



BANKING LEGISLATION & POLICY

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Recent Developments

MasterCard and Visa to Pay \$3 Billion in Antitrust Settlement

In April, MasterCard and Visa separately agreed to settle an antitrust suit, consenting to lower interchange fees, modify card policies, and pay over \$3 billion in damages over the next 10 years. The suit was brought by about 5 million merchants, including Wal-Mart Stores, Inc., The Limited, and Sears Roebuck & Co. The merchants argued that the card associations illegally tied their debit cards to their credit cards, forcing the retailers to accept signature debit payments (off-line debit) that carry a higher interchange fee than personal identification number (PIN)-based debit transactions (on-line debit). Merchants pay interchange fees to the card issuers for every card transaction. Off-line debit uses the credit card networks to clear and settle payments and can cost retailers about \$1.50 per \$100 transaction. On-line debit transactions are processed on ATM/POS networks where the interchange fee is about 15 cents.

The settlement occurred shortly after a U.S. district court ruled in favor of the plaintiff on many of the preliminary motions filed by the two sides (see *Judicial Developments* section). In addition to paying damages, both companies were to reduce their off-line debit interchange fees by August 1. In 2004, retailers will be able to decide whether or not to accept Visa and MasterCard debit cards along with their credit cards.

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Banks and Insurers Must Comply With FTC Do-Not-Call Rule

The Federal Communications Commission (FCC) announced that banks and insurers must observe the do-not-call list administered by the Federal

Trade Commission (FTC). Last fall the FTC issued a final rule to develop the do-not-call program to allow consumers to add their names to a list to indicate that they do not wish to be called by telemarketers. The FTC rule did not

apply to banks and insurers because the agency does not have authority over them, but the June 26 FCC rule extends the program to include the financial industry's telemarketers. These federal restrictions supercede any state do-not-call lists, although states will not be required to discontinue the use of their do-not-call lists. States that already have do-not-call lists are deciding separately whether or not to include their lists on the national list, meaning some consumers who have registered with their state's list may still have to register with the national database to have the protections of state and federal law.

On June 27 consumers began registering with the FTC by phone or online. The FTC and FCC will begin enforcing the do-not-call list October 1 for consumers who register by the end of August. The list does not apply to calls from tax-exempt, not-for-profit organizations and calls regarding political and religious speech. The rule permits firms to call customers with whom they enjoy an "established business relationship," which is presumed to exist for 18 months after a business transaction and three months after an inquiry or application.

The FTC rule also specifies certain performance requirements for telemarketing calls. Telemarketers may make

calls to people not registered on the list, but the calls must be transferred to a live sales agent within two seconds of the recipient's answering, to reduce "abandoned" and "dead-air" calls, when the recipient answers and there is no one on the line. Also, telemarketers must allow the phone to ring four times or for 15 seconds before disconnecting an unanswered call, and they are prohibited from blocking their caller identification information. Calls can be made only between 8 am and 9 pm, and callers must promptly tell the recipient the nature of the call, such as whether it is a sales pitch or a call from a charitable organization. The rule prohibits unauthorized billing for goods or services without express permission from the call recipient. Further, express permission must be obtained in writing before faxed advertisements may be sent to customers. For more information about the do-not-call rule, visit the FCC's web site at www.fcc.gov/cgb/donotcall or the FTC's web site, www.ftc.gov/donotcall. To reference the FTC's final rule, see 68 *Federal Register*, pp. 4580-679.

Visa and MasterCard Currency Conversion Fees to Be Refunded

Visa's and MasterCard's U.S. cardholders who used their cards to

make purchases in foreign countries after February 15, 1996, can expect a refund for currency conversion fees they paid for their purchases, a California superior court judge ruled April 5 (*Schwartz v. Visa International Corp.*, No. 822404-4). While the judge agreed the 1 percent fee was reasonable, he said the practice of not disclosing the fee to cardholders in monthly statements is unfair and in violation of the state's unfair competition law, the California Business and Professions Code.

The conversion fee is disclosed in the cardholder agreement, which is sent to customers when they receive their cards, but the fee is not itemized on monthly cardholder statements. The court found that customers are much more likely to read their monthly statements than the cardholder agreements. Therefore, the court reasoned, the currency conversion fee constituted a "hidden" charge. Visa International Corp., based in California, is required to refund all U.S. cardholders for fees paid since February 1996, and New York-based MasterCard International, Inc., is required to refund fees California cardholders paid in the same time period.

SUMMARY OF FEDERAL LEGISLATION

New Legislation

1. Fair and Accurate Credit Transactions Act (H.R. 2622). Introduced by Rep. Bachus (R-AL) on June 26, 2003.

Status: Ordered to be Reported by the House Committee on Financial Services.

Related Bills: H.R. 1766, S. 660, H.R. 2035, H.R. 818, S. 223

The House Financial Services Subcommittee on Financial Institutions introduced legislation to extend provisions of the Fair Credit Reporting Act (FCRA)

and to protect consumers from identity theft. The FCRA contains provisions that prevent states from enforcing certain credit reporting laws that are more restrictive than the FCRA, but those provisions are set to expire on January 1. This bill will remove the sunset provision to make uniform national credit reporting standards permanent. States would be prohibited from enforcing laws stricter than the FCRA that regulate: 1) the prescreening of consumer reports, 2) the time within which credit bureaus must respond to consumer disputes, 3) the duties of users of credit bureau informa-

tion, 4) the information contained in credit reports, 5) the duties of information providers, and 6) the exchange of information between affiliates.

Next, the bill combines features of other identity theft prevention bills introduced in Congress this year. The bill specifies that only the last four digits of a debit or credit card number may be printed on electronically printed receipts and the expiration date cannot be printed. Credit card issuers would be required to notify a consumer if they receive a change of address notification and a request for a new card in the same

30-day period. Federal banking regulators would be required to develop methods for depository institutions to recognize identity theft. Also, if a consumer is a fraud victim, he or she may request that a consumer reporting agency (CRA) include a fraud alert in his or her file. The fraud alert notifies credit issuers that the consumer doesn't want credit offered without special permission through an authorized procedure, such as by the consumer's approval at a specified telephone number. The Federal Trade Commission (FTC) would be required to develop procedures for CRAs to refer identity theft complaints and fraud alerts.

CRAs must develop policies and procedures for providing a notice of rights to consumers who believe they may be victims of fraud or identity theft. Consumers who file a police report to allege fraud can require any related information be removed from credit reports. If a person knows information is fraudulent or resulted from identity theft, he or she cannot give that information to a CRA. If a CRA learns that credit information is fraudulent, it would be required to notify the person about whom the information was filed. Consumers can notify a CRA or a reseller of information if they wish to have a CRA reinvestigate any disputed information contained in a credit report. Once notified, CRAs would be required to reinvestigate and update their records free of charge.

Consumers would be permitted to request one free copy of their credit report every year. The report must include the person's credit scores, a summary of how the scores were derived, and how the scores can be improved. If someone requests a report using an address that is different from the one on file with a CRA, the CRA must notify the requester of the discrepancy and update the information. The FTC would be required to develop procedures for victims of identity theft. The FTC and the Board of Governors of the Federal Reserve System will monitor how CRAs comply with the FCRA's requirements. Both agencies will report the results of their studies to Congress.

A final provision permits a consumer

report to be used in an investigation of an employee's suspected misconduct or illegal behavior. The information can be communicated to an employer as long as the report was not used to evaluate the person's credit standing. The information contained within the report may only be shared with the employer, or an agent of the employer, government officials, or a self-regulatory organization with authority over the employer and employee. The employer must disclose to the employee the nature and substance of any information contained within the report that results in an adverse action being taken against the employee.

2. Predatory Mortgage Lending Practices Reduction Act (H.R. 1663). Introduced by Rep. Jones (D-OH) on April 8, 2003.

Status: Referred to the House Subcommittee on Financial Institutions and Consumer Credit.

This bill requires that mortgage lenders and brokers be certified by the Department of Housing and Urban Development (HUD) to offer subprime mortgage loans. For purposes of this legislation, subprime mortgage loans are those where the borrower or the loan terms exhibit characteristics that indicate that the loan is subject to a significantly higher risk of default. To become certified, the lender or broker must demonstrate knowledge concerning: 1) federal laws related to mortgage lending, 2) appropriate subprime lending practices, 3) illegal and inappropriate subprime lending practices, and 4) contract laws regarding competency and incapacity to contract. Under this bill, the Secretary of Housing and Urban Development would be required to develop and implement the certification test and provide for training classes and materials, both written and on the World Wide Web. The secretary would also be responsible for determining when the certification would expire and how one could become recertified.

Subprime lenders would also be required to establish a "Best Practices"

plan. The plan would have to provide for the training and evaluation of employers, agents, and subcontractors to ensure that they are not engaging in predatory lending. Furthermore, the plan would have to include provisions for good faith resolutions of consumer complaints.

Lenders found to be engaging in unfair and deceptive acts or practices could be assigned civil penalties of up to \$10,000. HUD, along with the Board of Governors of the Federal Reserve System and the Federal Trade Commission, would be responsible for deciding what practices would be considered unfair and deceptive.

3. Small Business and Financial Institutions Tax Relief Act of 2003 (S. 850). Introduced by Sen. Allard (R-CO) on April 10, 2003.

Status: Referred to the Committee on Finance.

Related Bills: H.R. 714, H.R. 1896

This bill is designed to make it easier for banks to incorporate under Subchapter S, which would reduce tax burdens for many small banks. A Subchapter S corporation is one that elects a special tax status with the Internal Revenue Service to avoid a double-taxation at both the corporate and personal level by reporting all income or loss only once on stockholders' personal tax returns. Under this bill, the maximum number of shareholders allowed under Subchapter S would double to 150. Also, in the case of trust and individual retirement accounts that own bank stock, only the beneficiaries of the accounts would be treated as shareholders. If members of the same family own a bank's stock, that family would be treated as a single shareholder. Banks organized as S corporations would be permitted to issue preferred stock, and they would exclude interest income and dividends on assets that are held for liquidity purposes from their passive investment income test.

4. Secondary Mortgage Market Fair Competition Act (H.R. 2117). Introduced

by Rep. Stark (D-CA) on May 15, 2003.

Status: Referred to the House Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises.

This bill removes provisions of the Federal National Mortgage Association Charter Act that exempt government mortgage firms Fannie Mae and Freddie Mac from state and local taxation. This would allow private firms to better compete with the government-sponsored agencies.

5. Involuntary Bankruptcy Improvement Act of 2003 (H.R. 1529) Introduced by Rep. Sensenbrenner (R-WI) on April 1, 2003.

Status: Passed the House. Referred to the Senate Committee on the Judiciary.

This bill helps to clear the records of individuals harmed by false involuntary bankruptcy claims. Under current law, a debtor can be forced into bankruptcy if a creditor files an involuntary bankruptcy petition to preserve the debtor's assets. However, if the petition is found to have any false information in it and the court dismisses the case, this bill would allow the individual upon whom the claim was brought to request that the court expunge from all public records the case and anything relating to it. Also, the court can prohibit all consumer reporting agencies from reporting anything relating to the case.

6. Deposit Insurance Fairness and Opportunity Act (S. 913). Introduced by Sen. Santorum (R-PA) on April 11, 2003.

Status: Referred to the Committee on Banking, Housing, and Urban Affairs.

This bill ensures that financial institutions be returned the excess premiums paid into federal deposit insurance funds. When the amount of funds in the Bank Insurance Fund or Savings Association Insurance Fund exceeds 1.4 percent of total estimated

deposits insured, the surplus will be distributed to banks in the form of dividends. An institution's dividend share size will depend upon contributions to the funds since January 1, 1997.

7. United States Financial Policy Committee for Fair Capital Standards Act (H.R. 2043). Introduced by Rep. Bachus (R-AL) on May 9, 2003.

Status: Reported by Subcommittee to the full House Committee on Financial Services.

This bill establishes a committee to develop uniform U.S. positions on issues before the Basel Committee on Banking Supervision, which is currently developing new rules on international bank capital requirements. The new committee will be composed of the Secretary of the Treasury, the Chairman of the Board of Governors of the Federal Reserve System, the Comptroller of the Currency, and the Chairman of the Federal Deposit Insurance Corporation. The committee will report to Congress annually about proceedings in the preceding year and also before reaching any agreement with the Basel Committee. Reports to Congress would evaluate the cost of the Basel proposal, the effect on U.S. financial systems, the impact on competition, and the need for additional supervision and examination.

8. Consumer Privacy Protection Act of 2003 (H.R. 1636). Introduced by Rep. Stearns (R-FL) on April 3, 2003.

Status: Referred to the House Subcommittee on Commerce, Trade, and Consumer Protection.

When data collection agencies gather personally identifiable information from a consumer, they would be required to notify the consumer if the information might be used for purposes unrelated to the transaction in which it was collected. Personally identifiable information includes a person's first and last name, address, and telephone number. For purposes of this bill, data collection

agencies are defined as entities that collect, sell, disclose, or otherwise use a consumer's personally identifiable information. The bill does not apply to governmental agencies, not-for-profit entities, and other small-scale firms, defined as having fewer than 25 employees and having an annual gross revenue that is less than \$1 million.

Agencies covered by the bill would be required to develop privacy policies that explain what types of information may be used and by whom, and whether the consumer is required to provide the information to do business with the agency. If the information is subject to being sold, the privacy policy must further address who the buyers might be, what information might be bought, and how it might be used. The Federal Trade Commission (FTC) would be responsible for helping to design uniform wording and logos for the privacy policy notices.

Data collection agencies would also be required to provide consumers with the opportunity to either refuse to allow their information to be sold or disclosed or to permit it. This opportunity must be clearly outlined in the privacy policy and easily accessible to the consumer. These privacy programs would be self-regulated by the agencies, but the FTC would approve the self-regulatory program.

9. Financial Contracts Bankruptcy Reform Act of 2003 (H.R. 2120). Introduced by Rep. Toomey (R-PA) on May 15, 2003.

Status: Referred to the House Subcommittee on Commercial and Administrative Law.

This bill would make it easier for companies to net out their debts on derivative contracts and reduce the risk of loss in the event of a counterparty going bankrupt. The Federal Deposit Insurance Corporation and the National Credit Union Administration Board would be able to transfer a defaulting institution's contracts to a healthy financial institution without waiting for

bankruptcy court approval. Similar provisions were included in a broader House bankruptcy bill, H.R. 975, that passed the House in March.

10. The Securities Fraud Deterrence and Investor Restitution Act of 2003 (H.R. 2179). Introduced by Rep. Baker (R-LA) on May 21, 2003.

Status: Forwarded by Subcommittee to the full House Committee on Financial Services.

This bill would give the Securities and Exchange Commission (SEC) more

authority to investigate, punish, and deter securities laws violations. The SEC would be able to increase fines for securities fraud and return money to defrauded investors. The bill would allow the SEC to obtain and investigate a person's financial records without a court order. The SEC could preclude financial institutions from notifying customers that their records had been obtained by the SEC.

Pending Legislation

1. Check Clearing for the 21st Century Act (H.R. 1474). Introduced by Rep. Hart (R-PA) on March 27, 2003.

Status: Passed by both the House and the Senate.

This act would allow banks to transmit electronic checks for payments instead of using paper checks. To be a valid substitute, an electronic check must have all of the information on the front and back of the original check and state that it is a copy. This act will not require banks to use electronic checks instead of paper checks. For more information, see *Banking Legislation and Policy*, January-March 2003.

SUMMARY OF FEDERAL REGULATION

Financial Crimes Enforcement Network

Customer Identification (5/9/03)

Together, the Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of Thrift Supervision, and National Credit Union Administration issued a final rule to implement sections of the USA PATRIOT Act that require financial institutions to verify customers' identities when they open accounts. The rule requires banks, savings associations, credit unions, private banks, and trust companies to: (1) implement procedures to verify the identity of customers opening accounts, (2) maintain records of the information used to verify the person's identity, and (3) determine whether the person appears on any government lists of known or suspected terrorists.

First, financial institutions must develop and implement a customer identification program (CIP) that contains procedures for verifying a customer's identity. The CIP is to be part of the bank's overall Bank Secrecy Act compliance program. The bank must obtain from all customers a name, birth date, address, and an identification number, such as a taxpayer identification

number or other government-issued document. The CIP must include a description of the methods the financial institution will use to verify that the customer-provided materials are accurate. The CIP must also address how the financial institution will determine within a reasonable period of time if a customer is on any government-provided list of known or suspected terrorists. Financial institutions should keep records of the identifying information they received from the customer and the procedures they used to verify the accuracy of that information for at least five years after the account is closed or becomes dormant.

Beyond the basic requirements, the rule allows banks a substantial amount of flexibility in implementing their CIPs. The purpose of banks' having CIPs is to be reasonably sure they know the identity of their customers. So, for types of accounts that are at low-risk of being used by terrorists or money-launderers, the minimal standards may be sufficient. Other types of accounts that are higher-risk would require the bank to go further to verify a customer's identity.

This final rule became effective June 9, and financial institutions must be in compliance by October 1. For more information, see 68 *Federal Register*, pp. 25090-113.

Office of the Comptroller of the Currency

Foreign Banks (4/23/03)

The Office of the Comptroller of the Currency (OCC) issued this proposal to make rules regarding foreign banks' operations at U.S. branches more consistent with rules regulating similar operations at national banks. The proposed rule allows well-capitalized and well-managed U.S. branches of foreign banks (federal branches) to make noncontrolling equity investments in U.S. companies. Like national banks, the federal branch would need to provide notice to the OCC no more than 10 days after making the investment.

If an eligible federal branch opens a new office intrastate or expands its activities, it would be subject to expedited review. Currently these activities are subject to the same review process that a foreign bank would go through to open its initial federal branch. The proposal would require only that the federal branch notify the OCC 45 days in advance of the new branch's establishment. Opening a new office would require regulatory approval but would not require an additional license unless the new office had expanded activities. A federal branch will not be required to file with the OCC if it

contracts its activities. Finally, federal branches will no longer need to notify the OCC when closing or relocating. Comments on this proposed rule were due June 23. For more information, see 68 *Federal Register*, pp. 19949-58.

Derivatives (4/21/03)

In an April 21 letter (*OCC Interpretive Letter #962*), the OCC permitted a national bank to deal in electricity derivatives involving transfers of title to electricity. Bank of America was already engaged in cash-settled customer-driven derivative transactions involving electricity. The OCC concluded that allowing the bank to settle and hedge electricity derivative transactions by instantaneous transitory title transfers would not submit the bank to further risks. In such transactions, the bank will take title to electricity in a "chain of title," where the bank will pass the title down a chain from the initial seller to the ultimate buyer in a series of instantaneous back-to-back transactions. Therefore, the bank will never take actual physical delivery of electricity, but will temporarily hold title to it. Because Bank of America has already proven its ability to manage and handle risks associated with cash-settled derivative transactions, the OCC permitted it to engage in transitory title transfers, subject to appropriate safety and soundness measures.

The bank must enhance its risk measurement and management systems to accommodate transferring title. This will entail establishing a risk-management program including board supervision, managerial and staff expertise, and risk identification and control. Also, the bank must review electricity derivative contracts to verify that they conform to the bank's standards of integrity. Finally, the bank must develop a program to monitor its compliance with its policies and other regulatory requirements.

The Board of Governors of the Federal Reserve System

Foreign Banks (5/30/03)

The Federal Reserve Board (the Board)

issued a proposal amending Regulation K that would require edge and agreement corporations and foreign banks with U.S. offices to develop procedures to monitor compliance with the Bank Secrecy Act (BSA). Board-regulated U.S. branches and agencies of foreign banks would need to include in their BSA compliance program: (1) a system of internal controls to ensure ongoing compliance, (2) independent testing of compliance, (3) the designation of an individual or individuals responsible for coordinating and monitoring day-to-day compliance, and (4) training for appropriate personnel. These rules are consistent with those for domestic financial institutions.

Comments on this proposed rule were due June 30. For more information, see 68 *Federal Register*, pp. 32434-7.

Commodity Contracts (6/30/03)

The Board of Governors of the Federal Reserve System issued a final rule to amend Regulation Y, allowing bank holding companies (BHC) to enter into derivatives contracts that result in taking or making delivery of title to commodities on an instantaneous, pass-through basis without physically holding or transferring the commodity. For certain commodities, BHCs will also be able to enter into derivative contracts that do not require cash settlement or assignment, termination, or offset prior to delivery. For more information, see *Banking Legislation and Policy*, January-March 2003.

This final rule became effective August 4. For more information, see 68 *Federal Register*, pp. 39807-10.

Financial Accounting Standards Board

Qualifying Special-Purpose Entities (6/10/03)

The Financial Accounting Standards Board (FASB) issued a proposal that would refine the definition of qualifying special-purpose entities (QSPE), which were exempted from rules for consolidating assets and liabilities recently published in FASB's Interpretation No. 46 (see *Banking Legislation and Policy*, January-March

2003, for more information). Interpretation No. 46 instructed companies to consolidate variable interest entities (VIE), entities controlled by means other than voting interests, if the company is exposed to a majority of the risk of loss or is entitled to receive a majority of the VIE's residual returns. Consolidation would not be required, however, if the entity in question is a QSPE.

The proposal would amend FASB Statement 140 to refine the definition of QSPEs. To qualify, an entity must be distinct from the company that transfers assets to it (the transferor), and the assets transferred must be beyond the reach of a bankruptcy trustee (or other receiver) should the transferor enter bankruptcy. Second, the transferor may not exercise control over the assets transferred and the SPE must have the right to pledge or exchange the assets. Third, the SPE's activities and discretion must be limited by rules specified in the documents that create it, and those rules may be changed only by a vote of a majority of the beneficial interests held by investors other than the transferor. In particular, the SPE's ability to dispose of noncash financial assets must be limited to an automatic response to certain predetermined conditions. Finally, the financial assets transferred to the SPE must be passive in nature and must not include equity instruments. The SPE may hold servicing rights and passive derivative instruments as long as the counterparty is not the transferor.

Additional restrictions disqualify an entity from being a QSPE if the transferor or an owner of junior interest in the SPE provides liquidity facilities to assist the SPE in satisfying its financial obligations. Such liquidity facilities include financial guarantees, written options, or obligations to purchase beneficial interests from other investors. Owners of a junior interest in an SPE may not exercise control over the SPE's reissuance of beneficial interests (for example, rolling over commercial paper). If an SPE engages in the reissuance of beneficial interests, no single investor may provide a majority of the liquidity facilities available to the SPE. In general,

these provisions ensure that the transferor will not be obligated to come to the aid of the SPE should the SPE encounter financial difficulties.

This interpretation will be applied prospectively to SPEs beginning in the first quarter after it becomes final for public companies and after the first year for private companies. Existing SPEs will be evaluated on the basis of the accounting standards in existence at the time they were created, provided that they do not issue new beneficial interests or receive assets from the transferor in excess of those committed prior to the effective date of the statement.

Department of Housing and Urban Development

Flipping (5/1/03)

The Department of Housing and Urban Development (HUD) issued a final rule to reduce the instances of property "flipping," whereby a house that was recently bought, usually only a few days before, is resold for an artificially inflated value. These flipped properties will no longer be eligible for Federal Housing Administration (FHA)-insured mortgage financing, because now to be eligible, a property must be owned at least 90 days by the seller before it can be resold. Further, if the property is resold

90 to 180 days after the seller acquired it, the lender is required to document differences between the selling price and the purchase price if the selling price is somewhere between 50 and 150 percent above the purchase price, with the exact percentage to be determined by HUD. HUD is also permitted to impose additional rules for properties sold within 12 months of being purchased, including requiring additional documentation and appraisals.

This final rule became effective June 2. For more information, see 68 *Federal Register*, pp. 23370-6.

SUMMARY OF JUDICIAL DEVELOPMENTS

MasterCard and Visa Lose Several Preliminary Motions In the "Wal-Mart Suit"

The recent settlements in the Wal-Mart antitrust case between retailers and credit card associations Visa and MasterCard (see **Recent Developments**) occurred shortly after a federal district court ruled on preliminary motions submitted by each side. MasterCard and Visa asked the judge to dismiss the retailers' claims that the card companies had attempted to monopolize the debit card market and had attempted to tie debit card acceptance with credit card acceptance. Additionally, MasterCard requested a separate trial from Visa. The judge denied each of these motions.

The retailers also made several preliminary motions. They asked the judge to find that the defendants had worked independently and together to illegally tie credit cards to debit cards, forcing retailers to accept debit cards. The plaintiffs argued the associations' conduct represented a per se violation of antitrust law. The associations countered that any decision at trial should be based on the "rule of reason test." In general, it is more difficult to

establish illegal monopolistic behavior under the rule of reason test.

Under the per se test, the retailers would have to show the following: 1) that the tying arrangement affects a substantial amount of interstate commerce; 2) the two products are distinct; 3) the defendant actually tied the sale of the two products; and 4) the seller has appreciable market power in the tying market. In the preliminary hearing, the judge ruled that Visa had satisfied all of those conditions, and MasterCard had satisfied the first three, with the fourth to be determined at trial. The judge left open the possibility that a fifth element, foreclosure of competition or anti-competitive effect in the tied product market, might need to be considered.

The judge did not conclude that the trial would be decided on the basis of the per se test. Rather, the judge mentioned that the per se analysis had been used less frequently in deciding recent antitrust law, and the case might be better decided at trial using the rule-of-reason analysis. Under the rule-of-reason test, the merchants would have to prove that the associations' actions had an adverse

effect on competition. If the associations could show a pro-competitive redeeming virtue of their actions, the retailers would have to show that the same effect could have been achieved through an alternative means less restrictive to competition.

Federal Law Preempts State Usury Claims Against National Banks

The U.S. Supreme Court decided that actions filed in state courts against national banks for charging excessive interest may be removed to federal court because the claim arises under federal law, even if the complaint does not specifically refer to any federal law (*Beneficial National Bank v. Anderson*, No. 02-306, 6/2/03). In an Alabama court, taxpayers filed an action against Beneficial National Bank for allegedly charging usurious interest rates on tax refund anticipation loans. Beneficial is a national bank chartered under the National Bank Act (NBA). Beneficial removed the case to federal court, arguing that the NBA governs the amount of interest it may charge, and therefore, because the claim arises under federal law, it should be decided in

federal court. Specifically, sections 85 and 86 of the NBA establish the maximum interest rates national banks may charge and provide remedies for charging excessive interest. The U.S. Court of Appeals for the Eleventh Circuit held that the case should be remanded to state court, but the U.S. Supreme Court reversed.

The court noted that, as a general rule, a civil claim filed in state court would not be removable to federal court unless it specifically cites a federal claim, known as the “well-pleaded complaint” rule. Exceptions to that rule, however, include “complete preemption” provisions. If a federal law completely preempts a state law under which a claim is filed, the case is removable to federal court because it arises under federal law. The court decided that the NBA provided the exclusive cause of action for usury claims against national

banks, and therefore, the case arises under federal law and is removable to federal court.

Cities Cannot Ban ATM Fees

The U.S. Supreme Court left standing an earlier decision that cities could not ban automated teller machine (ATM) fees (*The City and County of San Francisco v. The Bank of America*, No. 02-1404, 5/27/03). In October, the U.S. Court of Appeals for the Ninth Circuit ruled that federal laws, particularly the Home Owners’ Loan Act (HOLA) and National Bank Act (NBA), preempt laws in San Francisco and Santa Monica that prohibit banks from charging noncustomers ATM fees. Both California cities banned ATM fees, saying they harm consumers, especially the poor and elderly who have less mobility, and undermine competition as customers at small financial institutions switch to larger ones with

more machines to avoid incurring fees for using other banks’ ATMs. The cities claimed that the Electronic Funds Transfer Act (EFTA) gives them the right to govern ATM fees as a consumer protection measure.

The Ninth Circuit disagreed, saying that banning fees is not a consumer protection that the EFTA intended, and the act’s anti-preemption provision does not preclude preemption of state laws by the HOLA and the NBA. The court reasoned that the HOLA and the NBA permit the Office of Thrift Supervision and the Office of the Comptroller of the Currency, respectively, to regulate savings associations and national banks. The regulators allow financial institutions to charge fees for ATM transactions. Therefore, the cities’ ordinances prohibiting ATM fees cannot be enforced.

SUMMARY OF THIRD DISTRICT DEVELOPMENTS

New Jersey

On May 1, New Jersey became the most recent state to adopt anti-predatory lending legislation as Governor James McGreevey signed a bill to curb abusive mortgage lending practices (P.L. 2003 Chapter 64). The bill prohibits creditors from financing health, life, debt cancellation, and debt suspension insurance. Also, creditors cannot make a loan to refinance a home loan that originated within the previous 60 months, known as loan “flipping,” unless the loan benefits the borrower. The law also places restrictions on late payment fees, prepayment fees, fees for balance inquiries, and provisions that allow the creditor to accelerate indebtedness.

The bill also places limitations on “high-cost home loans,” defined as loans for which the principal amount is less than \$350,000 that also meet or exceed the annual percentage rate threshold or certain total points and fees thresholds. High-cost home loans

cannot have scheduled payments that are more than double earlier average scheduled payments (“balloon payments”). The law also prohibits negative amortization and increasing interest rates upon default. Creditors wishing to make high-cost home mortgage loans must present a notice to the borrower that warns of the costs and consequences of high-cost home loans and acknowledges the probability of finding a lower-cost loan somewhere else. Before a borrower can finance points and fees in connection with a high-cost home loan, the creditor making the loan must receive confirmation that the borrower was counseled by a U.S. Department of Housing and Urban Development approved credit counselor.

Pennsylvania

Secretary of Banking William Schenck sent a letter to state-chartered banks, bank and trust companies, savings banks, and savings and loan associations warning

them to avoid relationships with third-party payday lenders. In his letter he defined payday loans as “small-dollar, short-term unsecured loans that borrowers promise to repay out of their next paycheck or regular income payments.” He cautioned that the Pennsylvania Department of Banking would respond similarly to federal banking regulators in addressing payday lending relationships and the safety and soundness risks they impose. The letter set a new requirement that prior to a bank’s entering the payday lending business, either on its own or through a third party, it should notify the department in writing. The notification should include an analysis of the risks involved with the proposal and identify the measures the bank would take to monitor and control for those risks.

For more information, the secretary’s April 1 letter is available at the department’s web site at www.banking.state.pa.us.