

Review Course on Interest Exportation

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Dodd-Frank's Interest Exportation Savings Clause

No provision of [the NBA] shall be construed as altering or otherwise affecting the authority conferred by [12 U.S.C. § 85] for the charging of interest by a national bank at the rate allowed by the laws of the State, territory, or district where the bank is located, including with respect to the meaning of 'interest' under such provision.

12 U.S.C. §25b(f)

National Bank Interest Exportation Provision ("Section 85")

Any association may take, receive, reserve, and charge on any loan . . . interest at the rate allowed by [1] the laws of the State, Territory, or District where the bank is located, or [2] at a rate of 1 per centum in excess of the discount rate on ninety-day commercial paper in effect at the Federal reserve bank in the Federal reserve district where the bank is located, whichever may be the greater, and no more.

12 U.S.C. §85.

Federal Savings Association Provision

Notwithstanding any State law, a savings association may charge interest on any extension of credit at a rate of not more than [1] 1 percent in excess of the discount rate on 90-day commercial paper in effect at the Federal Reserve bank in the Federal Reserve district in which such savings association is located or [2] at the rate allowed by the laws of the State in which such savings association is located, whichever is greater.

12 U.S.C. § 1463(g).

Federally-Insured State Banks

In order to prevent discrimination against State-chartered insured depository institutions, . . . if the applicable rate prescribed in this subsection exceeds the rate such State bank or insured branch of a foreign bank would be permitted to charge in the absence of this subsection, such State bank or such insured branch of a foreign bank may, notwithstanding any State constitution or statute which is hereby preempted for the purposes of this section, take, receive, reserve, and charge on any loan or discount made, or upon any note, bill of exchange, or other evidence of debt, interest [1] at a rate of not more than 1 per centum in excess of the discount rate on ninety-day commercial paper in effect at the Federal Reserve bank in the Federal Reserve district where such State bank or such insured branch of a foreign bank is located or [2] at the rate allowed by the laws of the State, territory, or district where the bank is located, whichever may be greater.

12 U.S.C. §1831d(a).

Origins of Interest Exportation

- In 1864, little interstate lending.
- About 100 years after the National Bank Act was passed, national banks began issuing credit cards to individuals in other states. Looking at the plain language of Section 85, they concluded that they were entitled to charge interest at the rate allowed by the laws of the states where they were located, even if the borrowers were “located” in different states.
- At first, some lower courts concluded that, plain language aside, this was so not was Congress had meant, and that national banks couldn’t rely on Section 85 when making loans in other states.
- In *Marquette Nat’l Bank of Minneapolis v. First of Omaha Serv. Corp.*, 439 U.S. 299 (1978), the Supreme Court held, in effect, that Section 85 says what it says.

Terminology and Analogies

- “Exportation” can be a useful analogy. But don’t take it too literally.
- You can also think about this as a choice of law provision. But even that isn’t entirely accurate.

Method of Preemption

- Does not just wipe away state standards.
- Replaces state standards with a federal standard.

Deference to the OCC

- Definition of “Interest” receives express Congressional blessing.
- Most favored lender?
- Material to the determination of the permitted interest?

Deference to the OCC

- Does the OCC make a “preemption determination” when it interprets Section 85?
- Supreme Court decision in *Smiley* suggests not:

[P]etitioner contends that no Comptroller interpretation of §85 is entitled to deference, because §85 is a provision that pre-empts state law. She argues that the "presumption against . . . pre-emption" . . . in effect trumps *Chevron*, and requires a court to make its own interpretation of §85 that will avoid (to the extent possible) pre-emption of state law. This argument confuses the question of the substantive (as opposed to pre-emptive) *meaning* of a statute with the question of *whether* a statute is pre-emptive. We may assume (without deciding) that the latter question must always be decided *de novo* by the courts. That is not the question at issue here; there is no doubt that §85 pre-empts state law.

Smiley v. Citibank (South Dakota), 517 U.S. 735, 744 (1996) (emphasis in original).

Impact on Op Subs

- Which trumps, the interest exportation savings clause or the provision eliminating preemption for op subs?

Roadmap

- What is “interest”?
- Where is bank located and which restrictions do you follow?
- What else do you need to follow?
- Common issues

What is “interest”?

What is Interest?

- OCC regulations define “interest” for purposes of Section 85 as follows:

Any payment compensating a creditor or prospective creditor for an extension of credit, making available of a line of credit, or any default or breach by a borrower of a condition upon which credit was extended.

What is Interest? (continued)

- The regulation and/or interpretations identify the following as examples of fees falling into the definition of “interest”:
 - Numerical periodic rates;
 - Late fees;
 - NSF fees;
 - Overlimit fees;
 - Annual fees;
 - Cash advance fees;
 - Membership fees;
 - Prepayment fees;
 - Account opening fees;
 - Fees for exercising fixed rate option;
 - Account closure fees.

What is Interest? (continued)

- “Interest” does not “ordinarily” include the following fees:
 - Appraisal fees;
 - Premiums and commissions attributable to credit insurance;
 - Finders' fees;
 - Fees for document preparation or notarization; and
 - Fees incurred to obtain credit reports.

What is Interest? (continued)

The Ultimate Test

- Fees that compensate creditor for extension of credit from fees vs. services performed.

Where is a Bank Located?

- Federal Thrifts:
 1. Headquarters state
 2. State where branch office is located if loan is “booked” in that state.
 - A loan is “booked” at the office where it is underwritten, approved, processed and disbursed.

Where is a Bank Located? (continued)

- National Banks:
 - State where headquarters or branch office provided non-ministerial functions performed in state.
 - Non-ministerial functions are (1) decision to extend credit, (2) the extension of credit, and (3) the disbursement of loan proceeds.

What is a Bank Located? (continued)

- State Chartered Banks:
Same test as for national banks.

Limitations Under Most Favored Lender Provisions (Interplay with State Law)

- Cannot adopt rate of competing federal lender.
- Override for federal thrifts and state chartered banks.
- State law limitation applicable to the class of loans that are material to the determination of the permitted interest rate.
- Must follow restrictions on “fees” that are considered “interest” under (1) federal most favored lender law, or (2) state law bank’s relying to charge a particular interest rate.
- State homestead laws.

Interplay with Other Laws/ Requirements

- Elimination of agent preemption.
- Preemption of fee restrictions under the federal laws.
- CARD Act.
- 501(a) of Depository Institutions Deregulation and Monetary Control Act of 1980.
- Alternative Mortgage Transaction Parity Act.

Which restrictions do you follow?

Most Favored Lender Principle

- Follow the rules applicable to the “most favored lender” under state law.
 - All-or-nothing rule.
- But also subject to limits on the types of loans that lender may make.
 - Dollar limits
 - Loan types
- Can rely on most favored lender even when making loans in your own state.

Analytical Process

Step 1: Determine which fees you charge are “interest” under federal law.

Step 2: Identify the lenders under state law that could make the loan at issue.

Step 3: Identify the restrictions on the fees you identified under Step 1 for each type of lender you identified under Step 2.

Step 4: Decide which set of restrictions you like best.

*Consider state parity statutes.

Alternative: Just find a lender with broad lending powers and generally favorable restrictions, and just follow the restrictions on the fees you identified in Step 1 applicable to that type of lender. (Hint: State-chartered banks usually are the most favored, or close to it.)

What else do you need to follow?

Material to the Determination of the Permitted Interest

- Restrictions that define the class of loans for which the permitted interest rate is allowed.
- Restriction establish the manner in which the permitted interest rate is determined.
 - A bank may use the “multiplier figure” (i.e., the permitted interest rate expressed as a percentage) prescribed by state law only if the bank complies with state laws governing “the proper arithmetical use of that figure.” *First National Bank in Mena v. Nowlin*, 509 F.2d 872, 877 (8th Cir. 1975).

Questions?