Case No. 21-15667

IN THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

WILLIAM KIVETT; BERNARD BRAVO; LISA BRAVO,
Plaintiffs-Appellees,

v.

FLAGSTAR BANK, FSB,
Defendant-Appellant.

On Appeal from the United States District Court for the Northern District of California (San Francisco), Case No. 3:18-cv-05131-WHA • The Honorable William Haskell Alsup, Senior District Judge

BRIEF OF *AMICI CURIAE* CONFERENCE OF STATE BANK SUPERVISORS AND AMERICAN ASSOCIATION OF RESIDENTIAL MORTGAGE REGULATORS IN SUPPORT OF APPELLEES AND AFFIRMANCE

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Corporate Disclosure Statement

Pursuant to Federal Rule of Appellate Procedure 26.1, *amici* Conference of State Bank Supervisors and American Association of Residential Mortgage Regulators state that they are nonprofit corporations without any parent corporations and no publicly held corporation owns 10% or more of their stock.

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Interest of *Amici Curiae*

Amici Conference of State Bank Supervisors (CSBS) and American Association of Residential Mortgage Regulators (AARMR) are national associations of state officials responsible for regulating state-chartered banks and state-licensed nonbank financial institutions (including mortgage lenders and servicers) in all 50 States, American Samoa, the District of Columbia, Guam, Puerto Rico, and the U.S. Virgin Islands.[1]

Since 1902, CSBS has played a leading role in defending our nation's dual system for regulating banks and other financial service providers. CSBS represents its members at the federal level and promotes collaboration among its members and federal regulatory agencies. Similarly, AARMR fosters effective state supervision and regulation of the residential mortgage industry by its members, thereby serving the needs of local communities and protecting the rights of consumers.

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[1] No counsel for a party or person other than *amici curiae*, their members, and their counsel authored any part of this brief or made any monetary contribution intended to fund the preparation or submission of the brief. This brief was funded solely by the *amici curiae* filing this brief. All parties have consented to the submission of this *amicus* brief.

CSBS owns and administers the Nationwide Multistate Licensing System (NMLS) for nonbank originators of residential mortgages. In 2008, Congress passed the Secure and Fair Enforcement for Mortgage Licensing Act, 12 U.S.C. §§ 5101-17, authorizing CSBS and AARMR to establish NMLS to "enhance consumer protection, and reduce fraud . . . [in] the residential mortgage industry." *Id.* § 5101.

CSBS and AARMR have a compelling interest in this case. On rehearing, this Court will decide whether to adhere to its previous decisions holding that Cal. Civ. Code § 2954.8(a) applies to national banks.[2] Section 2954.8(a) protects consumers by requiring national banks and other mortgage lenders to pay reasonable interest on customer balances in mortgage escrow accounts. A decision to preempt § 2954.8(a) would give national banks an unwarranted competitive advantage over state-chartered and state-licensed mortgage lenders and servicers and seriously impair the States' authority to regulate financial institutions and protect consumers.

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[2] *Kivett v. Flagstar Bank, FSB*, No. 21-15667 (9th Cir., May 17, 2022), 2022 WL 1553266 (*Kivett*), *vacated and remanded*, 144 S. Ct. 2628 (2024); *Lusnak v. Bank of Am., N.A.*, 883 F.3d 1185 (9th Cir.) (*Lusnak*), *cert. denied*, 139 S. Ct. 567 (2018).

Argument

I. This Court Should Reaffirm Its Decisions in *Kivett* and *Lusnak* and Reject Flagstar Bank's Preemption Claim.

A. Based on the Methodology Prescribed by the Supreme Court in *Cantero*, This Court Should Determine That Cal. Civ. Code § 2954.8(a) Does Not Prevent or Significantly Interfere with National Bank Powers.

In *Cantero v. Bank of Am., N.A.*, 602 U.S. 205, 213-14 (2024), the Supreme Court held that the "controlling legal standard" for deciding preemption cases under the National Bank Act (NBA) is the "prevents or significantly interferes" standard adopted in *Barnett Bank of Marion County, N.A. v. Nelson*, 517 U.S. 25 (1996), and codified in 12 U.S.C. § 25b(b)(1)(B), a provision of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank). The Supreme Court vacated and remanded the Second Circuit's decision in *Cantero* because that decision did not conform to the preemption standard established by *Barnett Bank* and Dodd-Frank.[3]

The Second Circuit held in *Cantero* that the NBA preempted N.Y. Gen. Oblig. L. (NYGOL) § 5-601, a New York interest-on-escrow statute

[3] 602 U.S. at 209, 213-14, 221, *vacating and remanding Cantero v. Bank of Am., N.A.*, 49 F.4th 121 (2d Cir. 2022).

that closely resembles Cal. Civ. Code § 2954.8(a). As the Supreme Court observed, the Second Circuit concluded that "federal law preempts any state law that 'purports to exercise control over a federally granted banking power,' regardless of 'the magnitude of its effects.'" *Cantero*, 602 U.S. at 213 (quoting 49 F.4th at 131).

The Supreme Court held that the Second Circuit erred by adopting an overbroad "categorical test" for preemption, which would "preempt virtually all state laws that regulate national banks, at least other than generally applicable state laws such as contract or property laws." *Id.* at 220-21. By refusing to consider the "magnitude" of a challenged state law's "effects" on national bank powers, the Second Circuit "did not analyze preemption in a manner consistent with Dodd-Frank and *Barnett Bank*." *Id.* at 213, 221.

To avoid the Second Circuit's error, the Supreme Court held that "[a] court applying that *Barnett Bank* standard must make a practical assessment of the nature and degree of the interference caused by a state law . . . with the national bank's exercise of its powers." *Id.* at 219-20. In making that assessment, the court should conduct a "nuanced comparative analysis" of the challenged state law consistent

with the Supreme Court's evaluations of state laws that were found to be preempted, or not preempted, in *Barnett Bank* and six other Supreme Court precedents identified in *Cantero*. *Id.* Those six decisions include (1) three cases holding that state laws were preempted – *Franklin Nat'l Bank v. New York*, 347 U.S. 373 (1954) (*Franklin*), *First Nat'l Bank of San Jose v. California*, 262 U.S. 366 (1923) (*San Jose*), and *Fidelity Fed. Sav. & Loan Ass'n v. de la Cuesta*, 458 U.S. 141 (1982) (*Fidelity*); and (2) three decisions holding that state laws were not preempted – *Anderson Nat'l Bank v. Luckett*, 321 U.S. 233 (1944) (*Anderson*), *McClellan v. Chipman*, 164 U.S. 347 (1896) (*McClellan*), and *Nat'l Bank v. Commonwealth*, 76 U.S. 353 (1869) (*Commonwealth*).

As shown in Part I.C, "the nature and degree of the interference" caused by Cal. Civ. Code § 2954.8(a) with the exercise of national bank powers is far less substantial than the magnitude of interference caused by each of the state laws evaluated in *Barnett Bank* and the other six key Supreme Court decisions identified in *Cantero*. Accordingly, a "nuanced comparative analysis" of § 2954.8(a) confirms that this Court should adhere to its decisions in *Kivett* and *Lusnak* and reject the preemption claim of Flagstar Bank (Flagstar).

B. Cal. Civ. Code § 2954.8(a) Is a Valid State Consumer Protection Law and Does Not Significantly Interfere with National Bank Powers.

1. Section 2954.8(a) Protects Consumers by Requiring Mortgage Lenders to Pay Reasonable Interest on Borrowers' Balances in Escrow Accounts.

Plaintiffs' mortgages required them to make monthly deposits into escrow accounts, which Flagstar used to pay Plaintiffs' property taxes and insurance premiums.[4] Plaintiffs' escrow accounts were mandatory savings accounts that imposed "forced budgeting" on them.[5] Plaintiffs' escrow accounts provided significant benefits to Flagstar by "protecting the loan collateral (the home) against tax foreclosure or uninsured damage." *Cantero*, 602 U.S. at 211. Plaintiffs' escrow accounts

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[4] Brief of Appellant, *Kivett v. Flagstar Bank*, No. 21-15667, 2021 WL 4507608 (9th Cir., Sept. 24, 2021) (Flagstar Brief), at *15-*16.

[5] *See Understanding escrow accounts*, EECU MORTGAGE SERVICES, https://eecu.org/personal-banking/mortgage-home-equity/resource-center/general-mortgage/understanding-escrow-accounts (last visited Jan. 21, 2025) ("Think of an escrow account as a savings account for your property taxes and insurance.") (information provided by federally-insured credit union); Erica Giovanetti, *What is Escrow?*, U.S. NEWS (Dec. 13, 2024), https://money.usnews.com/loans/mortgages/articles/what-is-escrow (A mortgage escrow account imposes "forced budgeting" on borrowers to ensure timely payment of real estate taxes and insurance premiums).

provided further substantial benefits to Flagstar by (1) enabling Flagstar to generate "float earnings" by investing the funds deposited by Plaintiffs, and (2) allowing Flagstar to earn substantial fees for servicing Plaintiffs' mortgages.[6]

In 1976, the California legislature adopted Cal. Civ. Code § 2954.8(a), which requires every "financial institution" providing mortgage loans secured by one-to-four family homes in California to pay at least 2% annual interest on borrowers' balances in escrow accounts. The California legislature adopted § 2954.8(a) after determining that "it was only fair for the homeowners who fund these escrow accounts to

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[6] *Hymes v. Bank of Am., N.A.*, 408 F. Supp. 3d 171, 176 (E.D.N.Y. 2019) ("During the period between when monthly deposits are required and taxes and insurance premiums come due, money belonging to the borrower simply accumulates in escrow. The lender may use this money to generate interest and income for itself, but the borrower has no access to it.") (*Hymes*), *rev'd sub nom. Cantero v. Bank of Am., N.A.*, 49 F.4th 121 (2d Cir. 2022), *vacated and remanded*, 602 U.S. 205 (2024); HW Media, *How retaining servicing provides a competitive advantage*, HOUSINGWIRE (Feb. 14, 2023), https://www.housingwire.com/articles/how-retaining-servicing-provides-a-competitive-advantage/ (Mortgage servicers receive a "standard service fee" equal to 0.25% of the principal balances of the mortgages they service); *Why Lenders Are Purchasing More MSRs in 2022*, PRIVOCORP (2022) , https://privocorp.com/blog/why-lenders-are-purchasing-more-msrs-in-2022/ (Mortgage servicers receive "servicing fees" and "ancillary fees" and also generate "float earnings" by investing borrowers' funds in escrow accounts).

share in their benefits."[7] As the bill's chief sponsor explained, "It is simply unacceptable to allow lenders the use of approximately $350,000,000 per year [of borrowers' funds held in escrow accounts] interest free."[8]

Section 2954.8(a) protects consumers by requiring mortgage lenders to pay reasonable interest on borrowers' balances in escrow accounts. That requirement is amply justified because borrowers make mandatory deposits to fund those accounts, and mortgage lenders receive significant benefits from those accounts.[9]

This Court has repeatedly held that consumer protection "is a field traditionally regulated by the states, [and] compelling evidence of an intention to preempt [by Congress] is required." *Lusnak*, 883 F.3d at 1191 (quoting *Aguayo v. U.S. Bank*, 653 F.3d 912, 917 (9th Cir. 2011),

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[7] Brief of the State of California as Amicus Curiae in Support of Appellees in *McShannock v. JP Morgan Chase Bank, N.A.*, No. 19-15899 (9th Cir., Oct. 14, 2019), 2019 WL 5328653, at *4 (describing § 2954.8(a)'s purpose).

[8] *Id.* at *5 (quoting Louis J. Papan).

[9] *Id.* at *3-*4 ("Banks benefit greatly from [mortgage] escrow accounts [because] escrow accounts have the potential to earn banks a profit while simultaneously guarding against the loss of their underlying mortgage investments.").

cert. denied, 568 U.S. 814 (2012) (quoting *Gen. Motors Corp. v. Abrams*, 897 F.2d 34, 41-42 (2d Cir. 1990)), *cert. denied*, 568 U.S. 814 (2012). Congress has expressed a strong intention in favor of applying state consumer protection laws to national banks. Under Dodd-Frank, a "state consumer financial law" that does not discriminate against national banks is preempted "only if" a court or the Office of the Comptroller of the Currency (OCC) determines that the state law "prevents or significantly interferes with the exercise by the national bank of its powers." 12 U.S.C. § 25b(b)(1)(B). State interest-on-escrow laws are "state consumer financial laws" covered by § 25b(b)(1)(B). 12 U.S.C. § 25b(a)(2); *Cantero*, 602 U.S. at 213.

Dodd-Frank expressed specific support for applying state interest-on-escrow laws to national banks by amending 15 U.S.C. § 1639d(g)(3). *Lusnak*, 883 F.3d at 1194-96. As amended, § 1639d(g)(3) requires national banks and other mortgage lenders to pay interest on escrow account balances pursuant to "applicable" state laws for the types of mortgages specified in 15 U.S.C. § 1639d(b). Plaintiffs' mortgages are not governed by § 1639d(g)(3), but that statute reflects Congress's view that national banks "can comply with state escrow interest laws

without any significant interference with their banking powers." *Lusnak*, 883 F.3d at 1196. Indeed, leading national banks have complied for years with § 2954.8(a) and other state interest-on-escrow statutes without experiencing any substantial problems with their mortgage escrow operations.[10]

2. Section 2954.8(a) Does Not Significantly Interfere with National Bank Powers.

New York's interest-on-escrow statute, NYGOL § 5-601, closely resembles Cal. Civ. Code § 2954.8(a) by requiring mortgage lenders to pay at least 2% annual interest on borrowers' balances in escrow accounts for mortgages secured by one-to-six family homes in New York. New York enacted § 5-601 in 1974 to redress an unfair advantage that mortgage lenders exploited by "giving themselves an interest-free loan for however long the mortgage escrow account remained in place." *Hymes*, 408 F. Supp. 3d at 176-77.

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[10] *Lusnak*, 883 F.3d at 1190 (noting Wells Fargo's compliance with § 2954.8(a)); Answering Brief of Plaintiffs-Appellees, *Kivett v. Flagstar Bank*, No. 21-15667 (9th Cir., Nov. 22, 2021), 2021 WL 5702573 (Kivett Brief), at *14-*15, *19 (describing compliance by Wells Fargo, JPMorgan Chase, and Citibank with § 2954.8(a) and other state interest-on-escrow laws).

In 1975, two three-judge federal district courts upheld the validity of NYGOL § 5-601 against constitutional challenges by a state savings bank and the Federal National Mortgage Association (FNMA).[11] In *JSB*, the district court held that § 5-601 represented a valid exercise of New York's "police power" to "safeguard the vital interests of its people." 390 F. Supp. at 1361-62. The court rejected the savings bank's challenge to § 5-601 under the Contract Clause and the Fourteenth Amendment's Due Process and Equal Protection Clauses. The New York legislature "concluded that mortgage lenders could 'well afford to pay' at least two percent interest-on-escrow accounts," and the savings bank "offer[ed] no evidence to rebut this finding." *Id.* at 1363. The savings bank also failed to show that it would suffer a net loss on its mortgage escrow accounts after paying the interest required by § 5-601. *Id.*[12] The Supreme Court summarily affirmed the district court's decision. *JSB*, 423 U.S. 802 (1975).

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[11] *Jamaica Sav. Bank v. Lefkowitz*, 390 F. Supp. 1357 (E.D.N.Y.) (three-judge court) (*JSB*), *aff'd without opinion*, 423 U.S. 802 (1975); *Federal Nat'l Mortg. Ass'n. v. Lefkowitz*, 390 F. Supp. 1364 (S.D.N.Y. 1975) (*FNMA*) (three-judge court).

[12] *See* Arthur E. Wilmarth, Jr., *On Remand in* Cantero*, the Second Circuit Should Reject Bank of America's Preemption Claim and Hold*

In *FNMA*, the district court adopted *JSB*'s reasoning in dismissing FNMA's constitutional challenges to § 5-601 under the Contract Clause and Equal Protection Clause. *FNMA*, 390 F. Supp. At 1367. The court also rejected FNMA's preemption claim under the Supremacy Clause. *Id.* at 1367-69. The court determined that the "closest analogy" to FNMA's Supremacy Clause claim was the national bank preemption claim rejected by the Supreme Court in *Anderson*. *Id.* at 1368. The court found that, "[a]s in *Anderson*, the state law at issue here does not discriminate against FNMA as a federal mortgage lending institution" or conflict with any federal statute. *FNMA*, 390 F. Supp. at 1369.

The court determined that § 5-601 did not violate the Supremacy Clause because its impact on FNMA was "insignificant." *Id.* The court pointed out that (i) § 5-601 "does not regulate how FNMA must keep or invest the escrow funds in its possession" and does not "interfere directly with [FNMA's] internal management," (ii) FNMA held mortgage escrow funds for the "ultimate benefit" of borrowers, and

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that New York's Interest-on-Escrow Law Applies to National Banks, 20 RUTGERS BUS. L. REV. 76, 81-83, 104-07 (2024) (Wilmarth, *Cantero*) (discussing *JSB*), available at https://ssrn.com/abstract=5080405.

those funds were intended "not to provide FNMA with income but rather to protect [FNMA's collateral] interest in the mortgaged property," and (iii) § 5-601 "in no way impairs this [collateral protection] purpose."[13]

The district court in *FNMA* concluded that, "although the burden [on FNMA] may be somewhat greater than that found in *Anderson*, [§ 5-601] is not so burdensome as to violate the Supremacy Clause." *FNMA*, 390 F. Supp. at 1369. In fact, as discussed below in Part I.C, the relatively minor impact of Cal. Civ. Code § 2954.8(a) and NYGOL § 5-601 on national banks is less substantial than the burden imposed on national banks by the Kentucky statute in *Anderson*. Sections 2954.8(a) and 5-601 only require mortgage lenders to "share with [borrowers] the profits which are realized from the investment of monies held" in escrow accounts. *JSB*, 390 F. Supp. at 1363. In contrast to the Kentucky law upheld in *Anderson*, §§ 2954.8(a) and 5-601 (i) do not deprive mortgage lenders of their custody of borrowers' funds held in escrow accounts and (ii) enable lenders to retain all profits

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[13] *Id.*; *see* Wilmarth, *Cantero*, *supra* note 12, at 84-85 (discussing *FNMA*).

from investing those funds in excess of the required 2% interest payment.

In *Hymes*, 408 F. Supp. 3d at 195, the district court similarly determined that NYGOL § 5-601's "degree of interference [with national bank powers] is minimal." The court emphasized that § 5-601 "does not bar the creation of mortgage escrow accounts, or subject them to state visitorial control, or otherwise limit the terms of their use." *Id.* While national banks must pay "modest interest" on borrowers' escrow balances, § 5-601 allows national banks to administer escrow accounts in a manner that is "relatively unimpaired and unhampered by the state law." *Id.* at 185-86, 195-96.

As shown by the analysis of NYGOL § 5-601 in *JSB*, *FNMA*, and *Hymes*, the parallel provisions of Cal. Civ. Code § 2954.8(a) do not significantly interfere with national bank powers. Flagstar has argued to the contrary, based on declarations submitted by two of its employees.[14] However, Plaintiffs showed that the claims of "significant interference" made by Flagstar's employees were based on "mere

[14] Flagstar Brief, *supra* note 4, at *27-*31.

speculation" and "conjecture, not fact."[15] Additionally, Flagstar has complied with § 2954.8(a) and other state interest-on-escrow laws for 80% of the loans in its mortgage servicing portfolio, which Flagstar "subservices" for third parties. Flagstar "offered no evidence that its *existent* compliance with Section 2954.8 interferes in any way with its banking operations."[16]

Flagstar has chosen not to comply with state interest-on-escrow laws only for mortgage loans that Flagstar services for its own account, representing just 20% of Flagstar's servicing portfolio. Flagstar has not shown that complying with § 2954.8(a) for one-fifth of its servicing portfolio would significantly impair any aspect of its mortgage business.[17]

Plaintiffs have documented that compliance by bank and nonbank mortgage lenders and servicers with § 2954.8(a) was "pervasive prior to *Lusnak*" and became "the all-but universal norm after the *Lusnak* decision."[18] The "pervasive compliance" with § 2954.8(a) – including by

[15] Kivett Brief, *supra* note 10, at *3-*14, *26.

[16] *Id.* at *7-*8, *14.

[17] *Id.* at *8, *26.

[18] *Id.* at *14-*15.

leading national banks such as Wells Fargo, JPMorgan Chase, and Citibank – completely undermines Flagstar's claim that § 2954.8(a) significantly interferes with national bank powers.[19]

C. A "Nuanced Comparative Analysis" of § 2954.8(a) with the State Laws Reviewed in Seven Key Supreme Court Decisions Identified in *Cantero* Confirms that § 2954.8(a) Does Not Significantly Interfere With National Bank Powers.

As shown above, Cal. Civ. Code § 2954.8(a) has an insignificant impact on national bank powers. Moreover, as required by *Cantero*, 602 U.S. at 219-21, a "nuanced comparative analysis" of § 2954.8(a) with the state laws evaluated in seven key Supreme Court decisions demonstrates that § 2954.8(a) does not significantly impair national bank powers.

The state laws preempted in *Barnett Bank*, *Franklin*, *San Jose*, and *Fidelity* imposed very severe burdens on federally-chartered banks. Florida's law in *Barnett Bank* was preempted because it prohibited

[19] *Id.* at *15, *18-*19.

most national banks from exercising their power to sell insurance from small town offices as explicitly authorized in 12 U.S.C. § 92.[20]

New York's statute in *Franklin* was preempted because it barred national banks from using the words "saving" or "savings" in advertising for savings deposits. The New York trial court determined that New York's statute imposed a "crippling obstruction" on a "necessary part" of the "banking business" of a national bank by "*restrict[ing]* it 'tremendously' . . . in obtaining 'savings deposits.'"[21] The Supreme Court agreed that national banks "depend upon their success in attracting private deposits," and that New York's statute created "a clear conflict" with federal statutes authorizing national banks to accept savings deposits. *Franklin*, 347 U.S. at 375-78.

The Supreme Court observed in *Franklin* that the federally-granted power to accept deposits was part of a broader federal scheme ensuring that national banks would be "at no disadvantage in

[20] *Barnett Bank*, 517 U.S. at 28-29, 31-35; *see* Wilmarth, *Cantero*, *supra* note 12, at 88-90 (discussing *Barnett Bank*).

[21] *People v. Franklin Nat'l Bank*, 200 Misc. 557, 568-71, 105 N.Y.S.2d 81, 92-95 (1951), *rev'd*, 281 App. Div. 757, 118 N.Y.S.2d 210, *aff'd*, 305 N.Y. 453, 113 N.E.2d 796 (1953), *rev'd*, 347 U.S. 373 (1954); *see* Wilmarth, *Cantero*, *supra* note 12, at 90-92 (discussing *Franklin*).

competition with state-created institutions." *Id.* at 375. New York's statute undermined that federal scheme by permitting only state-chartered savings institutions to use the terms "saving" or "savings" in advertising for savings deposits. *Id.* at 374, 374-75 n.1. The Supreme Court held that national banks "must be deemed to have the right to advertise [their savings deposits] by using the commonly understood description which Congress has specifically selected." *Id.* at 378.

In *San Jose*, 262 U.S. at 369-70, the challenged California escheat law was preempted because it "directly impair[ed]" and "interfere[d]" with the "plainly granted powers" of national banks to solicit and accept deposits. California's law required deposits to be escheated to the state upon "mere proof of dormancy" for over twenty years "without any determination of abandonment in fact."[22] California's law created an impermissible "conflict" with the NBA by attempting "to qualify in an unusual way agreements between national banks and their customers." *San Jose*, 262 U.S. at 369-70. The Supreme Court determined that California's law "alter[ed] the contracts of deposit in a manner

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[22] *Anderson*, 321 U.S. at 250-51 (discussing *San Jose*).

considered so unusual and so harsh in its application to depositors as to deter them from placing or keeping their funds in national banks."[23]

In *Fidelity*, 458 U.S. at 154-59, 159 n. 14, a California judicial rule created "an actual conflict" with a valid regulation issued by the Federal Home Loan Bank Board (FHLBB). The FHLBB's regulation gave federal savings associations "unrestricted" authority to enforce due-on-sale clauses in their mortgages. *Id.* at 146-47, 169 n.22. In contrast, California's judicial rule prohibited enforcement of due-on-sale clauses except in "cases where the lender's security is impaired," thereby "limiting the availability of an option the [FHLBB] considers essential to the economic soundness of the thrift industry." *Id.* at 155-56. The Supreme Court held that California's rule was preempted because it undermined the FHLBB's ability "to ensure the financial stability" of federal savings associations.[24]

The impact of § 2954.8(a) on national banks is plainly insignificant compared to the very severe burdens imposed by the

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[23] *Id.* at 250 (discussing *San Jose*); *see* Wilmarth, *Cantero*, *supra* note 12, at 92-93 (same).

[24] *Fidelity*, 458 U.S. at 154-56, 168-70 (quote on 170); *see* Wilmarth, *Cantero*, *supra* note 12, at 93-96 (discussing *Fidelity*).

preempted state laws in *Barnett Bank*, *Franklin*, *San Jose*, and *Fidelity*. The modest interest payment required by § 2954.8(a) is also less substantial than the state-law obligations that were upheld against preemption claims in *Anderson*, *McClellan*, and *Commonwealth*.

In *Anderson*, 321 U.S. at 238-40, a national bank argued that a Kentucky statute inflicted significant harm by requiring national banks to transfer custody of "presumptively abandoned" deposits to state authorities. Kentucky's law divested national banks of their control over long-dormant deposits, thereby terminating their ability to earn profits by investing those deposits in loans or government securities.[25]

In *McClellan*, 164 U.S. at 348-49, a national bank challenged a Massachusetts law that prohibited national banks from accepting preferential transfers of real property from insolvent debtors either to satisfy or secure antecedent debts. The national bank claimed that the Massachusetts law undermined the "stability" of national banks by interfering with their ability to "tak[e] security" through transfers of

[25] Brief in Behalf of Anderson Nat'l Bank in *Anderson Nat'l Bank v. Reeves*, 1944 WL 42454, at *18 (U.S., Jan. 18, 1944).

real property "whenever necessary for the protection of their property and assets."[26]

In *Commonwealth*, 76 U.S. at 358-63, a national bank challenged a Kentucky law requiring national banks to pay the state's tax on bank shares on behalf of their shareholders. The national bank argued that the Kentucky law compelled the bank to act as a "State servant" in fulfilling the "burdensome duty" of collecting Kentucky's bank shares tax from its shareholders "[w]ithout remuneration."[27]

The Supreme Court rejected the preemption claims in *Anderson*, *McClellan*, and *Commonwealth* after determining that the challenged state laws did not discriminate against national banks or create any conflicts with federal banking laws. The Court also concluded that the challenged state laws advanced legitimate state objectives – protecting long-dormant deposits in *Anderson*, preventing insolvent debtors from making preferential transfers to favored creditors in *McClellan*, and

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[26] *McClellan*, 164 U.S. at 352-53 (describing the national bank's argument).

[27] *Commonwealth*, 76 U.S. at 358 (summarizing the national bank's argument).

collecting a valid state tax owed by bank shareholders in *Commonwealth*.[28]

Similarly, Cal. Civ. Code § 2954.8(a) does not discriminate against national banks, does not conflict with any federal banking statute, and protects consumers by requiring payment of reasonable interest on funds deposited by borrowers in mortgage escrow accounts. Section 2954.8(a) does not impose any other restriction on the ability of national banks to administer mortgage escrow accounts.

Thus, a "nuanced comparative analysis" of § 2954.8(a) with the state laws evaluated in seven key Supreme Court decisions identified in *Cantero* demonstrates that the "the nature and degree of the interference caused by" § 2954.8(a) with national bank powers is less substantial than any of those seven state laws. *Cantero*, 602 U.S. at 219-21. Accordingly, this Court should reject Flagstar's claim that § 2954.8(a) significantly interferes with national bank powers.

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[28] *See* Wilmarth, *Cantero*, *supra* note 12, at 97-103 (discussing the Supreme Court's rejection of preemption claims in *Anderson*, *McClellan*, and *Commonwealth*).

D. The District Court Order in *Raoul* Does Not Support Flagstar's Preemption Claim.

A federal district court recently granted a preliminary injunction barring enforcement of the Illinois Interchange Fee Prohibition Act (IIFPA) against national banks. *Illinois Bankers Ass'n v. Raoul*, No. 24 C 7307 (N.D. Ill. Dec. 20, 2024), 2024 WL 5186840. The court concluded that plaintiffs showed a "likelihood of success" on their NBA preemption claim because IIFPA "significantly interferes" with national bank powers. The court determined that IIFPA prohibits national banks from (1) charging interchange fees on credit card payments of state taxes, local taxes, and gratuities, and (2) using data from credit card transactions for "many purposes," including "to monitor credit card fraud, address payment disputes, and facilitate cardholder loyalty programs." *Id.* at *8-*12. The court also stated that "the level of 'interference' that gives rise to preemption under the NBA is not very high." *Id.* at *11 (quoting *Monroe Retail Inc. v. RBS Citizens, N.A.*, 589 F.3d 274, 283 (6th Cir. 2009).

Raoul does not support Flagstar's preemption claim. Compared to IIFPA, Cal. Civ. Code 2954.8(a) has a much less substantial impact on national bank operations. Section 2954.8(a) requires only the payment

of reasonable interest on borrowers' balances in escrow accounts and does not affect any other aspect of mortgage lending or servicing. In contrast, the court in *Raoul* determined that "[t]he alleged cost of compliance [with the IIFPA's prohibitions] would likely be more crippling for some Illinois financial institutions than the State claims." *Id.* at *16.

In addition, the district court's statement in *Raoul* that a "not very high" level of interference is sufficient to establish preemption is contrary to the commonly-accepted meaning of "significant." Dictionaries define "significant" as "IMPORTANT" and "of a noticeably or measurably large amount."[29] Similarly, the Supreme Court and this Court have treated "significant" and "important" as equivalent terms in construing the National Environmental Policy Act (NEPA).[30]

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[29] MERRIAM-WEBSTER DICTIONARY, https://www.merriam-webster.com/dictionary/significant (all caps in original); *accord* DICTIONARY.COM (defining "significant" as "important and deserving of attention; of consequence" and "relatively large in amount or quantity"), https://www.dictionary.com/browse/significant.

[30] *Robertson v. Methow Valley Citizens Council*, 490 U.S. 332, 349 (1989) (By requiring federal agencies to "carefully consider detailed information concerning *significant* environmental impacts, . . . NEPA ensures that *important* effects will not be overlooked or underestimated") (emphasis added); *Calif. Wilderness Coalition v. U.S. Dept. of Energy*, 631 F.3d 1072, 1098 n.25 (9th Cir. 2011) (quoting a

The order in *Raoul* is preliminary. Important issues must still be determined, including the question of whether IIFPA – which focuses on the relationship between banks and merchants – is a "state consumer financial law" under 12 U.S.C. §25b(a)(2).

E. A Decision Preempting § 2954.8(a) Would Greatly Weaken the States' Authority to Charter and Regulate Financial Institutions and Protect Consumers.

A decision to preempt § 2954.8(a) would severely undermine the States' authority to charter, license, and regulate providers of financial services and protect consumers. Such a decision would distort the mortgage servicing market by giving national banks an unjustified competitive advantage in over a dozen states with interest-on-escrow laws.[31] Additionally, as discussed in Part II, a decision preempting § 2954.8(a) would encourage the OCC to redouble its unlawful efforts to preempt state consumer financial laws.

1984 decision holding that NEPA applies to federal power contracts that "*significantly* affect the environment because they involve *important* policy choices affecting energy conservation") (emphasis added; citation omitted).

[31] *See* Chris Clow, *U.S. Supreme Court to hear mortgage escrow case in February*, HOUSINGWIRE (Jan. 12, 2024), https://www.housingwire.com/articles/us-supreme-court-to-hear-mortgage-escrow-case-in-february/ ("At least thirteen states" have interest-on-escrow laws).

Mortgage servicing is performed by state banks, national banks, and state-licensed nonbank mortgage lenders and servicers.[32] Among the nation's top 50 mortgage servicers on June 30, 2024, state-licensed nonbanks held a significantly larger share of the mortgage servicing market than national banks did, as the following table shows:

Market Share of the 50 Largest Mortgage Servicers

	Servicing Market Share	**Number of Institutions**
National Banks	**34.7%**	**13**
State Licensed Nonbanks	**57.1%**	**26**
State Banks	**6.7%**	**8**
Federal Credit Unions	**1.2%**	**2**
Housing Finance Agencies	**0.3%**	**1**

Inside Mortgage Finance, "Top 50 Firms in Owned Mortgage Servicing: 2Q24," https://www.insidemortgagefinance.com/ (2024). Used with permission.

A decision preempting § 2954.8(a) would give national banks an unfair competitive edge by allowing them to ignore state interest-on-

[32] *See* Conference of State Banking Supervisors, *Reengineering Nonbank Supervision*, "Chapter Three: Overview of Nonbank Mortgage," at 27-35 (Sept. 2019) (describing the U.S. mortgage servicing market), https://www.csbs.org/sites/default/files/other-files/Chapter%20Three%20-%20Overview%20of%20Nonbank%20Mortgage_updated.pdf.

34.4escrow laws that apply to their state-chartered and state-licensed competitors. That outcome would conflict with 12 U.S.C. § 25b(b)(1)(B) and 15 U.S.C. § 1639d, which express a strong policy in favor of requiring national banks to comply with reasonable state interest-on-escrow laws. Preempting § 2954.8(a) would also (1) encourage state-chartered and state-licensed mortgage servicers to convert to national charters, undermining the States' authority to charter and regulate financial institutions; and (2) bolster the OCC's unlawful efforts to preempt state consumer protection laws, severely weakening the States' ability to protect consumers.

II. The OCC's Preemption Rule Violates 12 U.S.C. § 25b and Is Not Entitled to Any Deference.

Flagstar argues that § 2954.8(a) is preempted by a federal regulation, 12 C.F.R. § 34.4(a), which the OCC adopted in 2004 and reissued in 2011.[33] Both versions of § 34.4(a) declare that a "national bank may make real estate loans . . . without regard to state law limitations concerning: . . . (6) Escrow accounts."[34] The OCC's

[33] Flagstar Brief, *supra* note 4, at *6-*8, *33-*37.

[34] Bank Activities and Operations: Real Estate Lending and Appraisals, 69 Fed. Reg. 1904, 1917 (Jan. 13, 2004) (2004 OCC Preemption Rule);

regulation is unlawful, and not entitled to any deference, because the 2011 version violates 12 U.S.C. § 25b in several respects, and Congress and the Supreme Court repudiated the 2004 version.

A. The OCC's Regulation Violates 12 U.S.C. § 25b.

Under 12 U.S.C. § 25b(b)(1), the OCC may issue a regulation or order preempting a state consumer financial law "only if—. . . (B) in accordance with the legal standard for preemption in . . . *Barnett Bank*," the state law "prevents or significantly interferes with the exercise by the national bank of its powers." The OCC may not issue a preemptive regulation or order unless "substantial evidence, made on the record of the proceeding, supports the [OCC's] specific finding regarding the preemption of such [state law] in accordance with . . . *Barnett Bank*." *Id.* § 25b(c).

The OCC must act on a "case-by-case basis" when it issues a preemptive rule or order. *Id.* § 25b(b)(1)(B). To satisfy the "case-by-case" requirement, the OCC must consider "the impact of a particular State consumer financial law on any national bank that is subject to

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Office of Thrift Supervision Integration; Dodd-Frank Act Implementation, 76 Fed. Reg. 43549, 43569 (July 21, 2011) (2011 OCC Preemption Rule).

that law, or the law of any other State with substantively equivalent terms." *Id.* § 25b(b)(3)(A). The OCC must "first consult" with the Consumer Financial Protection Bureau (CFPB) and "take the views of the [CFPB] into account" before the OCC determines that "a State consumer financial law of another State has substantively equivalent terms as the one that the [OCC] is preempting." *Id.* § 25b(b)(3)(B).

The OCC violated several provisions of 12 U.S.C. § 25b when it issued the current version of 12 C.F.R. § 34.4 in 2011. First, the OCC's 2011 rule does not incorporate *Barnett Bank*'s "prevents or significantly interferes" preemption test, which Dodd-Frank codified in 12 U.S.C. § 25b(b)(1)(B). As *Cantero* confirms, the "prevents or significantly interferes" test is the "controlling legal standard" for determining "when a 'State consumer financial law' . . . is preempted with respect to national banks." 602 U.S. at 209, 213-14, 221.

The OCC intentionally omitted the "prevents or significantly interferes" standard from its 2011 rule. In adopting that rule, the OCC erroneously claimed that "the Dodd-Frank Act does not create a new stand-alone 'prevents or significantly interferes' preemption

standard."[35] The 2011 rule is plainly invalid for failing to incorporate the governing preemption standard established by *Barnett Bank*, codified in § 25b(b)(1)(B), and confirmed in *Cantero*.

Second, like the OCC's 2004 rule, the 2011 version of § 34.4(a) seeks to preempt fourteen broad categories of state consumer financial laws across the nation, including state laws regulating mortgage escrow accounts.[36] The 2011 rule's sweeping nationwide preemptions did not comply with Dodd-Frank's provisions requiring the OCC (i) to make preemption determinations on a "case-by-case basis," (ii) to support those determinations with "substantial evidence, made on the record of the proceeding," and (iii) to consult with the CFPB before preempting "substantively equivalent" laws enacted by more than one state. 12 U.S.C. §§ 25b(b)(1)(B), (b)(3) & (c).[37]

The OCC erroneously asserted that its 2011 rule did not need to comply with § 25b's requirements. The OCC claimed that the 2011

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[35] 2011 OCC Preemption Rule, *supra* note 34, at 43555.

[36] 2004 OCC Preemption Rule, *supra* note 34, at 1917; 2011 OCC Preemption Rule, *supra* note 34, at 43569.

[37] *See* Wilmarth, *Cantero*, *supra* note 12, at 111-13 (discussing the 2011 rule's multiple violations of 12 U.S.C. § 25b).

version of 12 C.F.R. § 34.4 carried forward the regulation's 2004 provisions, which remained valid after Congress enacted § 25b in 2010.[38]

The OCC's claim is untenable. Under § 25b(b)(1)(B), a State consumer financial law is preempted "only if" the OCC or a court makes a preemption determination in full compliance with § 25b's requirements. Dodd-Frank created a narrow exception to that requirement by including a limited grandfather clause, which preserves the applicability of preexisting OCC regulations and orders to "any contract entered into on or before July 21, 2010, by national banks . . . or subsidiaries thereof." 12 U.S.C. § 5553.

Dodd-Frank's limited grandfather clause makes clear that the OCC's preexisting preemption rules and orders – including its 2004 regulation – do not apply to transactions by national banks after July 21, 2010,[39] unless the OCC reissues those preemption determinations

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[38] 2011 OCC Preemption Rule, *supra* note 34, at 43557.

[39] In *McShannock v. JPMorgan Chase Bank, N.A.,* 976 F.3d 881, 885 n.3, 887 (9th Cir. 2020), this Court recognized that a "field preemption" regulation issued in 1996 by the Office of Thrift Supervision (1) had no further legal effect after Dodd-Frank's enactment and (2) applied only

in full compliance with § 25b. The OCC's contrary claim would make § 5553 meaningless, thereby violating "the canon against surplusage [that] is strongest when an interpretation would render superfluous another part of the same statutory scheme." *Marx v. Gen. Revenue Corp.*, 568 U.S. 371, 386 (2013).

Third, § 25b(d) requires the OCC to review each of its preemption determinations at least once every five years, after providing notice and opportunity for public comment. Following each review, the OCC must issue a public notice and a report to Congress stating whether the OCC intends to continue, rescind, or amend that preemption determination. The OCC has not conducted any review of 12 C.F.R. § 34.4 under § 25b(d), even though § 34.4 was issued over thirteen years ago.

Thus, § 34.4(a) is an invalid regulation that violates 12 U.S.C. § 25b in several respects. That regulation does not preempt Cal. Civ.

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to mortgage loans that were made by federal savings associations on or before July 21, 2010, as provided in § 5553.

Code § 2954.8(a) because it exceeds the OCC's authority[40] and represents an unlawful attempt to engage in "backdoor" preemption.[41]

B. The OCC's Regulation Is Not Entitled to Any Deference.

Under 12 U.S.C. § 25b(b)(5)(A), the OCC's preemptive rules and orders are not entitled to deference unless a reviewing court finds them to be "persuasive," based on the criteria specified in *Skidmore v. Swift & Co.*, 323 U.S. 134, 140 (1944).[42] Following the decision in *Loper Bright Enterprises v. Raimondo*, 603 U.S. 369, 389, 394, 402 (2024), all OCC interpretations of federal statutes governing national banks will receive only *Skidmore* deference. Under *Skidmore*, 12 C.F.R. § 34.4(a) is not entitled to any deference because Congress and the Supreme

[40] *Louisiana Pub. Serv. Comm'n v. FCC*, 476 U.S. 355, 374 (1986) ("[A] federal agency may pre-empt state law only when and if it is acting within the scope of its congressionally delegated authority.").

[41] *See* Catherine M. Sharkey, *Preemption by Preamble: Federal Agencies and the Federalization of Tort Law*, 56 DEPAUL L. REV. 227, 227-30, 251-52, 258-59 (2007) (criticizing efforts by federal agencies to achieve "backdoor federalization" by inserting unauthorized preemption claims in the preambles to their rules).

[42] *Lusnak*, 883 F.3d at 1192 (discussing the limited *Skidmore* deference given to OCC preemption determinations under 12 U.S.C. § 25b(b)(5)(A)).

Court repudiated the 2004 version of that rule, and the 2011 version violates several provisions of 12 U.S.C. § 25b.

As this Court observed in *Lusnak*, "Congress enacted Dodd-Frank in response to a 'financial crisis that nearly crippled the U.S. economy.'" 883 F.3d at 1189 (quoting S. Rep. No. 111-176, at 2 (2010)). The Senate Banking Committee determined that "a major cause" of the financial crisis was the "failure" of the OCC and other federal regulators "to stop abusive lending, particularly unsustainable home mortgage lending." S. Rep. No. 111-176, at 15 (2010) (quoting Travis Plunkett). Instead of supporting the States' efforts to combat predatory mortgage lending, the OCC preempted those efforts by issuing 12 C.F.R. § 34.4 in 2004. The OCC's 2004 regulation "exempted all national banks from State lending laws, including the anti-predatory lending laws." *Id.* at 16. The OCC's 2004 rule "actively created an environment where abusive mortgage lending could flourish without State controls." *Id.* at 17.[43]

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[43] *See also* Financial Crisis Inquiry Comm'n, *The Financial Crisis Inquiry Report* 13, 96-97, 111-13, 126 (2011) (criticizing the OCC's 2004 rule for preempting state anti-predatory lending laws) (FCIC Report), available at https://www.govinfo.gov/content/pkg/GPO-FCIC/pdf/GPO-FCIC.pdf.

Dodd-Frank repudiated the OCC's 2004 regulation by enacting 12 U.S.C. § 25b(b)(1)(B). Under § 25b(b)(1)(B), as the Senate Banking Committee explained, "[t]he standard for preempting State consumer financial law *would return*" to the "standard established by the Supreme Court in *Barnett*." S. Rep. No. 111-176, at 175 (2010) (emphasis added). As the Committee also made clear, § 25b(b)(1)(B)'s "prevents or significantly interferes" standard would have the legal effect of "undoing broader standards adopted by rules, orders, and interpretations issued by the OCC in 2004." *Id.*

In *Cuomo v. Clearing House Ass'n*, 557 U.S. 519 (2009), the Supreme Court rejected the OCC's underlying rationale for its 2004 preemption rule. The OCC's 2004 rule and a companion regulation declared that state laws applied to national banks only if they provided the "legal infrastructure that surrounds and supports the ability of national banks . . . to do business."[44] The Supreme Court disavowed the OCC's "infrastructure" rationale because it "can be found nowhere within the text of the statute" and "attempts to do what Congress

[44] *Cuomo*, 557 U.S. at 532-33 (quoting Bank Activities and Operations, 69 Fed. Reg. 1895, 1896 (Jan. 13, 2004)); *see also* 2004 OCC Preemption Rule, *supra* note 34, at 1912, 1913 (presenting the same "infrastructure" rationale).

declined to do: exempt national banks from all state banking laws, or at least state enforcement of those laws." *Id.* at 533.

Granting any deference to 12 C.F.R. § 34.4(a) would severely undermine the States' authority to protect consumers, thereby inflicting great harm on the American public that would extend far beyond mortgage escrow accounts. The OCC's regulation purports to exempt real estate loans made by national banks from fourteen broad categories of state consumer financial laws, including state laws regulating loan-to-value ratios, terms of credit, disclosure, advertising, mortgage origination and servicing, and use of credit reports. Deferring to that regulation would again expose consumers to the grave dangers created by the OCC's 2004 preemption rule.

As noted above, the Senate Banking Committee condemned the OCC's 2004 rule for having "actively created an environment where abusive mortgage lending could flourish without State controls." S. Rep. No. 111-176, at 17 (2010). Illinois Attorney General Lisa Madigan highlighted the devastating consequences of the OCC's 2004 rule in testimony presented to the Financial Crisis Inquiry Commission in 2010. As she explained, after the OCC issued the 2004 rule, "many of the largest mortgage-lenders shed their state licenses and sought shelter behind the shield of a national charter," thereby

hamstringing the States' efforts to combat predatory mortgage lending and unleashing "the worst lending abuses in our nation's history."[45]

This Court should reject Flagstar's argument that 12 C.F.R. § 34.4(a) preempts Cal. Civ. Code § 2954.8(a). The OCC's rule is invalid and not entitled to any deference because Congress and the Supreme Court repudiated the 2004 version of that rule, and the OCC adopted the 2011 version in a manner that was "not in accordance with law." *Loper Enterprises*, 603 U.S. at 391 (quoting 5 U.S.C. § 706(2)(A)).

Conclusion

This Court should adhere to its decisions in *Kivett* and *Lusnak* and reject Flagstar's preemption claim.

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[45] FCIC Report, *supra* note 43, at 13, 96-97, 113 (quoting Ms. Madigan's testimony).

UNITED STATES COURT OF APPEALS
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