1st Civil No. A110137

IN THE COURT OF APPEAL
FOR THE STATE OF CALIFORNIA
FIRST APPELLATE DISTRICT
DIVISION THREE

_____

PAUL MILLER, individually and on behalf of others similarly situated,

Plaintiff and Respondent,

v.

BANK OF AMERICA, NT & SA, a California corporation, and DOES 1-50,

Defendants and Appellants.

_____

ON APPEAL FROM THE SUPERIOR COURT OF THE COURT OF SAN FRANCISCO, JUDGE ANNE BOULIANE, CIV. CASE NO. 301917

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CENTER FOR RESPONSIBLE LENDING'S APPLICATION FOR LEAVE TO FILE AN *AMICUS CURIAE* BRIEF AND PROPOSED BRIEF IN SUPPORT OF PLAINTIFF AND RESPONDENT PAUL MILLER

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES

STATUTES

REGULATORY MATERIALS

OTHER AUTHORITIES

I. APPLICATION FOR LEAVE TO FILE AN *AMICUS CURIAE* BRIEF

To The Honorable William R. McGuiness, Presiding Justice of Division Three of the First Appellate District of the California Court of Appeal:

The Center for Responsible Lending ("CRL") requests leave to file an *amicus curiae* brief in this case in support of Paul Miller, *et al.*, regarding whether federal law and regulations preempt state law prohibiting a bank's seizure of Social Security and other government benefits to cover overdraft-related fees. CRL has done extensive research and policy work on issues related to preemption and overdraft loans. CRL has testified numerous times before Congress and regularly provides written and oral testimony to federal and state regulatory agencies. In 2005, CRL issued a research report entitled, *High Cost and Hidden From View: The $10.3 Billion Overdraft Loan Market*, which was one of the first attempts to quantify the amount of overdraft fees paid by consumers. CRL has also appeared before numerous other courts as an *amicus curiae*.

STATEMENT OF INTEREST OF *AMICUS CURIAE*

CRL is dedicated to protecting home ownership and enabling families to build wealth by working to eliminate abusive financial practices. A non-profit, non-partisan research and policy organization, CRL promotes responsible practices by financial institutions to assure access to fair terms of credit and opportunities to build assets for low-wealth families. CRL is an affiliate of the Center for Community Self-Help ("Self-Help"), which also includes a credit union and a loan fund. Self-Help has provided more than $4 billion in financing to help over 40,000 low-wealth borrowers in forty-seven

states buy homes, build businesses, and strengthen community resources. Self-Help also has experience as a provider of deposit accounts. Self-Help Credit Union has $210 million in assets and more than 12,800 accounts. CRL's affiliation with Self-Help provides CRL with important insight into the needs of financial institutions and their responsibilities to communities.

II. PROPOSED BRIEF OF *AMICUS CURIAE*

INTRODUCTION

At issue in this appeal is whether Bank of America can unilaterally seize its customers' directly-deposited government benefits to cover the sizeable fees it imposes for overdrafts. As the trial court recognized, California law under *Kruger v. Wells Fargo Bank*, 11 Cal. 3d 352 (1974), protects Social Security and other government benefits from such seizure because the benefits are intended exclusively for the support of qualified recipients. Bank of America and the United States on behalf of federal agencies including the Office of the Comptroller of the Currency ("OCC") contend that federal law preempts this aspect of California law and that the trial court's ruling undermines federal laws protective of consumer interests.

The Center for Responsible Lending ("CRL") submits this *amicus curiae* brief to address preemption and urge affirmance of the Superior Court's decision. In CRL's view, the government's position simply cannot be reconciled with the language of the OCC's own regulations or the National Bank Act, 12 U.S.C. § 21 *et seq.*, ("NBA") as interpreted by the Supreme Court. Bank of America has the burden to establish preemption, and a presumption against preemption applies because this case relates to the state's historic power to regulate debt collection in the banking arena. Even without such a presumption, the OCC's regulations would not preempt plaintiff's claims because: (1) the regulations expressly recognize that laws governing debt collection are generally not

preempted, (2) seizing funds after a deposit is distinct from all of the activities listed in the OCC's regulations as to which there is preemption, and (3) the OCC has not occupied the field for deposit-taking activities. Despite efforts by Bank of America and the OCC to conflate the OCC's authority with that of the OTS and to bootstrap from the Ninth Circuit's decision in *Lopez v. Washington Mutual Bank, FA*, 302 F.3d 900 (9th Cir.), *amended* 311 F.3d 928 (9th Cir. 2002), it is also clear that the OCC's authority under the NBA is much narrower than the OTS's authority under the Home Owners' Loan Act, 12 U.S.C. § 1461 *et seq.* ("HOLA"). CRL further believes that the policy concerns raised by Bank of America and its *amici* ring hollow in light of the recognized public interest in protecting Social Security benefits and the dangers of the overdraft product currently provided by banks.

BACKGROUND

The trial court found that Bank of America's overdraft fees or non-sufficient fund ("NSF") fees averaged $23.96 and could be as high as $32, with a daily maximum of $160. AA1261 ¶ 55; AA1265 ¶ 77.[1] As a result of high fees like these, customers pay triple- and even-quadruple digit interest rates for overdraft loans. For example, a $23.96 fee for an $80 overdraft loan translates into a 1,562% annual rate for a loan paid back in a week and a 781% annual rate if the loan is repaid in two weeks.

[1] Citations to the Appellant's Appendix are in the form "AA__." Citations to the Reporter's Transcript are in the form "RT__."

Evidence indicates that a disproportionate percentage of customers subject to overdraft or NSF fee collection are low- and moderate-income consumers and recipients of government benefits, who can least afford the triple- or quadruple-digit rates of overdraft loans.[2] Plaintiff's expert testified that Bank of America collected NSF fees from 1,299,167 accounts belonging to class members between August 13, 1994 and December 31, 2003 and assessed an average of 9 NSF fees per account. RT1421:16-1423:5. In total, Bank of America collected $284,385,741 in NSF fees from class members. *Id.* About 85% of all NSF fees collected by Bank of America are incurred by accounts with average monthly balances of less than $1,000. RT 2202:16-21 (Bowman). One disabled class member testified that he was repeatedly subject to NSF fees and that Bank of America once charged him five NSF charges, totaling $160, after he used his ATM card to purchase a total of $11 worth of items. RT1330:21-1331:10. These NSF fees left him with no money for food. RT1331:11-19.

After covering an overdraft, Bank of America's practice was to seize any money that was deposited into the customer's account—including government benefits—to collect the overdraft amount and any fees imposed. AA1259 ¶ 46. Bank of America would even seize money from another account held by the customer to pay overdraft amounts and overdraft-related fees. AA1261 ¶ 57. The trial court found that Bank of

[2] An executive vice president of one overdraft program vendor, Strunk & Associates, has been quoted as follows: "Areas of high unemployment, higher unemployment, you typically have more activity. . . . If you happen to be a bank that's on a military post, you're probably doing twice as much activity as any other bank." Alex Berenson, *Some Banks Encourage Overdrafts, Reaping Profits*, The New York Times, Jan. 22, 2003.

America had failed to establish the existence of a written agreement or contract with members of the class consenting to the use of Social Security funds to recover overdraft amounts and related fees in this fashion. AA1266 ¶ 82; AA1268 ¶ 88.

Plaintiff Paul Miller's experience with an overdraft caused by Bank of America's own error is illustrative of the effect that Bank of America's policy can have on its customers. Mr. Miller receives Social Security Insurance benefits due to a permanent mental disability and agreed to have his Social Security benefits directly deposited to his checking account after being told by Bank of America that his Social Security benefit payments would be safe and available when needed through direct deposit. AA1252-53 ¶¶ 14-15. In January 1998, Bank of America erroneously credited a deposit of $1,799.83 to Mr. Miller's account, which he assumed was a retroactive adjustment in his Social Security benefits. AA1253 ¶ 17. After noticing its error three months later, Bank of America removed the entire balance in Mr. Miller's account without providing him any prior notice. *Id.* at ¶ 18. Because the amount in Mr. Miller's account was not sufficient to cover the $1,799.83 that the bank claimed Mr. Miller owed, the bank then seized the Social Security benefits that were subsequently deposited into Mr. Miller's account. *Id.* at ¶ 19.

In desperate need of his benefits to ward off eviction, Mr. Miller contacted the bank, which advised him to set up a new account for direct deposit of his benefits. AA1253 ¶ 20; AA1254 ¶ 23. Based on Bank of America's representations, Mr. Miller

understood that his Social Security benefits would be protected in the new account. AA1254 ¶¶ 25. However, in keeping with its practice of reaching across accounts, Bank of America seized Mr. Miller's Social Security benefits from his new account, making those funds unavailable for his use to pay his necessary expenses. AA1254-55 ¶¶ 25-27; AA1261 ¶ 57. As a result of the overdraft caused by its own errors, Bank of America refused to honor a check that Mr. Miller wrote to pay his rent. AA1255 ¶ 28.

While some overdrafts like Mr. Miller's result from bank errors, others are deliberate extensions of credit by the bank. Overdraft loans may result when a bank pays out a check or honors an ATM or debit card transaction on an account that has insufficient funds. Overdraft loan programs today are a major source of fee income for banks.[3]

Although overdraft loans are extensions of credit, financial institutions that offer overdraft loan programs without a written agreement do not have to comply with Regulation Z's disclosure requirements regarding their triple- and quadruple-digit rates due to a technical exception in Regulation Z's definition of "finance charge." *See* Joint Guidance on Overdraft Protection Programs, 70 Fed. Reg. 9127, 9129-31 (Feb. 24, 2005) (citing 12 CFR § 226.4(c)(3)). Exploiting this exception, some banks automatically

[3] The vendors that market overdraft loan programs to financial institutions have publicly boasted about the dramatic increases in fee income that their programs generate. For example, Impact Financial Services, an overdraft program vendor, advertises, "Virtually all of our clients have increased the NSF fee income from 50-150% or more (with 100% or more being the norm), and those percentages are net of charge-offs, waives and refunds." *See* www.impactfinancial.com/about.html (accessed Jan.14, 2006).

enroll their checking account customers in overdraft loan programs without adequately disclosing the programs' exorbitant rates or telling the customers about less expensive options, such as linked checking and savings accounts and traditional lines of credit. *See generally* Jean Ann Fox & Patrick Woodall, Consumer Federation of America, *Overdrawn: Consumers Face Hidden Overdraft Charges From Nation's Largest Banks* (June 9, 2005), at http://www.consumerfed.org/pdfs/CFAOverdraftStudyJune2005.pdf.

ARGUMENT

A. Bank of America Bears the Burden to Establish Preemption, and a Presumption Against Preemption Should Apply.

A party claiming federal preemption of a state statute has the burden to demonstrate preemption. *See, e.g., Bronco Wine Co. v. Jolly*, 33 Cal. 4th 943, 956-57 (2004), *cert. denied*, 125 S. Ct. 1646 (2005); *Olszewski v. Scripps Health*, 30 Cal. 4th 798, 815 (2003). The California Supreme Court has recognized that "[c]onsideration of issues arising under the Supremacy Clause start[s] with the assumption that the historic police powers of the States [are] not to be superseded by . . . Federal Act unless that [is] the clear and manifest purpose of Congress" and that the "historic police powers of the States . . . extend . . . to banking, including national banking." *Peatros v. Bank of America NT & SA*, 22 Cal. 4th 147, 158-59 (2000) (citations omitted); *see also Smiley v. Citibank (South Dakota) N.A.*, 11 Cal. 4th 138, 148 (1995), *aff'd*, 517 U.S. 735 (1996); *Gibson v. World Sav. & Loan Ass'n*, 103 Cal. App. 4th 1291, 1300 (4th Dist. 2002).

Bank of America argues that the trial court erred in following this California Supreme Court authority and applying a presumption against preemption in this case. *See* Bank of Am. Br. at 36 n.13; *see also* U.S. Brief at 13 n.3 & 22 n.7. In support of its argument, Bank of America cites, *inter alia*, the Ninth Circuit's decision in *Wells Fargo Bank N.A. v. Boutris*, 419 F.3d 949, 956 (9th Cir. 2005). Underpinning the *Wells Fargo* decision is the Ninth Circuit's earlier decision in *Bank of America v. City & County of San Francisco*, 309 F.3d 551, 558-59 (9th Cir. 2002), which extended the Supreme Court's holding in *United States v. Locke*, 529 U.S. 89, 108 (2000), to the context of federal banking regulation. In *Locke*, the Supreme Court concluded that the presumption against preemption "is not triggered when the State regulates in areas where there has been a history of significant federal presence." 529 U.S. at 108.

The Ninth Circuit's extension of *Locke* into the banking arena is problematic and is not controlling. *See generally Cowan v. Myers*, 187 Cal. App. 3d 968, 985 (1986) ("[T]he decisions of the lower federal courts, even on federal questions, are not binding on this court."). *Locke* involved an area of the law—maritime commerce—where Congress has sought to establish "a uniformity of regulation." 529 U.S. at 108; *see* 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*, Annual Review of Banking and Financial Law 288-89 (2004). By contrast, the Supreme Court has recognized for over a hundred years that national banks "are governed in their

daily course of business far more by the laws of the State than of the nation" and that "their right to collect their debts . . . [is] based on State law." *Nat'l Bank v. Commonwealth*, 76 U.S. (9 Wall.) 353, 362 (1869), *quoted in Atherton v. FDIC*, 519 U.S. 213, 222-23 (1997).

Since *Locke* was decided, at least one California appellate court has suggested that the presumption against preemption applies in the banking context. *See Gibson*, 103 Cal. App. 4th at 1300. Just a month ago, the Ninth Circuit itself presumed that there was no preemption in analyzing a claim that an NBA provision granting national banks the power to dismiss bank officers "at pleasure" preempted application of an age discrimination statute to a national bank. *Kroske v. US Bank Corp.*, No. 04-35187, – F.3d –, 2005 WL 3502061, *4 (9th Cir. Dec. 23, 2005). Given these precedents and the California Supreme Court's explicit recognition that the presumption against preemption applies in the banking context, it was appropriate for the trial court to apply such a presumption in considering whether Bank of America had met its burden to establish preemption in this banking and debt collection case.

B. California Law As Set Forth in *Kruger* Is Not Preempted By the OCC Regulations or the National Bank Act.

The OCC operates under the NBA, and has promulgated a number of regulations, including *inter alia* 12 C.F.R. § 7.4007 governing deposit-taking and 12 C.F.R. § 7.4008 governing non-real estate lending. Bank of America and its *amici* contend that these provisions preempt California law to the extent that it prevents banks from seizing Social

Security benefits from their customers' account. In making this argument, both Bank of America and the United States rely heavily on the Ninth Circuit's decision in *Lopez v. Washington Mutual Bank, FA*, 302 F.3d 900 (9th Cir.), *amended* 311 F.3d 928 (9th Cir. 2002), which held that regulations promulgated by the Office of Thrift Supervision ("OTS") under HOLA preempted a claim under California Civil Procedure Code § 704.080. The United States asserts, for example, that "[t]he National Bank Act and regulations are legally indistinguishable from the statute and regulations at issue in *Lopez*, and, accordingly, compel the same conclusion here with respect to preemption." United States Br. at 3. In point of fact, the OCC's regulations and the NBA differ from the OTS regulations and HOLA in several critical ways and do *not* preempt the provision of California law at issue in this case.

1. The OCC's Regulations Do Not Preempt California Law Because Bank of America Is Collecting a Debt.

In asserting that the OCC's regulations preempt California law and are legally indistinguishable from the OTS's regulations, Bank of America and the OCC gloss over three key points: (1) the OCC's regulations expressly recognize that state laws governing the right to collect a debt are not inconsistent with the deposit-taking powers of national banks, while the OTS's regulations do not; (2) seizing protected funds from an account to collect a debt does not fall within any of the categories of activities as to which the OCC's regulations preempt state law ; and (3) unlike the OTS, the OCC has no regulation occupying the field (and, as explained in section B.2. below, does not have the authority

to promulgate one). Although agencies including the OCC have authority to interpret their own regulations, they are not entitled to deference when they posit an interpretation in an *amicus* brief that is inconsistent with the regulation's plain language, as the OCC has done here. *See Christensen v. Harris County*, 529 U.S. 576, 588 (2000) ("*Auer* deference is warranted only when the language of the regulation is ambiguous. The regulation in this case . . . is not ambiguous . . . . To defer to the agency's position would be to permit the agency, under the guise of interpreting a regulation, to create *de facto* a new regulation."); *Auer v. Robbins*, 519 U.S. 452, 461 (1997) (finding the Secretary of Labor's interpretation of his own regulation to be "controlling unless plainly erroneous or inconsistent with the regulation" (internal quotation marks omitted)).

a. <u>The OCC regulations expressly recognize that state laws governing debt collection are generally not preempted.</u>

The most obvious – and fatal – flaw in the argument of the Bank and its *amici* that *Lopez* mandates a reversal of the lower court's decision is that the OCC's regulations specifically identify state regulation of debt collection as an area that is generally *not* preempted. 12 C.F.R. § 7.4007(c), promulgated in 2004,[4] provides:

> State laws that are not preempted. State laws on the following subjects are not inconsistent with the deposit-taking powers of national banks and apply to national banks to the extent that they only incidentally affect the exercise of national banks' deposit-taking powers: . . . (4) Rights to collect debts . . . .

Other OCC regulations contain similar language regarding other bank powers. *See, e.g.*, 12 C.F.R. § 7.4008(e)(4) (non-real estate lending). This language has absolutely no

[4] *See* 69 Fed. Reg. 1904 (Jan. 13, 2004).

parallel in the OTS regulations that were in issue in *Lopez*. *See* 12 C.FR. §§ 557.11-.13 (deposit function). State laws governing debt collection are omitted from the OTS list of non-preempted state laws, while they are present in the OCC list of non-preempted state laws.

The treatment of debt collection in the OCC's regulation is a direct result of Supreme Court precedent. The OCC cast its 2004 regulation as a clarification of existing preemption law. 69 Fed. Reg. 1904, 1910 (Jan. 13, 2004). Given the over 140-year history of the NBA, the OCC did not have a clean slate upon which to write its view of what state laws could be viewed to "forbid, or to impair *significantly*" the exercise of a banking power. *Barnett Bank of Marion County, N.A. v. Nelson*, 517 U.S. 25, 33 (1996) (emphasis added).[5] In upholding Kentucky's right to require national banks to pay a state tax on their shareholders' shares of the banks' stocks, the Supreme Court said:

> [The national banks] *are 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 the State law incapacitates the banks from discharging their duties to the government that it becomes unconstitutional.

Nat'l Bank v. Commonwealth, 76 U.S. (9 Wall.) 353, 362 (1869) (emphasis added).[6] It is as a result of this explicit Supreme Court precedent interpreting the NBA that the OCC's

[5] *See* section B.2. *infra* for a discussion of the OCC's effort in its rules to remove from its preemption test the historic qualifications and limitations on preemption under the NBA.
[6] At the time the *Commonwealth* case was decided, the national banks' "duties to the government" included what was essentially a central banking function, a role turned over

2004 list of state laws that are not preempted includes "[r]ights to collect debts," as quoted above, as well as "[c]ontracts . . . ; and [a]cquisition and transfer of property." 12 C.F.R. §§ 7.4007(c) (deposit taking), 7.4008(e) (non-real estate lending); *see also* 12 C.F.R. § 34.4(b) (real estate lending).

The government tries to circumvent the plain language of the OCC's regulations by saying that the conduct involved is not collecting a debt. Without citing any authority or clearly articulating its rationale, the government posits in its *amicus* brief that because the obligations arise from deposit accounts rather than loan accounts, they are not debts. U.S. Brief at 22-23 & n.9, 28. Rather than building an argument of its own or explicating the government's position, Bank of America merely refers to the government's brief supporting the petition for a writ of supersedeas on this point. Bank of Am. Br. 36 n.13 (citing U.S. Writ Brief 19 n.4). Whatever the precise thinking may be behind these assertions, they do not survive scrutiny, as well-established authority makes it clear that

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to the Federal Reserve by Congress in 1913. Since 1913, national banks do not serve a governmental function, a point often overlooked when looking at the history of NBA preemption. *See generally Atherton v. FDIC*, 519 U.S. 213, 221-23 (1997); Wilmarth, *supra*, *23* Ann. Rev. Banking & Fin. L. at 240-45. *Compare Easton v. Iowa*, 188 U.S. 220, 229-30 (1903) (highlighting the role of national banks to "'aid the government in the administration of an important branch of the public service'" as distinct from the "mere business" of private banking) *with First Agric. Nat'l Bank of Berkshire County v. State Tax Comm'n*, 392 U.S. 339, 357 (1968) ("[T]here is little difference today between a national bank and its state-chartered competitor:…each exists for private profit.") (Marshall, J., dissenting).

Bank of America is collecting a "debt" arising from a deposit account when overdraft loans are made and NSF fees are taken.[7]

It is well established that when a bank pays an overdraft, it is extending a loan. *See, e.g., Hoffman v. Sec. Pac. Nat'l Bank*, 121 Cal. App. 3d 964, 969 (2d Dist. 1981) (noting that an overdraft is treated as an application for advance credit); *Popp v. Exchange Bank*, 189 Cal. 296, 300 (1922) (recognizing an overdraft as an indebtedness); 11 Am. Jur. 2d Banks and Financial Institutions § 937 (1997). The OCC has long since recognized this fact and recently reaffirmed it in the Joint Guidance on Overdraft Protection Programs, which states: "[w]hen overdrafts are paid, credit is extended." 70 Fed. Reg. 9127, 9129-30 (Feb. 24, 2005) (mandating that "overdraft balances" be reported as loans on the financial institutions' regulatory reports and noting that these programs are "intended essentially as short-term credit facilities"); *see also* OCC Interpretive Letter, 1984 WL 164096 (OCC May 22, 1984). Any time credit is extended, there is of course a debt, so overdraft amounts naturally constitute a debt. *Cf.* 15 U.S.C. §

[7] The OCC has tried in other contexts to stretch the deposit-taking authority afforded national banks beyond its limits. Following the Supreme Court decision in *Nationsbank of North Carolina, N.A. v. Variable Annuity Life Insurance Co.*, 513 U.S. 251 (1995), the OCC provided a bank a no-objection letter sanctioning the bank's sales of "retirement CDs." When the bank sought to enjoin administrative proceedings brought by the Florida Insurance Commissioner, the OCC filed an *amicus* brief supporting the bank and took the position that the retirement CD "was in fact a deposit, and that it represented the very essence of banking which is embodied in a bank's express authority to accept deposits." *Blackfeet Nat'l Bank v. Nelson*, 171 F.3d 1237, 1242 (11th Cir. 1999) (internal quotation marks omitted). The Eleventh Circuit rejected that reasoning and concluded that the OCC's interpretation was an "unreasonable expansion of the powers of national banks beyond those intended by Congress." *Id.*

1602(e) ("The term 'credit' means the right granted by a creditor to a debtor to defer payment of debt or to incur debt and defer its payment."); 12 C.F.R. § 226.2(a)(14) (defining "[c]redit" for purposes of Regulation Z as "the right to defer payment of debt or to incur debt and defer its payment"). As one treatise explains:

> An overdraft is considered to be in the nature of a loan. . . . Overdrafts do not leave a bank in the situation of having paid out money without a legally binding obligation for repayment. The Uniform Commercial Code (UCC) not only creates an obligation between the drawer of the overdraft and the payor bank, but also provides remedies for collection on the check itself, on the money itself, or on the obligation for which the check was drawn. *In other words, the bank may enforce the debt created by the overdraft in the same manner as any loan or promissory note may be enforced.*

Henry J. Bailey & Richard B. Hagedorn, Brady on Bank Checks 19.01 at 19-1 (Rev. Ed.) (emphasis added).[8]

Likewise, the NSF fees at issue in this case are "debts." As the trial court explained, "[w]hen Bank of America chooses to overdraw an account, it creates a debt in favor of the Bank, which the Bank, acting as a creditor, seeks to recover." AA1261 ¶ 54. In seizing overdraft amounts and NSF fees, the banks are collecting on these debts, an activity that California can regulate pursuant to the OCC's regulations. *See id.* at ¶ 55 ("NSF fees are collected in the same manner in which the Bank recovers the overdrafts; that is, the Bank collects the fees owed by seizing existing funds or any incoming deposits to the account."); *see also* Joint Guidance, 70 Fed. Reg. at 9130 n.9 (referring to "uncollected overdraft fees"). While the existence of credit presupposes the existence of

[8] The Uniform Commercial Code is not preempted under the NBA. *See* OCC Interpretive Letter No. 1005 (June 10, 2004).

debt, it is not necessary for a loan to be the source of the obligation creating a debt. "[T]he term debt, used in our statutes, should be given its modern legal significance, as including any sort of obligation to pay money." *Certified Grocers of California, Ltd. v. San Gabriel Valley Bank*, 150 Cal. App. 3d 281, 288 (2d Dist. 1983) (internal quotation marks omitted). A debt is "[a] fixed and certain obligation to pay money or some other valuable thing or things, either in the present or in the future." Black's Law Dictionary 403 (6th ed. 1990). The liability to pay NSF fees is clearly an "obligation" – a "debt" within the meaning of the law – just as the obligation to repay an overdraft loan constitutes a "debt."

Bank of America's characterization of its conduct as "account-balancing" instead of what it is plainly is – collecting "obligations," i.e. "debts" from its depositors' accounts – is simply an effort to use artful wordsmithing to avoid the import of the OCC's clear rule applying state law.

b. <u>Seizing funds from an account after deposit is distinct from all of the activities listed in the OCC's regulation as to which there is preemption.</u>

While denying *ipse dixit* that the activity at issue involves debt collection, the Bank of America and its *amici* try to recharacterize the specific activity as one that is subject to preemption. The activity involved is not the imposition of fees or charges on deposit accounts, but the seizure of Social Security benefits from bank accounts to collect overdraft-related debts. In an effort to make the case that it is an activity in the list of

preempted state laws (12 CFR § 7.4007(b)), rather than a non-preempted activity under 12 C.F.R § 7.4007 (c), Bank of America and the OCC point to banks' authority to receive deposits, to govern "funds availability," and to impose charges and fees connected to providing deposit account services. *See* Bank of America Brief at 33, 35, 38; U.S. Brief at 21-24. This authority, however, does not sustain the Bank of America and the OCC's claim of preemption.

The fact that a national bank has the authority to receive deposits and "exercise its deposit-taking power without regard to state law limitations concerning . . . [c]hecking accounts" under 12 C.F.R. § 7.4007(b)(2)(ii) is irrelevant because no one has challenged the bank's right to receive deposits. Rather, the issue here is a wholly separate one: whether the bank can unilaterally remove money from an account *after* a deposit has been taken. The provision of California law at issue here also does not affect "funds availability" within the meaning of 12 C.F.R. § 7.4007(b)(2)(iv) because it does not govern when funds in an account are available, but instead relates to whether the funds may be removed from the account to collect a debt.

Similarly, the fact that 12 C.F.R. § 7.4002 authorizes charges and fees connected to providing deposit account services does *not* mean that California law protecting Social Security benefits is preempted because plaintiff has not disputed the bank's right to charge fees and does not seek to limit or prohibit any charges or fees. Instead, plaintiff

has merely asserted that the banks cannot *collect* such charges or fees by seizing exempt Social Security benefits.

That the type of debt collection at issue here touches on authorized functions – deposit-taking and fee-charging – does not in and of itself create a significant impairment warranting preemption. The Supreme Court has had occasion to evaluate – and reject – a similar argument. In *McClellan v. Chipman Traders' National Bank*, 164 U.S. 347 (1896), a national bank argued that a state insolvency law on preferential transfers of real estate was preempted because national banks have authority to take real estate in connection with previous debts. Applying a conflict preemption test, the Supreme Court held that the state law did not prevent that activity; it merely imposed on national banks the "same conditions and restrictions to which all the other citizens of the state are subjected" and was not preempted. *Id.* at 358; *see also Anderson Nat'l Bank v. Luckett*, 321 U.S. 233, 248-49 (1944) ("[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.*") (emphasis added). Despite the efforts by Bank of America and its *amici* to recharacterize the Bank's activities, the activities simply are not ones as to which preemption applies.

c. <u>Unlike the OTS, the OCC has not occupied the field.</u>

The broad reading of the OCC's regulations advocated by the bank and the government and their insistence that *Lopez* controls cannot be reconciled with the fact

that the OCC has *not* occupied the field of deposit-taking for national banks. Unlike the OCC's regulations, the regulations at issue in *Lopez* plainly assert that the OTS has occupied the entire field of deposit-related regulations for federal savings associations. *Compare* 12 C.F.R. § 557.11(b) ("To further these purposes without undue regulatory duplication and burden, OTS hereby occupies the entire field of federal savings associations' deposit-related regulations. OTS intends to give federal savings associations maximum flexibility to exercise deposit-related powers according to a uniform federal scheme of regulation. Federal savings associations may exercise deposit-related powers as authorized under federal law, including this part, without regard to state laws purporting to regulate or otherwise affect deposit activities, except to the extent provided in Sec. 557.13. State law includes any statute, regulation, ruling, order, or judicial decision.") *with* 12 C.F.R. § 7.4007. Although Bank of America and the United States strive in their briefs to make the OTS and OCC regulations sound identical, the occupying-the-field language was added to the OTS regulations for a reason, as will be discussed in the next section, and its absence in the OCC regulations is fatal for their argument.

2. The National Bank Act Does Not Give the OCC the Authority to Preempt This Aspect of California Law.

Although the Court need not reach this issue because the plain language of the OCC's regulations does not preempt the aspect of California law at issue here, it is also important to note the OCC could not preempt a debt collection provision of this nature

under the NBA or occupy the field even if the OCC were to promulgate regulations that purported to do so. While the OCC would like to pretend that its authority is coextensive with the OTS's authority under HOLA, over a century of Supreme Court jurisprudence makes it clear that that is not the case.

The Supreme Court has described the preemptive scope of HOLA in much broader terms than it has used in describing the NBA, and in doing so, has ascribed sweeping powers to the federal regulatory agency overseeing thrifts. In the Court's words, Congress delegated to OTS's predecessor, the Federal Home Loan Bank Board ("FHLBB"), "broad authority to establish and regulate a uniform system," including specifying "best practices" according to its lights, not states' laws. *Fidelity Fed. Sav. & Loan Ass'n v. de la Cuesta*, 458 U.S. 141, 161, 166 (1982) (internal quotation marks omitted) (citing 12 U.S.C. § 1464(a)(1)). "Congress invested the Board with broad authority to regulate federal savings and loans so as to effect the statute's purposes, and plainly indicated that the Board need not feel bound by existing state law." 458 U.S. at 162.[9] Following the *de la Cuesta* decision, the FHLBB issued a rule functionally preempting the field, 12 C.F.R. § 545.2, 48 Fed. Reg. 23032, 23058 (May 23, 1983). In

[9] Despite the sweeping language, the *de la Cuesta* court nevertheless applied a conflict analysis to the FHLBB rule at bar, and thus did not decide whether the FHLBB's regulations occupied the field. 458 U.S. at 159 n.14. For a thorough discussion of preemption under HOLA, see generally National Consumer Law Center, *The Cost of Credit: Regulation, Preemption, and Industry Abuses* § 3.5.3 (3rd ed. 2005). For a discussion of express preemption, complete preemption, and conflict preemption, see *Kroske v. US Bank Corp.*, No. 04-35187, – F.3d –, 2005 WL 3502061, *3 (9th Cir. Dec. 23, 2005).

promulgating its current preemption regulations occupying the field, the OTS[10] has invoked its recognized authority under HOLA to determine "best practices" and look for uniform law.[11]

In its brief, the government seeks to superimpose this description of HOLA authority onto the NBA. *See, e.g.*, U.S. Brief at 23 n.10 (intent is that national banks operate under uniform rules subject to uniform regulation by OCC). It cites *Waite v. Dowley*, 94 U.S. 527, 533 (1876), for the proposition that "[w]here there exists a concurrent right of legislation in the States and in Congress, and the latter has exercised its power, there remains in the States no authority to legislate on the same matter." U.S. Brief at 17. But the *Waite* court goes on to say, "It is none the less true, however, that the line which divides what is occupied exclusively by any legislation of Congress from what is left open to the action of the States is not always well defined, and is often distinguished by such nice shades of difference on each side as to require the closest scrutiny when the principle is invoked, as it is in this case." 94 U.S. at 533. That close scrutiny highlights the differences that distinguish *Lopez.*

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[10] Following major problems with the savings and loan industry, Congress abolished the FHLBB and reorganized the law governing the thrift industry. Pub. L. No. 101-73 §§ 401-02 (1989). The FHLBB was replaced by the Office of Thrift Supervision, and the previous FHLBB regulations were transferred and recodified. *See* 54 Fed. Reg. 34637 (Aug. 21, 1989); 54 Fed. Reg. 49411 (Nov. 30, 1989).

[11] *See, e.g.*, 61 Fed. Reg. 50951, 50965-67 (Sep. 30, 1996) (promulgating OTS lending rule, codified at 12 C.F.R § 560.2); 62 Fed. Reg. 54759, 54761 n.12 (Oct. 22, 1997) (citing preemption discussion from earlier lending rule in promulgating OTS deposit rules, codified at 12 C.F.R. §§ 557.10 – 557.13).

In contrast to the language used in *de la Cuesta* concerning thrifts, the Supreme Court has emphasized for over a hundred years that national banks have two masters: state and federal law. *Nat'l Bank v. Commonwealth*, 76 U.S. (9 Wall.) 353, 362 (1869); *see also Atherton v. FDIC*, 519 U.S. 213, 222-23 (1997) (noting that the Court has recognized since the nineteenth century that federal chartered banks are subject to state law and that "[t]o point to a federal charter by itself shows no conflict, threat or need for 'federal common law'").[12] In *Anderson National Bank v. Luckett*, 321 U.S. 233 (1944),

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[12] *Talbott v. Bd. of Comm'rs*, 139 U.S. 438 (1891), cited in *Kroske v. US Bank Corp.*, No. 04-35187, – F.3d –, 2005 WL 3502061, *10 (9th Cir. Dec. 23, 2005) , is not to the contrary. Although *Kroske* cites *Talbott* for the proposition that Congress intended to "create a national banking system with 'uniform and universal operation throughout the entire territorial limits of the country,'" 2005 WL 3502061, at *10 (quoting *Talbott*, 139 U.S. at 443), the quote was dicta taken out of context. At issue in *Talbott* was whether national banks were subject to the law of a territory of the United States to the same extent as they were subject to the law of a state. The Court's answer to that question was yes, territories can apply their non-preempted laws to national banks to the same extent that states can. 139 U.S. at 446. The Court's example referred to the national banking system's obligation to "furnish a currency of uniform value," a function the national banks ceased to have in 1913, as explained in note 6 *supra*. In the context of the issue before it, the Court said:

> Differences arising from mere adaptation to local statutes is one thing, while discrimination by reason of locality or political organization is another, and essentially diverse. It does not conflict with the national character of the system that the banks of the various states and territories may charge and receive a rate of interest allowed by the local statutes; that is merely the adaptation of the system to the laws and customs of the various states; but it would militate much against its national character if banks organized under it were subjected to local taxation in one part of the Union, and exempted from it elsewhere.

Id. at 443.

Contrary to the implication in *Kroske* that the NBA demonstrates a Congressional purpose of "uniform regulation," *Talbott*'s reference to interest rates as a local adaptation that does not conflict with the national character of the system demonstrates that national uniformity as to bank functions, enumerated or incidental, is not integral to the NBA.

for example, a bank made an argument similar to the one Bank of America makes here: since the NBA authorizes national banks to take deposits, a Kentucky law relating to abandoned accounts constituted an "unconstitutional interference" and should be preempted. 321 U.S. at 239-40. The Supreme Court rejected that argument. As the Court explained, "[t]he deposits are debtor obligations of the bank, incurred and to be performed in the state where the bank is located, and hence are subject to the state's dominion." *Id*. at 241; *see also id.* at 248-49. "This Court has often pointed out that national banks are subject to state laws, unless those laws infringe the national banking laws or impose an undue burden on the performance of the banks' functions." *Id.* at 248. Under the Court's jurisprudence, not just any intrusion on a national bank power will suffice to give rise to preemption under the NBA; rather, the intrusion must "forbid, or . . . impair *significantly*" the exercise of an explicitly granted power. *Barnett Bank of Marion County, N.A. v. Nelson*, 517 U.S. 25, 33 (1996) (emphasis added).

While the courts have recognized that national banks have both enumerated and "incidental" powers, *see Nationsbank of North Carolina, N.A. v. Variable Annuity Life Ins. Co.*, 513 U.S. 251 (1995) (addressing banks' powers outside the context of preemption), it does not automatically follow that any state law governing that which is "incidental" to a bank power is automatically preempted, any more than is the case even

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Though the NBA preempted direct state regulation of interest rates, as it does now, the NBA by its own terms also referred banks back to state law. Under federal law, national banks may "borrow" whichever rate the state allows to its "most-favored-lender." 12 U.S.C. § 85; 12 C.F.R. § 7.4008(d)(2)(x) n.6. (While there is an alternative federal rate allowed, it is often irrelevant because historically the state rates have been higher.)

with expressly enumerated powers, such as deposit-taking, *see, e.g., Anderson Nat'l Bank v. Luckett*, 321 U.S. 233 (1944). While lending is an enumerated authority, state laws that directly affect lending have been held to apply to national banks. *See, e.g., McClellan v. Chipman Traders' Nat'l Bank*, 164 U.S. 346 (1896) (addressing preferential transfers on real estate lending).

In holding that a Pennsylvania law prohibiting redlining was not preempted, the Third Circuit recognized that, "[w]hatever may be the history of federal-state relations in other fields, regulation of banking has been one of dual control since the passage of the first National Bank Act in 1863." *Nat'l State Bank, Elizabeth, N.J. v. Long*, 630 F.2d 981, 985 (3rd Cir. 1980), *cited in Kroske v. US Bank Corp.*, No. 04-35187, – F.3d –, 2005 WL 3502061, *4 (9th Cir. Dec. 23, 2005). The *Long* court recognized that redlining is not a legitimate banking purpose that would be frustrated by state law, and its concern about encouraging circumvention of such laws is equally applicable to the instant facts. Here, Congress has not articulated a public purpose of making the exempt benefits sustaining elderly, disabled, and low-income citizens available to their creditors.

There can be no preemption in this case because prohibiting banks from seizing directly-deposited Social Security benefits does not "forbid, or . . . impair significantly" the exercise of any granted power. *Barnett Bank*, 517 U.S. at 33. The Supreme Court's very clear statements regarding national banks' rights to collect their debts reinforce this

conclusion. *See* section B.1.a. *supra* (citing *Nat'l Bank v. Commonwealth*, 76 U.S. (9 Wall.) 353, 362 (1869) and *Atherton v. FDIC*, 519 U.S. 213, 222-23 (1997)).

Because the Supreme Court's jurisprudence and the OCC's regulations exclude debt collection activities such as those challenged by plaintiff from NBA preemption, the validity of the 2004 OCC preemption rules is not at issue in this case. However, it is worth noting that the general preemption standards the OCC adopted in its rules are based largely on the OTS rules,[13] which derive from a different statute with a much broader sweep. The NBA leaves national banks subject to state law to a greater extent than HOLA does for thrifts. *See, e.g.*, *People v. Coast Fed. Sav. & Loan Ass'n*, 98 F. Supp. 311, 319 (S.D. Cal. 1951). A simple comparison of Supreme Court articulations of the respective tests demonstrates that the preemption tests under HOLA and the NBA differ, casting doubt on the propriety of the OCC borrowing so heavily from the OTS in its rulemaking. For the instant case, however, it suffices to say that state regulation of Bank of America's activities is not preempted under either the OCC's rules or the Supreme Court's interpretation of the NBA.

[13] The OCC adopted the OTS's general test that anything more than an "incidental" effect on an authorized power is preempted. 12 C.F.R. § 7.4007(b), (c). Though the OCC's rules purport to "clarify" existing preemption law under the NBA, the OCC turned to the OTS's analysis under HOLA for both the broad test and the rationale. For example, rather than recognizing that the NBA precedent on laws not preempted results from the application of a narrower preemption test than the test that applies under HOLA, the OCC characterizes its list of laws that are not preempted as ones which "form the legal infrastructure that makes it practicable to exercise a permissible Federal power." 69 Fed. Reg. at 1912, 1913. That is the construct used by the OTS in deriving its list of non-preempted state laws under HOLA. *See* 61 Fed. Reg. 50951, 50966 (Sep. 30, 1996). One would search the NBA preemption cases in vein for use of that analysis.

C. Reversing the Trial Court's Decision Would Hurt Recipients of Government Benefits.

The government's brief raises the implausible specter of a collapse of the system of electronic delivery of government benefits should the trial court's decision stand. U.S. Brief at 38-46. Arguments based on a parade of horribles have been made before in support of preemption, but "there can be no constitutional argument" without a "persuasive showing" of the posited negative consequences. *Anderson v. Luckett,* 321 U.S. 233, 242 (1944). It is highly ironic for the government to argue that national banks must be allowed to invade Social Security recipients' accounts to pay the banks' high fees and correct the banks' mistakes (as happened with Mr. Miller), in order "to protect beneficiaries from the hardships of existence." U.S. Brief at 11.[14]

The trial court's ruling appropriately prevents Bank of America from helping itself to its customers' Social Security and other government benefits to repay debts incurred through its own errors and high fee structures. Although Bank of America and its *amici* suggest that "overdraft protection" is a "valuable service" for consumers, *see, e.g.*, Bank of America Brief at 25-26; U.S. Brief at 41, overdraft loans in fact are high-cost short-term loans often made to the people who can least afford them, *see* Jacqueline Duby et

[14] Indeed, the government's zeal in supporting Bank of America in this case may well generate the same indignant response given by a commentator to an OCC *amicus* brief filed to support a financial institution's effort to halt a predatory lending investigation by the California Department of Corporations: "Instead of expressing concern over the indicia of predatory lending, the OCC filed an amicus brief supporting the subsidiary and actually petitioned to make an oral argument on behalf of the [national bank subsidiary] at taxpayers' expense." Christopher L. Peterson, *Federalism and Predatory Lending: Unmasking the Deregulatory Agenda*, 78 Temple L. Rev. 1, 77-78 (2005).

al., Center for Responsible Lending, *High Cost & Hidden From View: The $10 Billion Overdraft Loan Market* (May 26, 2005). Far from a courtesy service, overdraft programs today generate substantial fee income for banks and other financial institutions. *See generally* Jean Ann Fox & Patrick Woodall, Consumer Federation of America, *Overdrawn: Consumers Face Hidden Overdraft Charges From Nation's Largest Banks* (June 9, 2005), available at http://www.consumerfed.org/pdfs/CFAOverdraftStudyJune2005.pdf. *Cf. Perdue v. Crocker Nat'l Bank*, 38 Cal. 3d 913 (1985) (reversing dismissal of a claim challenging NSF fees as unconscionable). If the banks' concern is that they will not be able to collect overdraft-related fees if they are unable to help themselves to their customers' Social Security benefits, a far more rational and legally defensible solution is for banks to collect debts, especially those that they encourage, in compliance with procedures that apply to other debt collectors and to work out repayment arrangements when necessary to correct their own mistakes.

CONCLUSION

For the foregoing reasons, the judgment of the Superior Court should be affirmed.

Respectfully submitted,

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