedies, including refunds, restitution, damages, civil money penalties and injunctive relief.²¹⁶

Thus, Title X vests CFPB with broadly-defined powers to regulate providers of consumer financial products and services.²¹⁷ However, Title X does not authorize CFPB to regulate persons engaged in insurance, securities or commodity trading activities. In addition, sellers of nonfinancial goods and manufactured homes, real estate brokers, auto dealers, attorneys, accountants, and tax preparers are exempted from the CFPB’s jurisdiction unless they are significantly engaged in offering covered financial products or services.²¹⁸

B. Title X Empowers the States to Adopt Laws Providing Additional Protection to Consumers of Financial Services

Notwithstanding the broad powers granted to the CFPB, Title X does not give the federal government exclusive control over consumer financial protection. Instead, Title X authorizes the states to provide supplemental safeguards to consumers through both lawmaking (as described in this Part) and law enforcement (as discussed in the next Part). Section 1041(a)(1) provides that the CFP Act does not preempt state law “except to the extent that a state law is inconsistent with the provisions of [the CFP Act] and then only to the extent of the inconsistency.”²¹⁹ Section 1041(a)(2) explains that a state law is “not inconsistent” with the CFP Act—and therefore is not preempted—if the state law provides “greater” protection to consumers than the protection provided by the CFP Act.²²⁰ CFPB may determine whether any state law is preempted due to inconsistency

214. Dodd–Frank §§ 1002(12), 1031, 1036(a)(1)(B), 1052–55. Section 1031 of Dodd–Frank imposes strict limits on CFPB’s authority to adopt rules declaring acts or practices to be “unfair” or “abusive” and therefore unlawful under CFPB’s UDAAP authority. *Id.* § 1031(c)–(e). In addition, CFPB may not bring an administrative enforcement hearing to enforce an enumerated federal consumer financial law to the extent that the law in question specifically limits CFPB’s authority to do so. *Id.* § 1053(a)(2).

215. *Id.* §§ 1052–56; see Mierzewski et al., *supra* note 203, at 732–35 (describing CFPB’s enforcement powers). CFPB has authority to represent itself in the Supreme Court if it submits a request to the Attorney General and the Attorney General concurs or acquiesces in that request. Dodd–Frank § 1054(e).

216. Dodd–Frank §§ 1053–55. CFPB may not impose exemplary or punitive damages. *Id.* § 1055(a)(3).

217. See *id.* § 1002(5)–(6), (26) (defining “consumer financial product or service,” “covered person,” and “service provider”); Mierzewski et al., *supra* note 203, at 726 (describing persons, products, and services that are regulated under Title X).

218. See Dodd–Frank §§ 1027, 1029 (exempting designated industries from CFPB’s jurisdiction); see also H.R. REP. NO. 111-517, at 875 (2010) (Conf. Rep.), *reprinted in* 2010 U.S.C.C.A.N. 722, 731 (discussing statutory exceptions to CFPB’s jurisdiction); S. REP. NO. 111-176, at 160, 169–71 (2010) (same); Mierzewski et al., *supra* note 203, at 727–28 (same).

219. Dodd–Frank § 1041(a)(1).

220. *Id.* § 1041(a)(2); See S. REP. NO. 111-176, at 174 (2010) (“Section 1041 confirms that the [Title X] will not preempt State law if the State law provides greater protection for consumers.”).

with the CFP Act either “on its own motion or in response to a nonfrivolous petition initiated by any interested person.”²²¹

The general anti-preemption language contained in Section 1041 of Dodd–Frank does not determine the question of whether state laws are subject to preemption under either the National Bank Act (NBA)²²² or the Home Owners’ Loan Act (HOLA).²²³ Sections 1043–1048 of Dodd–Frank govern preemption issues under those two statutes.²²⁴ As shown below in Part III.D, Dodd–Frank significantly limits the OCC’s authority to preempt the application of state consumer financial laws to national banks and federal thrifts.

As explained above, the CFP Act preempts state laws only when they provide *less* protection than the CFP Act and the CFPB’s regulations.²²⁵ Consequently, the CFP Act establishes a “floor” and not a “ceiling” for consumer financial protection.²²⁶ The limited scope of preemption under the CFP Act is consistent with the “floor” preemption established by most federal laws that protect consumers of financial products, including the Equal Credit Opportunity Act (ECOA), the Electronic Funds Transfer Act (EFTA), the Fair Debt Collection Practices Act (FDCPA), and the Truth in Lending Act (TILA).²²⁷ In this regard, the Senate committee report on Dodd–Frank explained that “Federal consumer financial laws have historically established only minimum standards [of consumer protection] and have not precluded the States from enacting more protective standards. [The CFP Act] maintains that status quo.”²²⁸

By giving the states a supplemental lawmaking role with regard to consumer financial protection, Dodd–Frank encourages CFPB and the states to work together with the goal of providing optimal protection to consumers. To advance that goal, section 1041(c) requires CFPB to conduct a rulemaking proceeding whenever a majority of the states have adopted a resolution recommending that CFPB should establish or modify a consumer protection regulation.²²⁹ As noted in the Senate report, Section 1041(c) will enhance the states’ ability to persuade CFPB to “adjust [federal consumer protection]

221. Dodd–Frank § 1041(a)(2).

222. 12 U.S.C. §§ 1–216b (2006).

223. *Id.* §§ 1461–70.

224. *See infra* Part III.D (discussing Dodd–Frank’s establishment of new preemption standards under the NBA and HOLA).

225. *See infra* notes 219–21 and accompanying text (describing the limited preemption of state laws under Section 1041 of Dodd–Frank).

226. For an analysis of the important distinction—in terms of preemptive effect on the states—between federal statutes that establish “floors” and those that create “ceilings” of regulatory standards, see Buzbee, *supra* note 16, at 1564–72 (describing the difference between (i) federal environmental laws that establish “regulatory floors” and allow more stringent state requirements and (ii) federal energy and hazardous waste laws that create “preemptive ceilings” and prohibit any additional regulation by the states).

227. Like the CFP Act, ECOA, EFTA, and FDCPA provide that state laws are not “inconsistent” with federal law, and are therefore not preempted, if state laws provide “greater” protection to consumers than the protection provided by federal law. 15 U.S.C. § 1692n (2006) (FDCPA); *id.* § 1693d(f) (ECOA); *id.* § 1693q (EFTA). Similarly, courts have held that “states remain free to impose greater protections for borrowers” than the safeguards created by TILA. *Williams v. First Gov’t Mortg. & Investors Corp.*, 176 F.3d 497, 500 (D.C. Cir. 1999); *accord Black v. Financial Freedom Senior Funding Corp.* 112 Cal. Rptr. 2d 445, 461 (Cal. Ct. App. 2001).

228. S. REP. NO. 111-176, at 174 (2010).

229. Dodd–Frank § 1041(c).

standards over time.”²³⁰

C. Title X Enables State Attorneys General to Enforce the CFP Act and the CFPB’s Regulations

Section 1042 of Dodd–Frank authorizes state attorneys general (AGs) to enforce the CFP Act or CFPB’s regulations by filing actions in federal or state courts to secure civil remedies under the CFP Act or under other applicable federal or state laws.²³¹ Section 1042 also permits state AGs to enforce the CFP Act or CFPB’s regulations by bringing administrative enforcement proceedings against “any entity that is State-chartered, incorporated, licensed, or authorized to do business under State law.”²³² However, state AGs may not bring administrative enforcement proceedings against national banks or federal thrifts.²³³ State AGs may only file judicial enforcement actions against national banks or federal thrifts under the CFP Act, and such actions must be based on alleged violations of CFPB regulations.²³⁴ Thus, a state AG may not sue a national bank or federal thrift to enforce any statutory provision of the CFP Act (unless that statutory provision has been expressly incorporated in a CFPB regulation).

As a practical matter, the forgoing limitation means that state AGs are authorized to enforce only CFPB’s interpretations of the CFP Act (as embodied in CFPB regulations) against national banks or federal thrifts and only by filing lawsuits. For example, state AGs may not enforce Section 1036’s general statutory ban on UDAAP against national banks or federal thrifts.²³⁵ In contrast, state AGs may enforce the statutory provisions of the CFP Act, including the “generic UDAAP ban,” against state-chartered or state-licensed entities through either administrative or judicial enforcement proceedings.²³⁶

Section 1042(b)(1) requires a state AG to give CFPB a copy of each complaint that the AG has filed in any administrative or judicial proceeding to enforce the CFP Act or CFPB’s regulations.²³⁷ Upon receiving the AG’s complaint, CFPB may intervene as a party in the proceeding, may remove any state court action to federal district court, and may appeal any order or judgment to the same extent as any other party in the proceeding.²³⁸ Section 1042(b) ensures that CFPB will have the right to participate in all enforcement proceedings brought by state AGs under the CFP Act or CFPB’s regulations.

State AGs have authority under certain state and federal laws to enforce the CFP Act and CFPB’s rules against certain classes of persons who are not subject to CFPB’s

230. S. REP. NO. 111-176, at 175 (2010).

231. Dodd–Frank § 1042(a)(1).

232. *Id.*

233. *Id.*

234. *Id.* § 1042(a)(2).

235. Lauren Saunders, *The Role of the States Under the Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010*, NAT’L CONSUMER L. CTR. 2–3 (Dec. 2010), <http://www.nclc.org/images/pdf/legislation/dodd-frank-role-of-the-states.pdf> (citing Dodd–Frank §§ 1036(a)(1)(B), 1042(a)(1)–(2)).

236. *Id.*

237. The AG is required to give CFPB its complaint before initiating its enforcement action or, if “prior notice is not practicable, . . . immediately upon instituting the action.” Dodd–Frank § 1042(b)(1)(B).

238. *Id.* § 1042(b)(2).

enforcement jurisdiction.²³⁹ For example, state AGs could potentially “use CFPB rules as a basis for arguing that a merchant, retailer or seller has violated [a] *state law* ban on unfair or deceptive practices.”²⁴⁰ In addition, Section 1042(d) of Dodd–Frank stipulates that the CFP Act may not be construed to limit (i) the authority of a state AG or other responsible state official to initiate any enforcement action or other regulatory proceeding based “solely” on the law of that state, or (ii) the authority of state insurance or securities officials or agencies to take enforcement or other regulatory actions authorized by state securities laws or state insurance laws.²⁴¹ Thus, the CFP Act does not impair the enforcement powers granted to state AGs or state securities or insurance officials by valid state laws.

D. Dodd–Frank Limits the Preemptive Authority of the OCC with Respect to National Banks and Federal Thrifts

Title X of Dodd–Frank establishes new preemption standards under the NBA and HOLA. As shown below, the new standards impose significant limitations on the OCC’s authority to preempt the application of state consumer financial laws to national banks and federal thrifts. The new standards also require the OCC to make major changes in the preemption rules that were issued by the OTS and the OCC between 1996 and 2004.²⁴² The new standards do not address the applicability of general state laws to national banks and federal thrifts. However, I argue below that Title X’s silence with regard to general state laws should be construed to support the presumptive applicability of such laws to national banks and federal thrifts.²⁴³

1. Dodd–Frank Establishes New Preemption Standards That Govern the Application of State Consumer Financial Laws to National Banks and Federal Thrifts

Sections 1044 through 1047 of Dodd–Frank, which take effect on July 21, 2011, adopt new preemption standards that govern the applicability of state consumer financial laws to national banks and federal thrifts.²⁴⁴ The revised national bank preemption rules are contained in a new section (Section 5136C) of the NBA,²⁴⁵ while the altered thrift standards are set forth in a new provision (Section 6) of HOLA.²⁴⁶ The new preemption

239. Saunders, *supra* note 235, at 3–4 (describing the right of state AGs under certain state and federal laws to enforce the CFP Act or CFPB’s rules against smaller banks, thrifts, and credit unions (i.e., those with assets under \$10 billion) and also against auto dealers and certain merchants, retailers, and sellers, notwithstanding CFPB’s lack of enforcement jurisdiction over any of those persons).

240. *Id.* at 3 (emphasis in original).

241. Dodd–Frank § 1042(d).

242. *See supra* Part II.E.2 (discussing the preemption rules adopted by the OTS and the OCC).

243. *See infra* Part III.D.8 (explaining why general state laws should presumptively apply to national banks and federal thrifts).

244. Dodd–Frank §§ 1044, 1045, 1047(a) (enacting new preemption standards for national banks), *id.* §§ 1046, 1047(b) (enacting new preemption standards for federal thrifts). The effective date for these provisions is July 21, 2011, which the Secretary of the Treasury has established as the “designated transfer date.” *Id.* § 1048; *see* 75 Fed. Reg. 57,252 (Sept. 20, 2010).

245. Dodd–Frank §§ 1044, 1045, 1047(a) (enacting new § 5136C of the NBA) (to be codified at 12 U.S.C. § 25b).

246. *Id.* §§ 1046, 1047(b) (enacting new section 6 of HOLA (to be codified at 12 U.S.C. § 1465)).

standards for federal thrifts are equivalent to those for national banks.²⁴⁷

Dodd–Frank’s revised preemption standards apply to “state consumer financial laws,” which include state laws that (i) do not “directly or indirectly discriminate” against federally-chartered depository institutions, and (ii) “directly and specifically” regulate financial transactions involving consumers or their related accounts.²⁴⁸ For example, a state law that regulates the specific terms and conditions of a consumer loan (e.g., by prohibiting or limiting certain types of fees or amortization terms) should be treated as a state consumer financial law. In contrast, state laws that establish general requirements, standards, or prohibitions with respect to the conduct of business by both financial and nonfinancial firms—e.g., state laws prohibiting fraudulent or deceptive practices or unconscionable contracts—should not be treated as state consumer financial laws for purposes of Section 5136C of the NBA and Section 6 of HOLA. The statutory distinction in Dodd–Frank between state laws that “directly and specifically” regulate the terms and conditions of consumer financial transactions and other state laws that apply generally to a broad range of business conduct is consistent with a series of recent cases decided under both HOLA and the NBA. Those decisions have held that state laws of general applicability are less likely to create conflicts with either HOLA or the NBA and, therefore, are less likely to be preempted.²⁴⁹

2. Dodd–Frank’s New Standards Significantly Limit the OCC’s Authority to Preempt State Consumer Financial Laws

As shown below, Dodd–Frank’s new preemption standards impose several important limitations on the OCC’s authority to preempt state consumer financial laws. First, Dodd–Frank requires the OCC to apply conflict preemption principles and, in most cases, to justify each preemption determination by showing that a state consumer financial law prevents or significantly interferes with a national bank’s exercise of its federally-granted powers. Second, Dodd–Frank requires the OCC to make preemption determinations on a case-by-case basis and to show that each determination is supported by substantial evidence. Third, the OCC is entitled to receive only limited deference if its preemption determination is reviewed by a court.

247. *See id.* § 1046 (enacting new section 6(a) of HOLA, which provides that any preemption determinations made by a court or the responsible agency under HOLA “shall be made in accordance with the laws and legal standards applicable to national banks regarding the preemption of State law”).

248. *Id.* §§ 1044, 5136(c)(a)(2).

249. *See, e.g., In re Ocwen Loan Servicing, LLC Mortg. Servicing Litig.*, 491 F.3d 638, 643–46 (7th Cir. 2007) (affirming the applicability of general state laws to federal thrifts under HOLA); *Martinez v. Wells Fargo Home Mortg., Inc.*, 598 F.3d 549, 555–56 (9th Cir. 2010) (recognizing the applicability of general state laws to national banks under the NBA); *see also* *Jefferson v. Chase Home Fin.*, No. C 06-6510 TEH, 2008 WL 1883484, at *10–15 (N.D. Cal. Apr. 29, 2008); *Mwantembe v. TD Bank, N.A.*, 669 F. Supp. 2d 545, 553–54 (E.D. Pa. 2009); *Young v. Wells Fargo & Co.*, 671 F. Supp. 2d 1006, 1018–22 (S.D. Iowa 2009); *Augustin v. PNC Fin. Servs. Group, Inc.*, 707 F. Supp. 2d 1080, 1092–97 (D. Hawaii 2010); *Gutierrez v. Wells Fargo Bank, N.A.*, 730 F. Supp. 2d 1080, 1130–33 (N.D. Cal. 2010) (each holding that general state laws applied to national banks and were not preempted by the NBA).

a. Under Dodd–Frank, the OCC May Preempt a State Consumer Financial Law Only If That Law Prevents or Significantly Interferes With a National Bank’s Exercise of Its Powers

Paragraph (b)(1) of Section 5136C establishes three new tests for determining whether the NBA preempts a state consumer financial law.²⁵⁰ Under paragraph (b)(1), “State consumer financial laws are preempted, only if” (A) application of the state law has a “discriminatory effect on national banks” in comparison with state banks; (B) if the state law is preempted under the “legal standard for preemption” set forth in *Barnett Bank of Marion County, N.A. v. Nelson*,²⁵¹ as discussed below;²⁵² or (C) if the state law is preempted by a federal law other than a statute defining the powers of national banks.²⁵³ The first preemption test of nondiscrimination is straightforward and should not require great difficulty in application. If a state law discriminates against national banks either on its face or in its practical application, it will be preempted.²⁵⁴

The second preemption test, set forth in subparagraph (b)(1)(B), provides that a “state consumer financial law” will be preempted “in accordance with the legal standard for preemption in the decision of the Supreme Court . . . in *Barnett Bank of Marion County, N.A. v. Nelson* . . . 517 U.S. 25 (1996),”²⁵⁵ if the particular state law “prevents or significantly interferes with the exercise by the national bank of its powers.”²⁵⁶ Thus, subparagraph (b)(1)(B) expressly adopts the “prevent or significantly interferes with” test in *Barnett Bank* as the governing standard for determining whether state consumer financial laws apply to national banks.²⁵⁷ In addition, the relevant inquiry under *Barnett Bank* is to determine whether a challenged state law actually “prevents or significantly interferes with” the “exercise” of “powers” by a national bank.²⁵⁸

In Section 104(d)(2)(A) of the Gramm–Leach–Bliley Act,²⁵⁹ enacted in 1999, Congress incorporated the “prevent or significantly interfere with” standard of *Barnett Bank* as the governing rule for determining whether state laws regulating sales of insurance by depository institutions are preempted by federal law.²⁶⁰ Thus, Congress expressed its clear understanding in 1999 that the applicable preemption standard under *Barnett Bank* is the “prevent or significantly interfere with” test.²⁶¹ Similarly, the

250. Dodd–Frank § 1044 (to be codified at 12 U.S.C. § 25b(b)(1)(A)).

251. *Barnett Bank of Marion Cnty., N.A. v. Nelson*, 517 U.S. 25 (1996).

252. *Id.* (to be codified at 12 U.S.C. § 25b(b)(1)(B)); see *infra* notes 255–70 and accompanying text (discussing the *Barnett Bank* standard for preemption).

253. Dodd–Frank § 1044 (to be codified at 12 U.S.C. § 25(b)(1)(C)). See *infra* notes 275–82 and accompanying text (discussing the types of federal laws that are likely to be included under the third category).

254. Cf. *McClellan v. Chipman*, 164 U.S. 347, 360–61 (1896) (holding that national banks were required to comply with a “general and undiscriminating law” enacted by Massachusetts to prevent insolvent debtors from providing preferences to creditors).

255. Dodd–Frank § 1044 (to be codified at 12 U.S.C. § 25b(b)(1)(B)).

256. *Id.*; see *Barnett Bank*, 517 U.S. at 33 (upholding the states’ authority “to regulate national banks where . . . doing so does not prevent or significantly interfere with the national bank’s exercise of its powers”).

257. *Barnett Bank*, 517 U.S. at 33.

258. *Id.*

259. Gramm–Leach–Bliley Act, Pub. L. No. 106-102, § 104(d)(2)(A), 113 Stat. 1341, 1353 (codified at 15 U.S.C. § 6701(d)(2)(A) (2006)).

260. *Id.*

261. See H.R. REP. NO. 106-434, at 156–57 (1999) (Conf. Rep.), reprinted in 1999 U.S.C.C.A.N. 245, 251

conference committee report and the Senate committee report on Dodd–Frank confirm that Congress once again specifically endorsed the “prevent or significantly interferes with” standard of *Barnett Bank* as the controlling rule for determining whether state consumer financial laws are preempted under Section 5136C(b)(1)(B).²⁶²

The Supreme Court has not precisely defined the degree of interference that is required to invalidate a state law under the “significantly interferes with” standard set forth in *Barnett Bank*. A recent appellate court opinion concluded that “the level of ‘interference’ that gives rise to preemption under [*Barnett Bank*] is not very high.”²⁶³ However, as shown below, there are good reasons to believe that the Supreme Court would view that question differently, given the Court’s discussion of preemption in *Barnett Bank* and its interpretation of the meaning of the term “significant” in other federal statutes.

In *Barnett Bank*, the Court struck down a Florida statute, which prohibited national banks that were subsidiaries of BHCs from exercising a power granted by Congress (namely, the right to sell insurance in towns with 5000 or fewer inhabitants).²⁶⁴ The Court held that Florida could not “condition” a congressional grant of federal power by requiring “a grant of state permission” to exercise that power.²⁶⁵ Thus, the Florida law ran afoul of the “prevent” prong of the *Barnett Bank* standard because it prohibited most national banks from exercising an express power granted by Congress in a federal statute.²⁶⁶

The Court in *Barnett Bank* also pointed to the state law that it found to be preempted in *Franklin National Bank v. New York*.²⁶⁷ In *Franklin*, a New York statute prohibited national banks and state commercial banks from using the word “savings” in advertising for deposits and reserved that advertising privilege solely for state savings banks.²⁶⁸ The Court pointed out in *Franklin* that a provision of the Federal Reserve Act specifically authorized national banks to accept savings deposits, while the NBA also granted a general power to accept deposits.²⁶⁹ The Court made clear in *Franklin* that it viewed New York’s prohibition on advertising for savings deposits as a very prejudicial interference with the federally-granted power of national banks to accept savings deposits:

Modern competition for business finds advertising one of the most usual and useful of weapons. We cannot believe that the incidental powers granted to national banks should be construed so narrowly as to preclude the use of advertising in any branch of their authorized business. It would require some

(explaining that under the 1999 statute, “[w]ith respect to insurance sales, solicitations, and cross-marketing, States may not prevent or significantly interfere with the activities of depository institutions or their affiliates, as set forth in *Barnett Bank of Marion County N.A. v. Nelson*, 517 U.S. 25 (1996)”).

262. See H. R. REP. NO. 111-517, at 875 (2010), *reprinted in* 2010 U.S.C.C.A.N. 722, 731; S. REP. NO. 111-176, at 175–76 (2010).

263. *Monroe Retail, Inc. v. RBS Citizens, N.A.*, 589 F.3d 274, 283 (6th Cir. 2009).

264. *Barnett Bank of Marion Cnty., N.A. v. Nelson*, 517 U.S. 25, 28–38 (1996).

265. *Id.* at 34–35.

266. *Id.* at 31–35.

267. *Franklin Nat’l Bank v. New York*, 347 U.S. 373 (1954). See also *Barnett Bank*, 517 U.S. at 33 (referring to *Franklin* as “a case quite similar to this one”).

268. *Franklin*, 347 U.S. at 374.

269. *Id.* at 375–76.

affirmative indication to justify an interpretation that would permit a national bank to engage in a business but gave no right to let the public know about it.

... [National banks] do accept and pay interest on time deposits of people’s savings, and they must be deemed to have the right to advertise that fact by using the commonly understood description that Congress has specifically selected.²⁷⁰

The Court’s analysis of the preempted New York statute in *Franklin* suggests that a state law must create a substantial impediment to the exercise of a national bank power before the state law will be preempted under the “significantly interferes with” prong of the *Barnett Bank* standard. This view finds further support, at least by analogy, in Supreme Court decisions construing Sections 10(b) and 14(a) of the Securities Exchange Act of 1934 (1934 Act).²⁷¹ In those decisions, the Supreme Court indicated that the terms “significantly” and “materially” are essentially synonyms, and the Court also held that a “material” fact is one that a “reasonable investor” would be likely to view as “important.”²⁷²

The Court expressed a similar view of the connotation of the word “significant” in a decision that considered the duty of a federal agency to prepare an environmental impact statement (EIS) under the National Environmental Policy Act (NEPA) for a proposed course of action that had “significant environmental impacts.”²⁷³ In explaining why NEPA requires the filing of an EIS for a proposal with “significant” environmental consequences, the Court observed that “NEPA ensures that *important* effects will not be overlooked or underestimated only to be discovered later after resources have been committed or the die otherwise cast.”²⁷⁴ Accordingly, in order to conclude a state law “significantly interferes with” a national bank’s exercise of its powers, and is thereby preempted under Section 5136C(b)(1)(B), I believe that the courts or the OCC must find

270. *Id.* at 377–78.

271. 15 U.S.C. §§ 78j(b), 78n(a).

272. In *Basic, Inc. v. Levinson*, the Court adopted, for purposes of Section 10(b) of the 1934 Act, a “materiality” standard that requires a plaintiff shareholder to show “a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having *significantly* altered the ‘total mix’ of information made available.” *Basic, Inc. v. Levinson*, 485 U.S. 224, 231–32 (1988) (emphasis added) (quoting *TSC Indus., Inc. v. Northway*, 426 U.S. 438, 449 (1976) (adopting same materiality standard under Section 14(a)). The Court also held that “[a]n omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it *important* in deciding how to vote.” *Id.* at 231 (emphasis added) (quoting *TSC*, 426 U.S. at 449).

Similarly, in *Virginia Bankshares, Inc. v. Sandberg*, the Court held that “liability under [Section] 14(a) must rest not only on deceptiveness but on materiality as well (*i.e.*, it has to be *significant* enough to be *important* to a reasonable investor deciding how to vote.” *Virginia Bankshares, Inc. v. Sandberg*, 501 U.S. 1083, 1097 (1991) (emphasis added). The Court concluded that a misleading statement in shareholder proxy documents concerning the reasons why a corporation’s board of directors supported a proposed merger satisfied the test of materiality under Section 14(a). *Id.* at 1097–98. The Court explained that a “shareowner faced with a proxy request will think it *important* to know the directors’ beliefs about the course they recommend and their specific reasons for urging the stockholders to embrace it.” *Id.* at 1091 (emphasis added).

273. *Robertson v. Methow Valley Citizens Council*, 490 U.S. 332, 349 (1989). As the Court pointed out in *Robertson*, NEPA requires a federal agency to prepare an environmental impact statement with respect to any “major” proposal “*significantly* affecting the quality of the human environment.” *Id.* at 348 (emphasis added) (quoting 42 U.S.C. § 4332(C)).

274. *Id.* at 349.

that the challenged state law has an important (i.e., substantial) and adverse impact on the bank's ability to exercise those powers.

An additional interpretive question is raised by the third test in Section 5136C(b)(1)(C), which provides that a State consumer financial law can be preempted by "a provision of Federal law other than this title."²⁷⁵ In my view, a federal law is covered by the third test only if it is a law of general application—e.g., a federal criminal law, employment law or tax law—that does *not* grant a power to national banks, and the preemptive effect of those general laws should be determined in accordance with the particular provisions of those laws. In contrast, a federal statute or regulation granting any type of power to national banks should be subject to the *Barnett Bank* preemption standard described above, not the third test.

Barnett Bank dealt with a provision of the Federal Reserve Act that granted a power to national banks,²⁷⁶ and the same was true in *Franklin*.²⁷⁷ Similarly, the new preemption standards in Section 5136C refer in several places to Section 24 of the Federal Reserve Act,²⁷⁸ which authorizes national banks to make real estate loans. Congress identified the failure of federal regulators to stop abusive and unsound real estate lending as a leading cause of the financial crisis.²⁷⁹ The preemptive mortgage lending regulations issued by the OCC and the OTS were singled out for special criticism because they undermined efforts by many states to combat predatory lending.²⁸⁰ Because Section 5136C(b)(1)(B) specifically incorporates the *Barnett Bank* preemption standard, that statute should be interpreted as embodying the holding in *Barnett Bank* that the "prevent or significantly interferes with" standard is the governing test to be applied "[i]n defining the pre-emptive scope of statutes and regulations granting a power to national banks."²⁸¹ Accordingly, the *Barnett Bank* standard in Section 5136C(b)(1)(B) should be applied in any case that involves an alleged conflict between a state consumer financial law and a federal law that grants any "power" to a national bank, whether that federal law is codified in the NBA or in another federal statute such as the Federal Reserve Act.²⁸²

275. Dodd–Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 1044, 124 Stat. 1376, 2015 (2010) (enacting § 5136C(b)(1)(C) of the NBA).

276. *Barnett Bank of Marion Cnty., N.A. v. Nelson*, 517 U.S. 25 (1996) (discussing 12 U.S.C. § 92, which gives national banks the power to sell insurance in small towns); *see also* U.S. Nat'l Bank of Or. v. Indep. Ins. Agents of Am., Inc., 508 U.S. 439, 455–63 (1993) (holding that Section 92 was originally enacted in 1916 as part of the Federal Reserve Act, not the NBA).

277. *See Franklin Nat'l Bank v. New York*, 347 U.S. 373, 375–77 (1954) (discussing a provision of the Federal Reserve Act that authorized national banks to accept savings deposits).

278. Act of Dec. 23, 1913, ch. 6, § 24 (codified as amended at 12 U.S.C. § 371). For references to Section 24 in Dodd–Frank, *see* Dodd–Frank Section 1044 (to be codified at 12 U.S.C. §§ 25(b)(2), (b)(5)), and Section 1045 (to be codified at 12 U.S.C. § 25b(h)(2)).

279. S. REP. NO. 111-176, at 15–17 (2010); *see also supra* Part II (describing how regulatory failures by federal banking agencies contributed to the severity of the financial crisis).

280. S. REP. NO. 111-176, at 16–17; *see also supra* Part II.E.1, II.E.2 (discussing how the OTS's and OCC's preemptive regulations interfered with the states' ability to stop predatory mortgage lending).

281. *Barnett Bank*, 517 U.S. at 33. To make clear its deliberate choice of the "prevent or significantly interferes with" preemption standard for any case involving an alleged conflict between state law and a federal law conferring national bank powers, the Court restated the same standard in synonymous terms in the same paragraph of its opinion. *Id.* The Court said that "normally Congress would not want States to *forbid*, or to *impair significantly*, the exercise of a power that Congress explicitly granted." *Id.* (emphasis added).

282. The conference and Senate committee reports on Dodd–Frank confirm that the *Barnett Bank* standard

b. Dodd–Frank Requires the OCC to Act on a Case-by-Case Basis, to Show Substantial Evidence for Its Preemptive Determinations, and to Publish and Review Its Determinations Periodically

Section 5136C(b)(1)(B) of Dodd–Frank requires the OCC to make any “preemption determination . . . by regulation or order.”²⁸³ Thus, the OCC must issue each determination that federal law preempts a state consumer financial law in the form of a regulation or order, and the OCC may not make any preemption determination by issuing an opinion letter, court brief or informal guidance. This requirement should increase the formality and visibility to the public of OCC preemption determinations.²⁸⁴

In addition, the OCC must determine “on a case-by-case basis” whether particular state consumer financial laws are subject to preemption by federal law.²⁸⁵ The “case-by-case” requirement means that a preemption determination by the OCC will override only the particular state consumer financial law under consideration and other state laws that have “substantively equivalent terms.”²⁸⁶ Moreover, the OCC must consult with CFPB, and must take CFPB’s views into account, in determining whether other state consumer financial laws have “substantively equivalent terms” to the particular law that the OCC is preempting.²⁸⁷ The requirement for a “case-by-case” determination plainly bars the OCC from adopting blanket rules that preempt broad classes or categories of state law.

Section 5136C(c) provides that an OCC preemption determination will not be given preemptive effect “unless substantial evidence, made on the record of the proceeding, supports the specific finding regarding the preemption of [the State consumer financial law] in accordance with the decision of the Supreme Court . . . in [*Barnett Bank*].”²⁸⁸ Section 5136C(g) requires the OCC to publish, and update at least quarterly, a list of all OCC preemption determinations in effect. The required list must identify “the activities and practices covered by each determination and the requirements and constraints

is the governing test in all cases where it is alleged that state consumer financial laws “prevent or significantly interfere with national banks’ exercise of their powers.” H.R. REP. NO. 111-517, at 875 (2010) (Conf. Rep.), *reprinted in* 1990 U.S.C.C.A.N. 722, 731; *see also* S. REP. NO. 111-176, at 175–76 (2010).

283. Dodd–Frank § 1044. Section 5136C (b)(6) requires that each preemption determination issued by the OCC must be made by the Comptroller of the Currency and may not be delegated to any other officer or employee of the agency. *Id.* (enacting § 5136C(b)(6)).

284. Under a 1994 statute, the OCC is required to follow notice-and-comment procedures before issuing any interpretive rule or opinion letter concluding that federal law preempts state law in the areas of community reinvestment, consumer protection, fair lending or intrastate branching. 12 U.S.C. § 43(a) (1994). The OCC is also required to publish the final interpretive rule or opinion letter in the *Federal Register*. *Id.* § 43(b). Notice-and-comment procedures are not required, however, if the OCC or the courts have previously decided preemption issues that are essentially identical to those covered in the interpretive rule or opinion letter. *Id.* § 43(c).

The OCC will be required to comply with the requirements of Section 43 when it issues preemption determinations that are subject to Dodd–Frank and also cover one of the four subject areas enumerated in Section 43. However, any OCC preemption determination that is subject to Dodd–Frank must be issued in the form of a regulation or order, notwithstanding the permissibility of opinion letters under Section 43. *See* Dodd–Frank § 1044 (to be codified at 12 U.S.C. § 25b(b)(1)(B)) (requiring that “any preemption determination [by the OCC] under this subparagraph” must be made “by regulation or order”).

285. Dodd–Frank § 1044 (to be codified at 12 U.S.C. § 25(b)(1)(B)).

286. *Id.* (to be codified at 12 U.S.C. § 25b(b)(3)(A)).

287. *Id.* (to be codified at 12 U.S.C. § 25(b)(3)(B)).

288. *Id.* (to be codified at 12 U.S.C. § 25b(c)).

determined to be preempted.”²⁸⁹

Section 5136C(d) requires the OCC to conduct a review every five years, “through notice and public comment, of each determination that a provision of Federal law preempts a State consumer financial law.”²⁹⁰ After completing each quinquennial review, the OCC must either (i) publicly announce its decision to maintain or rescind each existing preemption determination, or (ii) publish proposals to modify particular preemption determinations.²⁹¹ Each proposal to amend a preemption determination must comply with the notice-and-comment procedures set forth in 12 U.S.C. § 43.²⁹² In addition, the OCC must submit a report of each quinquennial review of preemption determinations to the House and Senate committees responsible for banking matters.²⁹³ The quinquennial review process will facilitate a periodic public and congressional evaluation of the OCC’s preemption determinations.

c. Dodd–Frank Confirms that the NBA Is Governed by Conflict Preemption Rules, and that OCC Preemption Determinations Are Not Entitled to Chevron Deference

Section 5136C(b)(4) declares that the NBA “does not occupy the field in any area of State law.”²⁹⁴ Thus, Dodd–Frank affirms that conflict preemption principles, instead of field preemption principles, govern NBA preemption issues. That affirmation is consistent with *Barnett Bank*, which held that conflict preemption rules govern the determination of whether a state law is preempted by the NBA.²⁹⁵

Under Section 5136C(b)(5)(A), courts reviewing preemption determinations by the OCC must “assess the validity of such determinations, depending upon the thoroughness evident in the consideration of the agency, the validity of the reasoning of the agency, the consistency with other valid determinations made by the agency, and other factors which the court finds persuasive and relevant to its decision.”²⁹⁶ This standard for judicial review of OCC preemption determinations is essentially the same as *Skidmore* deference, which was defined by the Supreme Court in *Skidmore v. Swift & Co.*²⁹⁷ Under *Skidmore* deference, an agency’s ruling “is eligible to claim respect according to its persuasiveness.”²⁹⁸ The weight to be given by a court to the agency’s ruling under *Skidmore* depends on “all those factors which give it power to persuade, if lacking power to control.”²⁹⁹ In contrast, the much stronger principle of *Chevron* deference, established in *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*,³⁰⁰ requires a

289. *Id.* (to be codified at 12 U.S.C. § 25b(g)).

290. Dodd–Frank § 1044 (to be codified at 12 U.S.C. § 25b(d)(1)).

291. *Id.*

292. *Id.*; see also *supra* note 284 (discussing 12 U.S.C. § 43).

293. Dodd–Frank § 1044 (to be codified at 12 U.S.C. § 25b(d)(2)).

294. *Id.* (to be codified at 12 U.S.C. § 25(b)(4)).

295. See *Barnett Bank of Marion Cnty., N.A. v. Nelson*, 517 U.S. 25, 31 (1988) (stating that “[i]n this case we must ask whether or not the Federal and State Statutes are in ‘irreconcilable conflict’”).

296. Dodd–Frank § 1044 (to be codified at 12 U.S.C. § 25b(b)(5)(A)).

297. *Skidmore v. Swift & Co.*, 323 U.S. 134 (1944). See Saunders, *supra* note 235, at 6 (explaining that Dodd–Frank requires courts reviewing challenges to OCC preemption determinations to apply “the less deferential *Skidmore* standard”) (emphasis in original; footnote omitted).

298. *United States v. Mead Corp.*, 533 U.S. 218, 221 (2001).

299. *Id.* at 228 (quoting *Skidmore*, 323 U.S. at 140).

300. *Chevron U.S.A., Inc. v. Natural Def. Council, Inc.*, 467 U.S. 837 (1984).

reviewing court “to accept the agency’s position if Congress has not previously spoken to the point at issue and the agency’s interpretation is reasonable.”³⁰¹

Section 5136C(b)(5)(A) is one of the most important provisions of Dodd–Frank from the perspective of the states because it ensures that reviewing courts will evaluate the OCC’s preemption determinations without giving strong deference to the OCC’s interpretations of the NBA. *Skidmore* deference will not allow the OCC to claim that each alleged instance of statutory silence or ambiguity in the NBA creates a legislative “gap” that the OCC has authority to fill by issuing preemptive rulings that displace state law. Unlike *Chevron*, *Skidmore*’s more demanding standard of review will compel the OCC to bear the burden of persuading the courts that its preemption determinations are valid.

I have previously argued that when a court reviews a federal agency’s claim of preemption based on an ambiguous federal statute, the court should require a “plain statement” of congressional intent to delegate preemptive authority to the agency.³⁰² Such an approach would be consistent with “the federalism-based canons articulated in *Gregory* [*v. Ashcroft*]³⁰³.”³⁰⁴ As I explained:

Gregory held that the courts may not conclude that a [federal] statute alters ‘the state-federal balance’ in the absence of a ‘plain statement’ of Congress’ intent to change that balance. The [Supreme] Court explained that this ‘plain statement rule’ helps to ensure that ‘the political process’ has given appropriate consideration to the states’ interest in being protected ‘against intrusive exercises of Congress’ Commerce Clause powers.’

....

To preserve our federal structure, *Gregory*’s ban on judicial inference of preemptive intent from ambiguous statutes should apply with at least equal force when federal agencies claim to speak for Congress in asserting preemption based on statutory ambiguity. Unlike Congress, federal agencies are less vulnerable to discipline from ‘the political process’ and do not provide the states with any constitutionally-guaranteed structure of representation that would promote a vigorous and thorough discussion of the states’ interests and concerns before a preemptive regulation is adopted.³⁰⁵

As I pointed out, granting *Chevron* deference to agency preemptive rulings conflicts with *Gregory* because it gives agencies “a far-reaching power to override state law, except in those rare situations where Congress has unambiguously barred an agency from acting.”³⁰⁶ For example, a highly deferential *Chevron*-based approach, which was advocated by Justice Thomas in his dissenting opinion in *Cuomo*, “would have created a virtually conclusive presumption in favor of the OCC’s authority to preempt the states’ sovereign law enforcement powers, even though the OCC was relying on an admittedly

301. *Mead*, 533 U.S. at 229.

302. Wilmarth, *supra* note 112, at 38–39 (footnote omitted).

303. *Gregory v. Ashcroft*, 501 U.S. 452 (1991).

304. Wilmarth, *supra* note 112, at 39.

305. *Id.* at 38–39.

306. *Id.* at 37.

ambiguous statute.”³⁰⁷ Fortunately, a majority of the Supreme Court rejected that approach in *Cuomo*.³⁰⁸

Section 5136C(b)(5)(A) makes clear that the OCC may not obtain *Chevron* deference for its future preemption determinations.³⁰⁹ Dodd–Frank’s endorsement of *Skidmore* deference will force the OCC to bear the burden of persuading the courts that its preemption determinations are correct. In addition, *Skidmore* deference will encourage the courts to resolve the OCC’s preemption claims “in a manner that gives appropriate weight to the interests of state autonomy within our federal system.”³¹⁰

d. Dodd–Frank Denies Preemptive Immunity to Most Subsidiaries, Affiliates and Agents of National Banks

Section 5136C contains three overlapping provisions that affirm the applicability of state laws to subsidiaries, affiliates and agents of national banks. First, Section 5136C(b)(2) declares that the NBA’s provisions “do not preempt, annul, or affect the applicability of any State law to any subsidiary or affiliate of a national bank (other than a subsidiary or affiliate that is chartered as a national bank).”³¹¹ Thus, paragraph (b)(2) establishes that the NBA does not preempt the application of state laws to any non-bank subsidiary or affiliate of a national bank. That provision effectively overrules *Watters v. Wachovia Bank, N.A.*,³¹² which held that state mortgage lending laws did not apply to a state-chartered operating subsidiary of a national bank as long as the NBA preempted such laws from applying to the parent bank.³¹³ Thus, the holding in *Watters* will no longer be valid after Title X of Dodd–Frank becomes effective on July 21, 2011.³¹⁴

Second, Section 5136C(e) provides that:

[N]otwithstanding any provision of [the NBA], a State consumer financial law shall apply to a subsidiary or affiliate of a national bank (other than a subsidiary

307. *Id.* See *Cuomo v. Clearing House Ass’n, LLC*, 129 S. Ct. 2710, 2733 (2009) (Thomas, J., dissenting in part) (stating that, under *Chevron*, the Supreme Court was required “only to decide whether the construction adopted by the [OCC] is unambiguously foreclosed by the statute’s text”).

308. Wilmarth, *supra* note 112, at 1, 6–12, 16–19, 44–46 (explaining the reasons why the majority in *Cuomo* refused to defer to the OCC under *Chevron* and instead struck down the OCC’s preemptive regulation).

309. Section 5136C(b)(5)(B) provides that, except with regard to preemption determinations, “nothing in this section shall affect the deference that a court may afford to the [OCC] in making determinations regarding the meaning or interpretation of [the NBA] or other Federal laws.” Dodd–Frank § 1044 (enacting § 5136C(b)(5)(B) of the NBA). Thus, the OCC remains free to invoke *Chevron* in support of its rulings that do not involve preemption determinations. *Id.*

310. Wilmarth, *supra* note 112, at 40; see also *id.* at 35–36 (suggesting that *Skidmore* deference is consistent with “the judiciary’s responsibility to ensure that preemption issues are resolved in accordance with constitutional and statutory limits on federal power”).

311. *Id.* (to be codified at 12 U.S.C. § 25b(b)(2)).

312. *Watters v. Wachovia Bank, N.A.*, 550 U.S. 1 (2007).

313. *Id.* at 15–21. For authorities concluding that Dodd–Frank overrules the holding in *Watters*, see Saunders, *supra* note 235, at 5; Nancy L. Perkins & Beth S. DeSimone, *Has Financial Regulatory Reform Materially Altered the Preemption Landscape for Federally Chartered Institutions?*, 127 BANKING L.J. 759, 761 (2010). See also *supra* note 244 (explaining that Title X of Dodd–Frank takes effect on July 21, 2011).

314. Saunders, *supra* note 235, at 5; Perkins & DeSimone, *supra* note 313, at 761; see also *Cuomo v. Clearing House Ass’n*, 129 S. Ct. 2710, 2717 (2009) (explaining that “the sole question [in *Watters*] was whether operating subsidiaries of national banks enjoyed [preemptive] immunity from state visitation. The opinion addresses and answers no other question.”).

or affiliate that is chartered as a national bank) to the same extent that the State consumer financial law applies to any person, corporation, or other entity subject to such State law.³¹⁵

Subsection (e) covers much of the same ground as paragraph (b)(2), except that subsection (e) focuses on nondiscrimination (i.e., the equal application of state laws to all affected persons) and applies only to “State consumer financial laws” instead of all state laws.³¹⁶ If a state consumer financial law applies on a nondiscriminatory basis to any person, corporation, or other entity, then the same law applies equally to a non-bank subsidiary or affiliate of a national bank.

Third, Section 5136C(h) provides that “[n]o provision of [the NBA] shall be construed as preempting, annulling, altering or affecting the applicability of State law to any subsidiary, other affiliate, or agent of a national bank (other than a subsidiary, affiliate, or agent that is chartered as a national bank).”³¹⁷ The non-preemptive language of subsection (h) closely resembles the text of paragraph (b)(2). However, subsection (h) has a broader scope because it declares that the NBA does not preempt the application of state law to agents of national banks. Subsection (h) thereby effectively overrules past lower court decisions holding that agents of national banks were entitled to a preemptive immunity from state laws comparable to that granted to operating subsidiaries by the Supreme Court in *Watters*.³¹⁸

3. Dodd–Frank Requires the OCC to Rescind or Modify Its Existing Preemption Rules Except for the Regulation Governing the Charging of “Interest” under 12 U.S.C. § 85

Section 5136C of the NBA, as enacted by Dodd–Frank, directly conflicts with the blanket preemption regulations that the OCC adopted in 2004 with regard to real estate loans, deposits, non-real estate loans, and other “operations” of national banks.³¹⁹ The OCC’s regulations mandate an across-the-board preemption of state laws that “obstruct, impair, or condition a national bank’s ability to fully exercise” its powers in four broadly-defined areas of the banking business: (i) real estate lending, (ii) other types of lending, (iii) deposit-taking, and (iv) other “activities” authorized for national banks under federal law.³²⁰ As shown below, the OCC’s 2004 preemption rules conflict with Section 5136C in three major respects.

First, Dodd–Frank overrides the “obstruct, impair, or condition” preemption test contained in the OCC’s 2004 preemption rules. Second, the OCC’s blanket preemption rules contravene Dodd–Frank’s requirements for individualized, “case-by-case” preemption determinations that are supported by “substantial evidence.” Third, in view of Dodd–Frank’s provisions upholding the application of state law to non-bank subsidiaries,

315. Dodd–Frank § 1044 (to be codified at 12 U.S.C. § 25b(e)).

316. Compare *id.* with Dodd–Frank § 1044 (to be codified at 12 U.S.C. § 25b(b)(2)).

317. *Id.* § 1045 (enacting § 5136(h) of the NBA).

318. See, e.g., *Pacific Capital Bank, N.A. v. Connecticut*, 542 F.3d 341, 353 (2d Cir. 2008) (holding that the NBA preempted the application of a state law to an agent of a national bank); *SPGGC, L.L.C. v. Ayotte*, 488 F.3d 525, 536 (1st Cir. 2007) (same).

319. See 12 C.F.R. §§ 34.4, 7.4007, 7.4008, 7.4009 (2010). For a detailed description of the OCC’s 2004 preemption rules, see Wilmarth, *supra* note 93, at 227–28, 233–36, 298–99, 316–17.

320. *Id.* at 233 (describing the OCC’s 2004 rules and quoting Bank Activities and Operations; Real Estate Lending and Appraisals, 69 Fed. Reg. 1904, 1916–17 (Jan. 13, 2004)).

affiliates, and agents of national banks, the OCC must rescind its preemptive regulation for operating subsidiaries.

a. The OCC's Preemption Test Conflicts with the Barnett Bank Preemption Standard Incorporated by Dodd–Frank

The “obstruct, impair, or condition” preemption test contained in the OCC’s regulations has a much broader scope than the “prevents or significantly interferes with” standard set forth in Section 5136C(b)(1)(B). In fact, when the OCC adopted its preemption rules in 2004, it specifically *declined* to adopt the “prevent or significantly interfere with” standard that was articulated in *Barnett Bank*.³²¹ The OCC argued that the “variety of [preemption] formulations” that it abstracted from Supreme Court cases “defeats any suggestion that any one phrase constitutes the exclusive standard for preemption.”³²² The OCC also asserted that its “obstruct, impair, or condition” test was “a distillation of the various preemption constructs articulated by the Supreme Court” but was not “in any way inconsistent” with *Barnett Bank*.³²³

Notwithstanding the OCC’s claims, its 2004 preemption test is plainly incompatible with the preemption standard adopted by Congress in Section 5136C(b)(1)(B). The OCC’s test omits the word “significantly,” and it thereby contemplates the preemption of state laws that only modestly or even trivially burden the exercise of national bank powers.³²⁴ Moreover, the OCC’s preemption rules provide that even general state laws (e.g., laws dealing with contracts, crimes, real property, torts, and zoning) are subject to preemption if they more than “incidentally affect” the exercise of national bank powers.³²⁵ The OCC asserted in its 2004 rulemaking that state laws apply to national banks only to the extent that such laws make it possible for national banks to exercise their powers: “In general, [non-preempted state laws] do not attempt to regulate the manner or content of national banks’ [powers] but instead form the legal infrastructure that makes it practicable to exercise a permissible Federal power.”³²⁶ Thus, the OCC’s “legal infrastructure” theory contemplates a preemption regime that would override all state laws except for those that *support* the exercise of national bank powers.³²⁷ In other

321. See Bank Activities and Operations; Real Estate Lending and Appraisals, 69 Fed. Reg. at 1910 (quoting *Barnett Bank*’s adoption of the “prevent or significantly interfere with” standard, but asserting that the OCC’s “obstruct, impair, or condition” would “better convey the range of effects on national bank powers that the [Supreme] Court has found to be impermissible”).

322. *Id.*

323. *Id.*

324. Wilmarth, *supra* note 93, at 233–36, 316–17.

325. 12 C.F.R. §§ 7.4007(c), 7.4008(e), 7.4009(c)(2), 34.4(b) (2010).

326. Bank Activities and Operations; Real Estate Lending and Appraisals, 69 Fed. Reg. at 1912; *see also id.* at 1913 (reiterating the “legal infrastructure” theory of preemption). The OCC relied on the same theory in a parallel rulemaking that preempted state officials from exercising “visitorial powers” over national banks. The OCC identified non-preempted state laws as those establishing “the legal infrastructure that surrounds and supports the ability of national banks—and others—to do business.” Bank Activities and Operations, 69 Fed. Reg. 1896 (Jan. 13, 2004). The OCC further declared, “[T]hese [non-preempted] state laws provide a framework for a national bank’s ability to exercise powers granted under Federal law; they do not obstruct or condition a national bank’s exercise of those powers.” *Id.*

327. See Wilmarth, *supra* note 93, at 235–36, 316–17 (describing the sweeping preemptive claims asserted by the OCC in the preamble to its 2004 preemption rules).

words, as I pointed out in 2004, the OCC’s theory allows “only *helpful* state laws” to apply to national banks, thereby creating “a regime of field preemption in everything but name.”³²⁸

The Supreme Court strongly criticized the OCC’s “legal infrastructure” theory in *Cuomo*.³²⁹ The Court declared that the OCC’s theory “does not comport with the [NBA]” because the theory “attempts to do what Congress declined to do: exempt national banks from all state banking laws, or at least state enforcement of those laws.”³³⁰ Thus, *Cuomo* severely undermined the theoretical justification underlying the OCC’s 2004 preemption rules.

In addition, the Senate committee report and the conference report on Dodd–Frank confirm that the *Barnett Bank* standard incorporated in Section 5136C(b)(1)(B) overrides the OCC’s preemption test and allows a wider range of state consumer financial laws to apply to national banks. The Senate committee report explains:

Section 1044 [of Dodd–Frank] amends the National Bank Act to clarify the preemption standard relating to State consumer financial laws as applied to national banks The standard for preempting State consumer financial law would return to what it had been for decades, those recognized by the Supreme Court in *Barnett Bank v. Nelson*, 517 U.S. 25 (1996), *undoing broader standards adopted by rules, orders, and interpretations issued by the OCC in 2004*.³³¹

Similarly, the conference report affirms that Dodd–Frank “*revises* the standard the OCC will use to preempt state consumer protection laws. It codifies the standard in the 1996 Supreme Court case of [*Barnett Bank*].”³³² Therefore, notwithstanding recent statements by lawyers representing national banks,³³³ the OCC’s 2004 preemption test will not be valid when Section 5136C(b)(1)(B) becomes effective on July 21, 2011.³³⁴

328. *Id.* at 236, 317.

329. *Cuomo v. Clearing House Ass’n*, 129 S. Ct. 2710 (2009).

330. *Id.* at 2719–20. In *Cuomo* the Supreme Court rejected the OCC’s invocation of its “legal infrastructure” doctrine in support of another preemption rule, which attempted to bar state officials from bringing any actions to enforce state laws against national banks. *See id.* at 2719–20 (quoting and discussing Bank Activities and Operations, 69 Fed. Reg. 1895, 1896 (2004)). The Court held that the OCC lacked authority to prevent state attorneys general from bringing judicial proceedings to enforce non-preempted state laws against national banks. *Id.* at 2720–22.

331. S. REP. NO. 111-176, at 175 (2010) (emphasis added).

332. H.R. REP. NO. 111-517, at 875 (2010) (Conf. Rep.), *reprinted in* 2010 U.S.C.C.A.N. 722, 731 (emphasis added).

333. Cheyenne Hopkins, *Preemption After Dodd–Frank May Not Be As Weak As You Heard*, AM. BANKER, Mar. 15, 2011, at 1 (quoting (i) comment by Robert Cook that “[t]he substance of federal preemption analysis hasn’t changed at all,” and (ii) statement by Howard Cayne that “Congress made no change to preemption as it applies to national banks”).

334. *See supra* note 244 and accompanying text (explaining that Title X of Dodd–Frank takes effect on July 21, 2011).

b. The OCC's Blanket Preemption Rules Are No Longer Valid in View of Dodd–Frank's Mandate for "Case-by-Case" Determinations Supported by "Substantial Evidence"

As discussed above, Section 5136C(b) requires the OCC (i) to make each preemption determination on a "case-by-case basis," and (ii) to consult with the CFPB before deciding that additional state laws are subject to preemption because their terms are "substantively equivalent" to a particular law that the OCC has preempted.³³⁵ In addition, under Section 5136C(c), the OCC must demonstrate that each of its preemption determinations is justified by "substantial evidence, made on the record of the proceeding," which "supports the specific finding regarding the preemption of such [state law] in accordance with the legal standard of [*Barnett Bank*]."³³⁶ The OCC's 2004 preemption rules do not satisfy any of these requirements.

The OCC's preemption rules violate Dodd–Frank's "case-by-case" requirement because (i) they preempt broad categories of state law and do not contain any individualized analysis of why particular state laws violate the *Barnett Bank* standard, and (ii) the OCC did not consult with the CFPB before adopting its categorical preemptions of multiple state laws.³³⁷ Indeed, the OCC acknowledged when it issued its rules that it was "identifying [preempted] state laws in a more generic way."³³⁸ The OCC's 2004 rulemaking also did not contain Dodd–Frank's required demonstration of "substantial evidence" to justify each OCC determination that a particular state law ran afoul of the *Barnett Bank* standard.³³⁹ Rather, the OCC gave only scattered examples of state laws that allegedly "created higher costs and increased operational challenges" for national banks, and the OCC justified its across-the-board preemption rules by declaring that national banks should be free to operate under "uniform, consistent, and predictable standards . . . without interference from inconsistent state laws, consistent with the national character of the national banking system."³⁴⁰ That generalized assertion cannot be squared with Dodd–Frank's adoption of the *Barnett Bank* preemption standard or with Dodd–Frank's mandate that the OCC must make preemption determinations on a "case-by-case" basis and with support from "substantial evidence" in the record. Hence, the OCC's 2004 preemption rules must be rescinded in their entirety, and any replacement rules must comply fully with Dodd–Frank's requirements.

c. The OCC's Preemptive Rule for Operating Subsidiaries Conflicts with Dodd–Frank

As described above, Section 5136C contains three provisions that affirm the applicability of state laws to non-bank subsidiaries, affiliates, or agents of national banks.³⁴¹ Those provisions require the OCC to rescind a preemptive regulation issued in

335. Dodd–Frank § 1044 (to be codified at 12 U.S.C. §§ 25b(b)(1)(B), (b)(1)(B), (b)(3)).

336. *Id.* (to be codified at 12 U.S.C. § 25b(c)).

337. *Compare id.* (to be codified at 12 U.S.C. § 25b(b)(1)(B), (b)(3)) (establishing new preemption standards under the NBA) with 12 C.F.R. §§ 7.4007(b), 7.4008(d), 7.4009(b), 34.4(a) (2010) (OCC regulations declaring broad preemptions of general categories of state laws instead of providing an individualized list of state statutes and regulations to be preempted).

338. Bank Activities and Operations; Real Estate Lending and Appraisals, 69 Fed. Reg. 1911 (Jan. 13, 2004).

339. Dodd–Frank § 1044 (to be codified at 12 U.S.C. § 25b(c)).

340. Bank Activities and Operations; Real Estate Lending and Appraisals, 69 Fed. Reg. at 1908.

341. *See supra* Part III.D.2.d (discussing §§ 5136C(b)(2), (e), (h)).

2001, which declared that operating subsidiaries are entitled to the same preemptive immunity from state laws as their parent national banks enjoy under the NBA.³⁴² The Supreme Court upheld that regulation in its 2007 decision in *Watters*.³⁴³ However, Dodd–Frank overrules the Court’s decision and mandates that non-bank subsidiaries, affiliates, and agents of national banks must comply with applicable state laws.³⁴⁴

d. The OCC’s Existing Preemption Rules Must Conform to Dodd–Frank by July 21, 2011

Some commentators have suggested that the preemption provisions of Dodd–Frank apply only to “future [OCC preemption] determinations, and [therefore] previous agency rulings still stand.”³⁴⁵ However, four provisions of Dodd–Frank make clear that all but one of the OCC’s existing preemption rules will be invalid unless they are brought into conformity with Dodd–Frank’s new preemption standards by July 21, 2011.

First, Section 5136C(b)(1) provides that “State consumer financial laws are preempted, *only if*” such laws violate one of the three preemption standards contained in that paragraph.³⁴⁶ The “only if” language makes clear that Dodd–Frank’s new preemption standards establish the controlling and *exclusive* requirements for justifying any preemption of state consumer financial laws.³⁴⁷ Second, Section 1048 of Dodd–Frank provides that the new preemption standards for the NBA and HOLA established by Sections 1044 through 1047 “shall become effective on the designated transfer date” (*viz.*, July 21, 2011).³⁴⁸ Subject to two special carve-outs described below, Section 1048 requires the OCC’s to comply fully with the new preemption standards on and after July 21, 2011.

Third, Section 5136C(f) expressly preserves the existing authority of each national bank, under 12 U.S.C. § 85, to charge interest “at the rate allowed by the laws of the State . . . where the bank is located.”³⁴⁹ Subsection (f) also preserves “the meaning of ‘interest’ under [12 U.S.C. § 85].”³⁵⁰ The Senate committee report explains that Dodd–Frank “does not alter or affect existing laws regarding the charging of interest by national banks.”³⁵¹ Thus, Subsection (f) preserves the OCC’s existing preemptive regulation

342. See Investment Securities: Bank Activities and Operations; Leasing, 66 Fed. Reg. 34,784–34,790 (July 2, 2001) (adopting 12 C.F.R. § 7.4006 (2008)).

343. *Watters v. Wachovia Bank, N.A.*, 550 U.S. 1 (2007).

344. Saunders, *supra* note 235, at 5 (explaining that “Dodd–Frank ends preemption for bank operating subsidiaries by reversing *Watters v. Wachovia Bank* and the regulation *Watters* upheld”) (footnote omitted); Perkins & DeSimone, *supra* note 313, at 761 (agreeing that Dodd–Frank “effectively reverses the holding of *Watters*”); see also S. REP. NO. 111-176, at 176 (2010) (explaining that, under Dodd–Frank, “State law applies to State-chartered nondepository institution subsidiaries, affiliates, and agents of national banks, other than entities that are themselves chartered as national banks”).

345. Hopkins, *supra* note 333 (summarizing comments by unnamed “preemption advocates”).

346. Dodd–Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 1044, 124 Stat. 1376, 2015 (2010) (to be codified at 12 U.S.C. § 25b(b)(1)) (emphasis added).

347. See S. REP. NO. 111-176, at 175 (2010) (explaining that “Section 1044 amends the [NBA] to clarify the preemption standard relating to State consumer financial laws as applied to national banks,” and “this section sets out three circumstances under which a State consumer financial law can be preempted”).

348. Dodd–Frank § 1048; see also *supra* note 244 (explaining that the effective date for Dodd–Frank’s new preemption standards is July 21, 2011).

349. Dodd–Frank § 1044 (to be codified at 12 U.S.C. § 25b(f)).

350. *Id.*

351. S. REP. NO. 111-176, at 176.

defining the meaning of “interest” under Section 85, as well as interpretive rulings and court decisions that have given national banks “most favored lender” status and an expansive power to “export” interest rates across state lines under Section 85.³⁵²

Section 5136C(f)’s explicit preservation of the OCC’s existing preemption regulation under 12 U.S.C. § 85 provides strong evidence of Congress’s intent—as also manifested in Section 1048—that the OCC’s preemption rules in *other* areas must be brought into compliance with Title X of Dodd–Frank by July 21, 2011.³⁵³ This congressional understanding is confirmed by the fourth relevant provision of Dodd–Frank—Section 1043. Section 1043 provides that Title X of Dodd–Frank and CFPB’s regulations and orders thereunder:

shall not be construed to affect the applicability of any rule, order, guidance or interpretation by the OCC or OTS regarding the preemption of State law by a Federal banking law to any contract entered into by banks, thrifts, or affiliates and subsidiaries thereof, prior to the date of enactment of the CFP Act.³⁵⁴

As explained in the Senate committee report, Section 1043 is intended to “provide stability to existing contracts” by preserving the applicability of OCC and OTS preemptive rulings to contracts that were made *before* the enactment date of Dodd–Frank.³⁵⁵ There would have been no reason for Congress to enact Section 1043 if Congress had intended to allow existing OCC and OTS preemption rules to apply to *new* consumer financial agreements that are made *after* July 21, 2010.

Thus, apart from Dodd–Frank’s two special carve-outs for (i) the OCC’s preemptive regulation governing the charging of “interest,” and (ii) the continued application of the OCC’s existing preemption rules to contracts made by national banks and federal thrifts before July 22, 2010, the OCC’s preemption rules will *not* be valid after July 21, 2011, *unless* they are brought into full compliance with the new preemption standards and requirements established by Section 5136C.³⁵⁶ Remarkably, as of March 2011—eight

352. See 12 C.F.R. § 7.4001 (2010) (defining the meaning of “interest” for purposes of 12 U.S.C. § 85 and the authority of each national bank to charge “interest” based on the law of the state where the bank is “located”). Because the term “interest” is not defined in 12 U.S.C. § 85, section 5136C(f)’s explicit preservation of the “meaning of ‘interest’” is obviously intended to preserve the validity of the OCC’s definition of “interest” in 12 C.F.R. § 7.4001(a). See generally Elizabeth R. Schiltz, *The Amazing, Elastic, Ever-Expanding Exportation Doctrine and Its Effect on Predatory Lending Regulation*, 88 MINN. L. REV. 518 (2004) (providing a comprehensive analysis of the “most favored lender” and “exportation” doctrines under 12 U.S.C. § 85).

353. See *infra* note 356 (describing two canons of statutory construction that support the foregoing conclusion).

354. Dodd–Frank § 1043 (to be codified at 12 U.S.C. § 5553).

355. S. REP. NO. 111-176, at 175 (2010) (emphasis added). The scope of § 1043’s grandfather clause is not entirely clear. For example, it is not clear whether a pre-2010 contract made by a national bank would continue to receive grandfathered treatment under Section 1043 (and would continue to be governed by the OCC’s 2004 preemption rules) if that contract is modified in any way after July 21, 2010.

356. As shown above, Dodd–Frank’s carve-outs permit the OCC’s existing preemption rules to have continued application under two narrowly limited circumstances. In view of those carve-outs, the canon of statutory construction known as *expressio unius est exclusio alterius* supports the conclusion that Congress did *not* intend to preserve the OCC’s existing preemption rules in any other area *unless* those rules conform to Dodd–Frank’s new preemption standards. See *First Nat’l Bank in St. Louis v. Missouri*, 263 U.S. 640, 657-58 (1924) (holding, in view of federal statutes granting branching permission to national banks only in carefully limited circumstances, that national banks did not have authority to establish branches under any other circumstances); *Indep. Ins. Agents of Am., Inc. v. Hawke*, 211 F.3d 638, 644-45 (D.C. Cir. 2000) (holding,

months after Dodd–Frank’s enactment and only four months before the effective date of Section 5136C—the OCC had not issued any public notice indicating how it intended to respond to the new standards and requirements of Section 5136C.³⁵⁷ Indeed, the OCC had not yet modified its visitorial powers regulation, even though the Supreme Court’s 2009 decision in *Cuomo* invalidated a portion of that regulation.³⁵⁸

4. *Dodd–Frank Affirms the Authority of State AGs to Enforce Applicable Laws Against National Banks*

Section 1047(a) of Dodd–Frank enacts a new section 5136C(i) of the NBA.³⁵⁹ Section 5136C(i) provides:

In accordance with the decision of the Supreme Court . . . in [*Cuomo*], no provision of [the NBA] which relates to visitorial powers or otherwise limits or restricts the visitorial authority to which any national bank is subject shall be construed as limiting or restricting the authority of any attorney general (or other chief law enforcement officer) of any State to bring an action against a national bank in a court of appropriate jurisdiction to enforce an applicable law and to seek relief as authorized by such law.³⁶⁰

Thus, Subsection (i) expressly endorses the Supreme Court’s decision in *Cuomo*,³⁶¹ which held that the NBA does *not* preempt the authority of a state attorney general (AG) to seek judicial enforcement of non-preempted state laws against national banks.³⁶² Subsection (i) also evidently upholds the right of a state AGs to seek judicial enforcement of any applicable federal law “as authorized by such law,” because Subsection (i) refers to the enforcement of “applicable law” rather than “applicable State law.”³⁶³

based in part on the *expressio unius* canon, that a federal statute allowing national banks to sell insurance in towns under 5000 provided compelling evidence of Congress’ intent not to allow national banks to sell insurance at other locations). The canon against “surplusage” leads to the same conclusion. The two special carve-outs in Dodd–Frank would be rendered “meaningless,” in violation of that canon, if the OCC were allowed to retain all of its existing preemption rules despite their nonconformity with Dodd–Frank’s new preemption standards. *Hawke*, 211 F.3d at 643–45; *see also* *Arkansas Best Corp. v. Comm’r*, 485 U.S. 212, 218 (1988) (refusing to interpret a federal tax statute “in a manner that makes surplusage of [five special] statutory exclusions”).

357. Hopkins, *supra* note 333.

358. In *Cuomo v. Clearing House Association*, the Court invalidated 12 C.F.R. § 7.4000 to the extent that the regulation barred state officials from seeking judicial enforcement of non-preempted state laws against national banks. *Cuomo v. Clearing House Ass’n*, 129 S. Ct. 2710, 2721–22 (2009). As of April 5, 2011, the Government Printing Office website showed that the OCC had not amended 12 C.F.R. § 7.4000 since January 13, 2004, and that subsections (a)(iv) and (b)(2) of that regulation remained in force. The OCC relied on those subsections in *Cuomo* to support its claim that state officials were prohibited from suing national banks to enforce non-preempted state laws. The Supreme Court held that the OCC lacked authority to adopt such a prohibition. *See Cuomo*, 129 S. Ct. at 2714–15, 2721–22; *id.* at 2722 (Thomas, J., dissenting); *see also Electronic Code of Federal Regulations*, U.S. GOV’T PRINTING OFFICE, <http://ecfr.gpoaccess.gov/cgi/t/text/text-idx?c=ecfr&sid=d7126a89d8938f9481bc8ea5e8083dca&rgn=div8&view=text&node=12:1.0.1.1.7.4.4.1&idno=12> (last visited June 29, 2011) (reprinting 12 C.F.R. § 7.4000 as in effect on April 5, 2011).

359. Dodd–Frank § 1047(a) (to be codified at 12 U.S.C. § 25b(i)).

360. *Id.*

361. *Cuomo*, 129 S. Ct. at 2710 (2009).

362. Saunders, *supra* note 235, at 9; Wilmarth, *supra* note 112, at 1–12, 16–19.

363. Dodd–Frank § 1047(a) (enacting § 5136C(i) of the NBA).

Interpreting Subsection (i) to permit state AGs to enforce applicable federal law “as authorized by such law” would be consistent with the Supreme Court’s reasoning in *Cuomo*. In *Cuomo*, the Court held that “ordinary enforcement of the law” by state AGs through the courts does not represent a prohibited exercise of “visitorial powers” over national banks.³⁶⁴ Moreover, the NBA itself indicates that state officials may exercise “visitorial powers” over national banks to the extent “authorized by Federal law.”³⁶⁵

Dodd–Frank’s explicit incorporation of *Cuomo* provides a significant benefit to the states because it effectively removes the possibility that *Cuomo* (a 5–4 decision) might have been overruled by a subsequent decision of the Supreme Court. Without Dodd–Frank’s affirmation of *Cuomo*, such a possibility would have been a matter of potential concern to the states, in view of the fact that two members of the majority in *Cuomo* (Justices Souter and Stevens) have subsequently retired from the Court.

5. *Dodd–Frank Establishes Preemption Standards under HOLA That Are Equivalent to Those Embodied in the NBA*

Dodd–Frank enacts a new Section 6 of HOLA.³⁶⁶ Section 6(a) provides that every preemption determination made by a court or agency under HOLA “shall be made in accordance with the laws and legal standards applicable to national banks regarding the preemption of State law.”³⁶⁷ Thus, Dodd–Frank establishes new preemption standards for state consumer financial laws under HOLA that are equivalent to the new preemption standards created under Section 5136C of the NBA for national banks.³⁶⁸ This outcome appears to create a significant change in existing law. Before Dodd–Frank was enacted, several lower courts concluded that the OTS had a broader power to preempt state law under HOLA than the OCC possessed under the NBA.³⁶⁹

Section 6(b) declares that HOLA “does not occupy the field in any area of State law.”³⁷⁰ Thus, future preemption determinations under HOLA must be based on conflict preemption principles. In addition, Section 6(c) provides that the authority of state AGs to seek judicial enforcement of “applicable law” against national banks under section 5136C(i) “shall apply to Federal savings associations, and any subsidiary thereof, to the same extent and in the same manner, as if such savings associations, or subsidiaries thereof, were national banks or subsidiaries of national banks, respectively.”³⁷¹ Thus, Section 6(c) incorporates Section 5136C(i) and its affirmation of the right of state officials to seek judicial enforcement of applicable laws against federally-chartered depository

364. *Cuomo*, 129 S. Ct. at 2715, 2721–22.

365. 12 U.S.C. § 484(a) (2006).

366. Dodd–Frank §§ 1046, 1047(b) (enacting § 6 of HOLA).

367. *Id.* § 1046 (enacting § 6(a) of HOLA).

368. *See* S. REP. NO. 111-176, at 176 (2010) (“Section 1046 amends [HOLA] to clarify that State law preemption standards for Federal savings associations and their subsidiaries shall be made in accordance with the standards applicable to national banks.”).

369. *See, e.g.,* *Bank of Am. v. City of San Francisco*, 309 F.3d 551, 558–64 (9th Cir. 2002), *cert. denied*, 538 U.S. 1069 (2003) (holding that HOLA established a regime of field preemption while preemption issues under the NBA should be determined based on conflict preemption principles). *See also* Wilmarth, *supra* note 93, at 321–24 (discussing other lower court decisions indicating that the OTS possessed a broader authority under HOLA to adopt rules preempting state laws than the OCC was granted under the NBA).

370. Dodd–Frank § 1046 (enacting § 6(b) of HOLA).

371. *Id.* § 1047(b) (enacting § 6(c) of HOLA).

institutions.³⁷²

Dodd–Frank’s denial of field preemption under HOLA will require the OCC to rescind, or fundamentally rewrite, three of the OTS’s preemptive regulations.³⁷³ Those regulations purport to occupy the field with respect to the deposit-taking, lending, and other “operations” of federal thrifts and are therefore incompatible with Section 6(b)’s conflict preemption regime. Similarly, the new preemption standards for national banks contained in Section 5136C of the NBA—which will apply to federal thrifts under Section 6(a) of HOLA after July 21, 2011—will require the rescission or modification of many of the provisions contained in the OTS’s preemptive regulations with respect to deposit-taking, lending and other “operations.”³⁷⁴ Those OTS regulations are similar to the OCC’s 2004 blanket preemption rules, discussed above, and therefore do not comply with the requirements of Section 5136C for (i) application of the “prevents or significantly interferes with” preemption standard, (ii) “case-by-case” preemption determinations instead of broad categorical rules, and (iii) a showing of “substantial evidence” supporting each preemption determination.³⁷⁵

In addition, Section 6(a)’s incorporation of Section 5136C(b)(2), (e), and (h) mandates the application of state laws to subsidiaries, affiliates, and agents of federal thrifts.³⁷⁶ As discussed above, Section 5136C(b)(2), (e), and (h) effectively overrule the preemptive immunity that operating subsidiaries and agents of national banks were granted by an OCC regulation and court decisions.³⁷⁷ Consequently, Section 6(a) will require rescission of (i) an OTS preemptive regulation that purports to give operating subsidiaries a general immunity from state laws,³⁷⁸ and (ii) an OTS preemptive ruling that provided a comparable immunity to agents of federal thrifts.³⁷⁹

Like the new Section 5136C of the NBA, the new section 6 of HOLA does not establish an explicit preemption standard for state laws of general applicability because those laws do not fall within the definition of “State consumer financial laws.”³⁸⁰ However, Section 6(a) provides that any preemption determination “regarding the relation of State law to a provision of [HOLA]” must be “made in accordance with the laws and legal standards applicable to national banks regarding the preemption of State law.”³⁸¹ As shown in the next Part, Supreme Court decisions indicate that general state

372. See *supra* Part III.D.4 (discussing § 5136C(i) of the NBA).

373. 12 C.F.R. §§ 557.11(b), 560.2(a), 545.2 (2010). As of July 21, 2011 (the “designated transfer date”), the OCC will assume responsibility for administering and enforcing the OTS’s regulations governing federally-chartered thrifts. See *supra* notes 160, 192, 244 and accompanying text.

374. *Id.*

375. See *supra* Parts III.D.3.a, III.D.3.b (explaining why the OCC’s 2004 preemption rules do not comply with the requirements of § 5136C); Wilmarth, *supra* note 93, at 228, 233–35 (describing the close similarity between the OCC’s and the OTS’s preemption rules).

376. See *supra* Parts III.D.2.d, III.D.3.c (discussing Sections 5136C(b)(2), (e), (h) of the NBA).

377. See *id.* (discussing court decisions overruled by Sections 5136C(b)(2), (e) and (h)).

378. See 12 C.F.R. § 559.3(n) (declaring that state laws are preempted from applying to operating subsidiaries to the same extent that such laws are preempted with respect to the parent thrifts).

379. See *State Farm Bank, F.S.B. v. Reardon*, 539 F.3d 336 (6th Cir. 2008) (upholding OTS ruling declaring that agents of a federal thrift did not have to comply with state laws regulating mortgage brokers).

380. See *supra* note 248 and accompanying text (discussing Dodd–Frank’s definition of “State consumer financial laws”).

381. Dodd–Frank § 1046 (enacting § 6(a) of HOLA).

laws presumptively apply to national banks.³⁸² Section 6(a) will require the courts and federal agencies to apply the same standard in determining the application of general state laws to federal thrifts.

6. Dodd–Frank Does Not Address State Laws of General Application, But Those Laws Should Presumptively Apply to National Banks under Existing Judicial Precedents

As explained above, Dodd–Frank establishes a new preemption standard for national banks and federal thrifts that refers only to “State consumer financial laws” and does not mention state laws of general application.³⁸³ Accordingly, Dodd–Frank’s new preemption standards and requirements do not alter the applicability of general state laws to national banks and federal thrifts.³⁸⁴ In these circumstances, two background assumptions support the presumptive application of state laws to national banks.

First, when construing a “federal statutory scheme that is comprehensive and detailed” the Supreme Court has opined that “matters left unaddressed in such a scheme are presumably left subject to the disposition provided by state law.”³⁸⁵ Accordingly, Dodd–Frank’s silence with regard to preemption of general state laws should raise an inference that Congress contemplated the presumptive application of such laws to national banks.³⁸⁶ Second, the Court has explained that “Congress is presumed to be aware of an administrative or judicial interpretation of a statute and to adopt that interpretation when it re-enacts a statute without change.”³⁸⁷ Consequently, Section 5136C should be construed in harmony with Supreme Court decisions that predated Dodd–Frank and defined the applicability of general state laws to national banks. As shown below, those decisions support a presumption in favor of applying state laws of general application to national banks.

In its 2009 decision in *Cuomo*,³⁸⁸ the Supreme Court declared that: “States . . . have always enforced their general laws against national banks—and have enforced their banking-related laws against national banks for at least 85 years, as evidenced by [*First National Bank in St. Louis v. Missouri*],³⁸⁹ in which we upheld enforcement of a state

382. Part III.D.6, *infra*.

383. *See supra* notes 248–49 and accompanying text (discussing the fact that Dodd–Frank’s new preemption standards apply only to “State consumer financial laws” and do not apply to general state laws).

384. *See* S. REP. NO. 111-176, at 175 (2010) (stating that Dodd–Frank’s new preemption standard for national banks and federal thrifts “does not alter the preemption standards for State laws of general applicability to business conduct”).

385. *O’Melveny & Myers v. FDIC*, 512 U.S. 79, 85 (1994).

386. Similarly, the House-Senate conference report on a 1994 interstate banking statute expressed the conferees’ agreement with the general application of state laws to national banks. The conferees explained that “[u]nder well-established judicial principles, national banks are subject to State law in many significant respects. . . . Courts generally use a rule of construction that avoids finding a conflict where possible.” H.R. REP. NO. 103-651 at 53 (Conf. Rep.), *reprinted in* 1994 U.S.C.C.A.N. 2068, 2074. The conferees added that the 1994 legislation “does not change these judicially-established principles.” *Id.*; *see also* Wilmarth, *supra* note 93, at 208–09 (contending that the conference report supports the view that “Congress strongly reaffirmed its support for the general application of state laws to national banks when it passed the [1994 legislation]”).

387. *Forest Grove Sch. Dist. v. T.A.*, 129 S. Ct. 2484, 2492 (2009) (quoting *Lorillard v. Pons*, 434 U.S. 575, 580 (1978)).

388. *Cuomo v. Clearing House Ass’n*, 129 S. Ct. 2710 (2009).

389. *First Nat’l Bank in St. Louis v. Missouri*, 263 U.S. 640, 656 (1924).

anti-bank-branching law.”³⁹⁰

Thus, *Cuomo* affirmed the applicability of “general [state] laws” to national banks.³⁹¹ When Congress passed Dodd–Frank, it was plainly aware of the Court’s opinion in *Cuomo* because, as discussed above, Congress expressly adopted *Cuomo* as the governing standard for defining the states’ judicial enforcement authority against national banks under Section 5136C(i).³⁹²

Moreover, the *St. Louis* decision—which *Cuomo* explicitly endorsed—supports the view that a presumption against preemption should be applied in determining whether general state laws apply to national banks. *St. Louis* held that, under the NBA, “the rule [is] the operation of general state laws upon the dealings and contracts of national banks,” while preemption is an “exception” that applies only when state laws “expressly conflict with the laws of the United States or frustrate the purpose for which national banks were created, or impair their efficiency to discharge the duties imposed upon them by the law of the United States.”³⁹³ Thus, the presumptive “rule” under *St. Louis* is the applicability of “general state laws” to the business operations of national banks.³⁹⁴

Cuomo and *St. Louis* are consistent with *Atherton v. FDIC*,³⁹⁵ which declared that “federally chartered banks are subject to state law.”³⁹⁶ As support for that principle, *Atherton* quoted prior Supreme Court decisions reaching back to *National Bank v. Commonwealth*³⁹⁷—issued only six years after the NBA’s enactment—where the Supreme Court held that national banks

[a]re subject to the laws of the State, and are governed in their daily course of business far more by the laws of the State than of the nation. All their contracts are governed and construed by State laws. Their acquisition and transfer of property, their right to collect their debts, and their liability to be sued for debts, are all based on State law. It is only when State law incapacitates the [national] banks from discharging their duties to the [federal] government that it becomes unconstitutional.³⁹⁸

Thus, *Commonwealth* upheld the applicability of general state laws to national banks unless such laws “incapacitate[d]” national banks from fulfilling their “duties” to the United States. Under the NBA as originally enacted in 1863 and amended in 1864, the duties of national banks were (i) to issue a national currency in the form of national bank notes, and (ii) to purchase and deposit Treasury bonds with the United States Treasury to ensure the payment of those notes.³⁹⁹ The foregoing duties were phased out following

390. *Cuomo*, 129 S. Ct. at 2720.

391. *Id.*

392. *See supra* Part III.D.4 (discussing the incorporation of *Cuomo* in section 5136C(i) of the NBA).

393. *St. Louis*, 263 U.S. at 656 (quoting *McClellan v. Chipman*, 164 U.S. 347, 357 (1896)).

394. *Id.*

395. *Atherton v. FDIC*, 519 U.S. 213 (1997).

396. *Id.* at 222.

397. *National Bank v. Commonwealth*, 76 U.S. (9 Wall.) 353 (1870).

398. *Atherton*, 519 U.S. at 222–23 (quoting *Commonwealth*, 76 U.S. at 362).

399. Levitin, *supra* note 17, at 174–75; Wilmarth, *supra* note 93, at 241, 241–42 n.60; *see also* *Tiffany v. Nat’l Bank of Missouri*, 85 U.S. 409, 413 (1874) (observing that national banks 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”).

enactment of the Federal Reserve Act in 1913, and national banks stopped issuing bank notes by 1935.⁴⁰⁰ Accordingly, the “duties” referred to in *Commonwealth* are no longer relevant, and general state laws therefore apply to national banks in the absence of a direct and irreconcilable conflict with federal law.⁴⁰¹

Commonwealth’s affirmation that state law generally controls the “right [of national banks] to collect their debts” as well as “their contracts” and “[t]heir acquisition and transfer of property” was quoted with approval in *McClellan v. Chipman*.⁴⁰² *McClellan* held that a national bank was required to comply with a Massachusetts statute that prohibited any transfer of property by an insolvent debtor “with a view to give a preference to a creditor or person who has a claim against him.”⁴⁰³ *McClellan* upheld the applicability of the Massachusetts statute even though the state law imposed a limitation on the express power of national banks to accept transfers of real property in satisfaction of debts previously contracted under 12 U.S.C. § 29. The Supreme Court explained:

No function of such [national] banks is destroyed or hampered by allowing the banks to exercise the power to take real estate, provided only they do so under the same conditions and restrictions to which all the other citizens of the State are subjected, one of which limitations arises from the provisions of the state law which in case of insolvency seeks to forbid preferences between creditors.⁴⁰⁴

Thus, *McClellan* found “no conflict between the special power conferred by Congress upon national banks to take real estate for certain purposes, and the general and undiscriminating law of the State of Massachusetts subjecting the taking of real estate to certain restrictions, in order to prevent preferences in cases of insolvency.”⁴⁰⁵

Similarly, in *Anderson National Bank v. Lockett*⁴⁰⁶ the Court held that national banks were required to comply with a Kentucky statute that required all banks to transfer dormant deposit accounts to state authorities for a determination of whether such accounts had been abandoned and should be escheated to the state.⁴⁰⁷ A national bank, supported by the OCC as *amicus curiae*, challenged the Kentucky statute on grounds of preemption.⁴⁰⁸ The Supreme Court rejected the bank’s preemption claim, declaring that “the mere fact that the depositor’s account is in a national bank does not render it immune to attachment by creditors of the depositor, as authorized by state law.”⁴⁰⁹ The Court further explained that:

[A] bank account is . . . part of the mass of property within the state whose transfer and devolution is subject to state control It has never been suggested that non-discriminatory [state] laws of this type are so burdensome

400. Levitin, *supra* note 17, at 175.

401. *Id.*; Wilmarth, *supra* note 93, at 241–46.

402. *McClellan v. Chipman*, 164 U.S. 347, 357 (1896).

403. *Id.* at 348 (quoting 157 Mass. Pub. Stat. § 96 (1882)).

404. *Id.* at 358.

405. *Id.* at 359, 361.

406. *Anderson Nat’l Bank v. Lockett*, 321 U.S. 233 (1948).

407. *Id.* at 247.

408. *Id.* at 236.

409. *Id.* at 248.

as to be inapplicable to the accounts of depositors in national banks.⁴¹⁰

Luckett thereby confirmed that the power of national banks to accept deposits is subject to nondiscriminatory, general state laws establishing contract rights and creditors’ rights with respect to personal property, including deposit accounts. In this regard, the Supreme Court held that:

[A]n inseparable incident of a national bank’s privilege of receiving deposits is its obligation to pay them to the persons entitled to demand payment according to the law of the state where it does business. A demand for payment of an account by one entitled to make the demand does not infringe or interfere with any authorized function of the bank.⁴¹¹

As noted above, courts generally follow a canon of statutory construction that Congress is presumed to approve judicial interpretations of portions of a statute that Congress reenacts without change.⁴¹² Because the NBA, as amended by Section 5136C, does not mention any preemption of general state laws,⁴¹³ courts should construe the NBA in harmony with *Cuomo*, *Commonwealth*, *McClellan*, *Luckett*, and *Atherton*, all of which support the presumptive application of general state laws to national banks. Thus, Section 5136C should be deemed to leave undisturbed existing Supreme Court precedents governing the application of general state laws to national banks.

The Supreme Court’s decision in *Wyeth v. Levine*⁴¹⁴ provides further support for the conclusion that state laws of general application presumptively apply to national banks. In *Wyeth*, the Supreme Court held that provisions of the Federal Food, Drug, and Cosmetic Act (FDCA) governing the approval of drug labels by the Food and Drug Administration (FDA) did not preempt failure-to-warn claims under state tort law.⁴¹⁵ In reaching that conclusion, the Court noted that Congress had expressly preempted state common-law claims with respect to “medical devices” but had not passed any similar law with respect to drug labeling.⁴¹⁶ Moreover, Congress was aware of the existence of state common-law remedies when it enacted and amended the FDCA.⁴¹⁷ The Court held that

[Congress’] silence on this issue, coupled with its certain awareness of the prevalence of state tort litigation, is powerful evidence that Congress did not intend FDA oversight to be the exclusive means of ensuring drug safety and effectiveness. As Justice O’Connor explained in her opinion for a unanimous Court: ‘The case for federal pre-emption is particularly weak where Congress has indicated its awareness of the operation of state law in a field of federal interest, and has nonetheless decided to stand by both concepts and to tolerate

410. *Id.* (citations omitted).

411. *Anderson*, 321 U.S. at 248–49.

412. *See supra* note 387 and accompanying text (citing and quoting *Forest Grove Sch. Dist. v. T.A.*, 129 S. Ct. 2484, 2492 (2009)).

413. *See supra* notes 248–49 and accompanying text (explaining that the new preemption standards in Section 5136C refer only to “State consumer financial laws” and do not mention state laws of general application).

414. *Wyeth v. Levine*, 555 U.S. 555, 129 S. Ct. 1187 (2009).

415. *Id.* at 1204.

416. *Id.* at 1200.

417. *Id.* at 1199 n.7, 1199–1200.

whatever tension there [is] between them.”⁴¹⁸

The Court’s reasoning in *Wyeth* strongly supports the presumptive application of general state laws to national banks.⁴¹⁹ With respect to national banks, Dodd–Frank has established an express preemption regime for “State consumer financial laws,” whose contours are carefully defined by Section 5136C, in the same manner that the FDCA prescribes an express preemption regime for “medical devices.”⁴²⁰ However, Dodd–Frank does not establish any system of express preemption for national banks with regard to state laws of general application (including state common-law rules governing contracts, property rights, and torts) in the same way that the FDCA does not prescribe a system of express preemption for drug labels. Under these circumstances, *Wyeth* held that the courts should apply a “presumption against pre-emption” of general state laws despite the federal government’s regulatory presence in the field.⁴²¹ *Wyeth* explained:

We rely on the presumption [against preemption] because respect for the States as ‘independent sovereigns in our federal system’ leads us to assume that ‘Congress does not cavalierly pre-empt state-law causes of action,’ *Medtronic, Inc. v. Lohr*, 518 U.S. 470, 485 (1996). The presumption thus accounts for the historic presence of state law but does not rely on the absence of federal regulation.⁴²²

In *Cuomo*, the Court indicated that the reasoning of *Wyeth* also applies to the NBA, because the Court cited *Wyeth* to illustrate its observation that the simultaneous application of federal and state laws to national banks “echoes many other mixed state/federal regimes in which the Federal Government exercises general oversight while leaving state substantive law in place.”⁴²³ As shown above, several of the Court’s decisions under the NBA provide additional support for the conclusion that general state laws presumptively apply to national banks.⁴²⁴

IV. TITLE X OF DODD–FRANK CREATES A REGIME OF INTERACTIVE FEDERALISM THAT WILL PROVIDE BETTER SAFEGUARDS FOR CONSUMERS OF FINANCIAL SERVICES

Title X of Dodd–Frank establishes a regime of “interactive federalism” by granting overlapping powers to CFPB and state officials to adopt and enforce consumer financial protection laws.⁴²⁵ The interactive regime created by Title X is likely to produce

418. *Id.* at 1200 (quoting *Bonita Boats, Inc. v. Thunder Craft Boats, Inc.*, 489 U.S. 141, 166–67 (1989) (internal quotation marks omitted)).

419. *See* *Smith v. BAC Home Loans Servicing, LP*, No. 2110-w-00364, 2011 WL 843937, at *4, *11 (S.D. W. Va. Mar. 11, 2011) (holding, in view of *Wyeth*, that a presumption against preemption should be applied in determining the applicability of state laws of general application to national banks).

420. *See Wyeth*, 129 S. Ct. at 1200 (citing 12 U.S.C. § 360(k)(a)).

421. *Id.* at 1195, 1195 n.3.

422. *Id.* at 1195 n.3. *See also id.* at 1200 (indicating that Congress’s decision not to establish an express preemption regime for drug labeling supported the application of “the presumption against pre-emption”).

423. *Cuomo v. Clearing House Ass’n, L.L.C.*, 129 S. Ct. 2710, 2718 (2009) (citing *Wyeth*).

424. *See supra* notes 388–411 and accompanying text (discussing *Commonwealth, McClellan, St. Louis, Anderson*, and *Cuomo*).

425. *See supra* Part III.A–C (discussing the concurrent authority of CFPB and the states to adopt and enforce consumer financial protection laws). For discussions of “interactive federalism,” a concept used to describe the legal, political and social effects of overlapping federal and state regulatory roles in various fields

significant public benefits by promoting both cooperation and competition among federal and state officials. First, as shown in Part IV.A, Title X will encourage experimentation, innovation, and continuous reform as federal and state officials consult with each other and also compete with each other to provide optimal consumer financial protection. Second, as shown in Part IV.B, Title X will enable state legislatures and state AGs to assist CFPB in counteracting political influence exerted by the financial services industry.

A. Title X Will Promote Beneficial Cooperation, Competition, and Innovation by CFPB and State Officials

Title X’s regime of interactive federalism will encourage a “dynamic interaction” among federal and state officials as they exercise their concurrent authorities over the field of consumer financial protection.⁴²⁶ The interplay among federal and state authorities under Title X will benefit the public in at least four ways. First, federal and state officials will take different approaches in addressing the challenge of protecting consumers of financial services, and the resulting alternative strategies will produce fruitful experimentation and innovation.⁴²⁷ For example, the “dual banking system” consisting of federally-chartered and state-chartered banks has “permitted states to act as ‘laboratories’ in experimenting with new banking products, structures, and supervisory approaches, and Congress has subsequently incorporated many of the states’ successful innovations into federal legislation.”⁴²⁸ Similarly, concurrent enforcement of a wide range of federal regulatory statutes by federal and state officials has encouraged experimentation and innovation in enforcement approaches.⁴²⁹

Second, dual regulation promotes dialogue among federal and state officials, which in turn facilitates learning and regulatory improvement.⁴³⁰ For example, in the field of environmental protection, most federal statutes—like Title X of Dodd–Frank—establish minimum “floor” requirements and permit states to adopt supplemental safeguards.⁴³¹ Such statutes create “many venues in which policy choices are explored” and stimulate extensive “interaction among federal and state regulators, as well as other stakeholders,” thereby encouraging “more rigorous regulatory analysis” that will “challenge the status quo.”⁴³²

Third, overlapping federal and state authorities offer “alternative forms of relief”

of economic and social policy, see Robert Ahdieh, *Dialectical Regulation*, 38 CONN. L. REV. 863, 881–82 (2006); Robert A. Schapiro, *Toward a Theory of Interactive Federalism*, 91 IOWA L. REV. 243, 248–49, 252–54 (2005).

426. Schapiro, *supra* note 425, at 249.

427. Ahdieh, *supra* note 425, at 883, 891–92; Schapiro, *supra* note 425, at 288.

428. Wilmarth, *supra* note 93, at 259–65. See also Arthur E. Wilmarth, Jr., *The Expansion of State Bank Powers, the Federal Response, and the Case for Preserving the Dual Banking System*, 58 FORDHAM L. REV. 1133, 1157 (1990) (observing that “the dual banking system has enabled the states to act as ‘laborator[ies]’ for ‘experimentation’ in the manner envisioned by Justice Brandeis in . . . *New State Ice Co. v. Liebmann*.”); *New State Ice Co. v. Liebmann*, 285 U.S. 262, 311 (1932) (Brandeis, J., dissenting).

429. Margaret H. Lemos, *State Enforcement of Federal Law* 29–32, 26–27 (Cardozo Legal Stud. Working Paper No. 313, 2010), available at <http://ssrn.com/abstract=1685458>.

430. Schapiro, *supra* note 425, at 288; see also Ahdieh, *supra* note 425, at 889 (observing that “recurrently interacting [federal and state] agencies” may benefit through “adaptive learning from one another”).

431. Buzbee, *supra* note 16, at 1564–68.

432. *Id.* at 1588.

and thereby provide “an additional source of protection if one or the other government should fail to offer adequate protection.”⁴³³ Enforcement actions by state officials to combat securities abuses between 2002 and 2006 provide a vivid illustration of the “fail-safe function” that state officials can perform when federal regulators do not provide adequate protection to consumers and investors.⁴³⁴ As discussed above, New York Attorney General Eliot Spitzer, Massachusetts Secretary of State William Galvin, and other state regulators brought numerous enforcement proceedings against major securities firms after the SEC failed to act, and those state proceedings ultimately persuaded the SEC to take similar steps.⁴³⁵ Similarly, state enforcement initiatives in other fields (including antitrust, environmental protection, and regulation of tobacco and other dangerous products) have spurred beneficial changes in national policy.⁴³⁶ In contrast, as discussed above, the OCC’s and OTS’s preemptive regulations largely undermined states’ efforts to combat predatory lending during the housing bubble that led to the financial crisis.⁴³⁷

Fourth, overlapping federal and state lawmaking and enforcement roles can promote beneficial “regulatory competition.”⁴³⁸ Although it is possible for federal–state competition to produce “over-regulation,” the growing power of large financial conglomerates, the globalization of financial markets, and the magnitude of the recent financial crisis indicate that “under-regulation and regulatory gaps” pose greater threats to the welfare of consumers and investors.⁴³⁹ Regulatory regimes that create overlapping federal and state responsibilities are likely to reduce the risk of “under-regulation,” particularly when regulators at either level of government are vulnerable to “regulatory capture.”⁴⁴⁰ In this regard, Gillian Metzger has suggested that *Cuomo*, *Wyeth*, and other recent Supreme Court decisions reflect the Court’s “concern that federal agencies may be systematically failing to meet their statutory responsibilities” as well as the Court’s appreciation for “the role of state law and state enforcement in improving federal

433. Schapiro, *supra* note 425, at 289–90; *see also* Ahdieh, *supra* note 425, at 883.

434. Ahdieh, *supra* note 425, at 885–88; *see also* Jones, *supra* note 156, at 114–26. In addition to the supplemental protection provided by state enforcement actions, private litigants can use state tort laws and other state laws of general application to “ferret out error or misdeeds, and prompt change despite uninterested regulators, possibly ignorant public interest groups, and resistant industry.” Buzbee, *supra* note 16, at 1589; *see also supra* Part III.D.6 (discussing the applicability of general state laws to national banks).

435. Ahdieh, *supra* note 425, at 885–88, 891; Jones, *supra* note 156, at 14–26; *see also supra* notes 156–57 and accompanying text (discussing state enforcement actions to stop abusive practices by securities firms).

436. *See* Buzbee, *supra* note 16, at 1564–68, 1586–89; Lemos, *supra* note 429, at 21–32.

437. *See supra* Part II.E.2 (describing preemption of state anti-predatory lending laws by the OCC and OTS).

438. Ahdieh, *supra* note 425, at 889–90; *see also* Jones, *supra* note 156, at 121–24 (describing how “vertical competition” between state AGs and the SEC produced stronger investor protection).

439. Ahdieh, *supra* note 425, at 889–90; *see also* Schapiro, *supra* note 425, at 290–91 (acknowledging that regulatory “[o]verlap has its costs” resulting from a lack of “uniformity” between federal and state laws); *supra* Parts II.E.4, II.E.5 (contending that federal preemption played an important role in enabling large financial institutions to become more heavily engaged in risky nonprime lending, thereby aggravating the financial crisis and requiring costly federal bailouts of failing institutions); Wilmarth, *supra* note 19, at 1008–24, 1043–46 (same).

440. Ahdieh, *supra* note 425, at 887 n.136, 888; *see also* Jones, *supra* note 156, at 123–25 (contending that “[m]aintaining multiple levels of regulation provides an antidote to regulatory capture” and also “maximize[s] scarce government resources” by making it possible for federal and state officials to share “the costs of complex investigations”).

regulatory performance.”⁴⁴¹

B. Title X Reduces the Risk that CFPB Might Be Captured by the Financial Services Industry

Avoiding “capture” by regulated firms is a perennial challenge for most regulatory agencies.⁴⁴² Congress designed CFPB to be especially resistant to capture by the financial services industry, because members of Congress and analysts agreed that the industry had exercised excessive influence over bank regulators during the period leading up to the financial crisis.⁴⁴³ To strengthen CFPB’s defenses against political or regulatory capture (i) Congress gave CFPB substantial independence in making policies, issuing regulations and bringing enforcement proceedings, and (ii) Congress provided CFPB with an independent source of funding that does not depend on either congressional appropriations or industry-paid assessments.⁴⁴⁴

Nevertheless, CFPB continues to face daunting political challenges due to the determined and well-funded opposition of major financial institutions and their trade associations and political allies. During the debates over Dodd–Frank, big banks and their allies lobbied vigorously to keep consumer protection functions within the traditional banking agencies and to prevent the creation of any independent consumer financial protection agency.⁴⁴⁵ After Republicans took control of the House of Representatives in January 2011, they introduced bills to weaken CFPB by (i) removing CFPB’s independent funding and making its budget subject to annual congressional appropriations, (ii) replacing CFPB’s Director with a five-person commission, (iii) enhancing FSOC’s ability to veto CFPB’s regulations, and (iv) preventing CFPB from exercising its authorities until the Senate confirms the first CFPB Director.⁴⁴⁶ House

441. Gillian E. Metzger, *Federalism and Federal Agency Reform*, 111 COLUM. L. REV. 1, 25 (2011); *see also id.* at 37 (observing that recent Supreme Court decisions “could signal that the Court has adopted a new understanding of federal-state relations under which the states have a special role in monitoring and improving federal administration”).

442. Barkow, *supra* note 7, at 17–18, 21–24 (discussing problem of regulatory capture); Buzbee, *supra* note 16, at 1594–95, 1609–10 (same); Levitin, *supra* note 17, at 159–61 (same).

443. *See* S. REP. NO. 111-176, at 9–11, 15–21, 161–64 (2010) (discussing need for a strong and independent CFPB in view of past failures by federal banking agencies); Bar-Gill & Warren, *supra* note 27, at 90–95 (describing influence wielded by large financial institutions and other reasons why federal banking agencies failed to protect consumers from abusive financial practices); Levitin, *supra* note 17, at 152–61 (same); McCoy et al., *supra* note 36, at 1343–66 (same); Wilmarth, *supra* note 112, at 19–31 (same).

444. S. REP. NO. 111-176, at 11, 161–67, 172–73, 177 (2010); *see also* Barkow, *supra* note 7, at 74–75, 77 (describing how CFPB’s organization and funding are designed to protect CFPB against the risk of capture); *supra* Part III.A (discussing CFPB’s organization and funding).

445. Barkow, *supra* note 7, at 73; *see also* Joe Adler, *Birth of a New Kind of Regulator*, AM. BANKER, Dec. 2, 2010, at 12A (“While the [banking] industry had several problems with Dodd–Frank, and many opposed it outright, it was the consumer agency that generated the most heartache during debate.”); Paul Wiseman et al., *Big Job Looms for New Consumer Protection Agency*, USA TODAY, June 24, 2010, at 1B (“Financial industry lobbyists have fought the new agency through every step of the legislative process. And they aren’t likely to give up once it is up and running.”); Robert G. Kaiser, *The CFPB: How a crusade to protect consumers lost its steam*, WASH. POST, Jan. 31, 2010, at G01 (“Business groups—most vociferously the U.S. Chamber of Commerce and the American Bankers Association—have campaigned fiercely against what they describe as an unneeded, intrusive new agency that would increase the cost of doing business.”).

446. Mike Ferrulo, *Regulatory Reform: Neugebarger Bill Would Allow Congress to Control Purse Strings*

Republican leaders have acted in lockstep with major banks and their trade associations, which continue to express vehement opposition to the implementation of CFPB's mandate.⁴⁴⁷

In addition, commentators have noted that regulated industries ultimately succeeded in weakening and dominating the Consumer Product Safety Commission (CPSC), despite CPSC's original goal of protecting consumers against hazardous products.⁴⁴⁸ Although CPSC bears a surface resemblance to CFPB, an important distinction is that CPSC's product-safety rules completely preempt the states' ability to adopt additional requirements, and state AGs lacked authority to enforce CPSC's rules until 2008.⁴⁴⁹ In contrast, as discussed above, (i) the CFP Act and CFPB regulations establish only minimum requirements and allow the states to adopt supplemental consumer safeguards, and (ii) Title X of Dodd–Frank authorizes state AGs to enforce the CFP Act (except against national banks and federal thrifts) and to enforce CFPB regulations against *all* providers of consumer financial services.⁴⁵⁰ Thus, while state legislatures and state AGs have been largely powerless to assist CPSC, they are potentially influential partners who can help CFPB to mobilize public support and resist capture by industry forces.⁴⁵¹

State AGs have political motivations that make them more resistant to regulatory capture than federal agency officials. Most state AGs are elected rather than appointed, and they typically aspire to become governors or Senators.⁴⁵² The political ambitions of state AGs give them strong incentives to appeal to citizen electors by bringing public enforcement actions to protect consumers and investors.⁴⁵³ Thus, state AGs are less susceptible to industry influence than federal financial regulators because (i) state AGs aim to attract the votes of ordinary citizens in future elections, while financial regulators often hope to obtain future employment with large financial institutions or their service providers, and (ii) the offices of state AGs are funded by taxpayer revenues, while most federal financial regulatory agencies are funded directly or indirectly by industry-paid

of Consumer Agency, 96 BANKING REP. (BNA) 285 (Feb. 15, 2011); Phil Mattingly & Carter Dougherty, *U.S. Consumer Bureau Funding Would Drop 40 Percent Under Republican Plan*, BLOOMBERG.COM (Feb. 15, 2011), <http://www.bloomberg.com/news/2011-02-15/house-republicans-target-consumer-protection-bureau-funding-in-budget-bill.html>; Cheyenne Hopkins, *Political Sniping Dominates House Hearing on the CFPB*, AM. BANKER, Apr. 7, 2011, at 3; Jennifer Liberto, *Republicans Aim to Weaken Consumer Bureau*, CNNMONEY.COM (Apr. 6, 2011), http://money.cnn.com/2011/04/06/news/economy/republicans_consumer_bureau/index.htm. As explained above, Dodd–Frank authorizes FSOC to override a CFPB regulation if two-thirds of FSOC's voting members determine that the regulation would threaten the safety and soundness of the United States banking system or the financial stability of the United States. See *supra* note 211 and accompanying text (discussing FSOC's authority to veto CFPB's regulations). A bill proposed by Rep. Sean Duffy (R-Wis.) would allow a majority of FSOC's voting members to reject a CFPB rule if the rule threatened the safety and soundness of the United States banking system. Hopkins, *supra*.

447. Joe Nocera, *Talking Business: An Advocate Who Scares Republicans*, N.Y. TIMES, Mar. 19, 2011, at B1; *New Consumer Agency Under Fire From GOP, Banks*, ASSOC. PRESS FIN. WIRE, Mar. 16, 2011.

448. Barkow, *supra* note 7, at 65–72; Levitin, *supra* note 17, at 162.

449. Barkow, *supra* note 7, at 69–72.

450. *Id.* at 75–76; see *supra* Parts III.B, III.C (describing the states' supplemental lawmaking and law enforcement powers under Title X of Dodd–Frank).

451. Barkow, *supra* note 7, at 69–72, 75–76.

452. Levitin, *supra* note 17, at 199–203. As Adam Levitin observes, “the National Association of Attorneys General is often jocularly referred to as the National Association of Aspiring Governors.” *Id.* at 200 n.278.

453. *Id.* at 199–203; Barkow, *supra* note 7, at 56–57; Lemos, *supra* note 429, at 19–27, 33–34, 43.

assessments.⁴⁵⁴

Moreover, it is far more difficult for the financial services industry to capture 50 state AGs than it is to dominate a single federal agency.⁴⁵⁵ Even a few state officials can act as influential public “entrepreneurs” in exposing serious abuses that federal agencies have neglected.⁴⁵⁶ Eliot Spitzer and William Galvin showed the ability of state enforcers to capture the public’s attention and to influence national policy when they uncovered multiple securities scandals that the SEC had overlooked; indeed, their enforcement actions ultimately persuaded the SEC to take its own remedial steps.⁴⁵⁷

During the debates on Dodd–Frank, state AGs were among the strongest supporters of an independent federal consumer financial protection agency.⁴⁵⁸ After Dodd–Frank was enacted, Elizabeth Warren—who first proposed the agency’s creation and was appointed to oversee CFPB’s organization—declared that state AGs were CFPB’s “natural partners” and asked for their help.⁴⁵⁹ CFPB appointed former Ohio AG Richard Cordray as the first director of CFPB’s enforcement division,⁴⁶⁰ and CFPB subsequently entered into cooperative agreements with state banking commissioners and state AGs.⁴⁶¹ Thus, it appears that state officials—empowered by Title X of Dodd–Frank—will be CFPB’s staunchest regulatory and political allies as CFPB seeks to implement its mission of protecting consumers from unfair, deceptive and abusive financial products.

454. Lemos, *supra* note 429, at 19–27; Levitin, *supra* note 17, at 152–61, 199–203; *see also supra* Part II.D.2 (describing evidence that the financial services industry exerted significant influence over federal financial regulators during the credit boom leading up to the financial crisis). Margaret Lemos points out that state AGs have financial incentives as well as political motivations that encourage vigorous enforcement, because state AGs frequently use their recoveries of financial penalties to fund their own offices or to contribute to their states’ budgets (with associated political benefits). Lemos, *supra* note 429, at 25–27.

455. Barkow, *supra* note 7, at 56–58; Levitin, *supra* note 17, at 205.

456. Lemos, *supra* note 429, at 19 (describing state officials as “natural policy entrepreneurs who can significantly influence what sorts of conditions are publicly recognized as problems”) (quoting Roderick Hills, *Against Preemption: How Federalism Can Improve the National Legislative Process*, 82 N.Y.U. L. REV. 1, 15–16 (2007)); Levitin, *supra* note 17, at 199–200 (describing state AGs as “normative entrepreneurs who seek to promote certain policy norms as part of their political ambitions”).

457. Jones, *supra* note 156, at 14–26; Lemos, *supra* note 429, at 20–21; Levitin, *supra* note 17, at 201.

458. Mike Ferrulo, *Regulatory Reform: State Attorneys General Make Push for Consumer Financial Protection Agency*, 94 BANKING REP. (BNA) 309 (Feb. 16, 2010); Kaiser, *supra* note 445.

459. Carter Dougherty, *Warren Recruits Dodd–Frank Enforcers From 50 States*, BLOOMBERG.COM (Dec. 2, 2010), <http://www.businessweek.com/news/2010-12-02/warren-recruits-Dodd-Frank-enforcers-from-50-states.html> (“Enlisting state attorneys general is part of Warren’s strategy of making common cause with people who believe in the agency’s new mission and can support it for the long term.”); *see also* Adler, *supra* note 445 (describing Professor Warren’s role in conceiving and organizing CFPB); Julianna Goldman, *Warren Plays Volcker-Like Role for Obama in Finance Regulation*, BLOOMBERG.COM (Sept. 24, 2010), <http://www.businessweek.com/news/2010-09-24/warren-plays-volcker-like-role-for-obama-in-finance-regulation.html> (same).

460. Cheyenne Hopkins, *Ohio AG Among Three CFPB Hires*, AM. BANKER, Dec. 16, 2010, at 16.

461. Thecla Fabian, *State Bank Regulators Agree to Cooperate, Focus on Non-Bank Providers*, 96 BANKING REP. (BNA) 54 (Jan. 11, 2011) (reporting on agreement between CFPB and state banking commissioners to coordinate examination procedures and share examination findings with respect to non-bank providers of consumer financial services, including mortgage lenders, money transmitters, check cashers, payday lenders, and consumer finance companies); Cheyenne Hopkins, *Consumer Bureau, AGs Tout Cooperation*, AM. BANKER, Apr. 23, 2011, at 3 (reporting on joint statement of principles issued by CFPB and the 50 state AGs to develop joint training programs and coordinate enforcement activities).

V. CONCLUSION

Congress decided to establish CFPB after concluding that federal bank regulators had repeatedly failed to provide effective safeguards for consumers during the credit boom leading up to the financial crisis. Congress determined that federal banking agencies accommodated the desires of large financial institutions for immediate short-term profits, overlooked concerns about those institutions' long-term safety and soundness, and disregarded the dangers posed to consumers by predatory lending practices. In addition, Congress criticized the OCC and the OTS for preempting the efforts of many states to combat predatory practices.

In view of the federal regulators' systematic failures to protect consumers of financial services, Congress enacted Title X of Dodd–Frank. Title X removes consumer financial protection responsibilities from the federal banking agencies and centralizes those tasks within CFPB. Title X promotes CFPB's independence by granting CFPB autonomy in its policymaking, rulemaking and enforcement functions, and by giving CFPB an independent source of funding. In order to supplement the protections provided by CFPB's regulations, Title X authorizes the states to adopt laws providing additional safeguards for consumers of financial services. In order to increase the effectiveness of CFPB's enforcement efforts, Title X empowers state AGs to bring administrative and judicial proceedings to enforce Title X's statutory provisions and CFPB's regulations. Title X also imposes significant limitations on the OCC's ability to preempt the application of state laws to national banks and federal thrifts.

By encouraging both cooperation and competition among CFPB and state officials, Title X will promote experimentation, innovation, and continuous reform in consumer financial protection. Moreover, state legislatures and state AGs could play crucial roles in resisting efforts by major financial institutions and their political allies to weaken CFPB's independence and undermine its effectiveness. In view of the formidable political clout wielded by large financial conglomerates, Title X's grants of enhanced authority to state legislators and state AGs could prove to be vital safeguards for consumers of financial services.