Problems of Federalism in the Regulation of Consumer Financial Services Offered by Commercial Banks, Part I

Ralph J. Rohner

The Catholic University of America, Columbus School of Law

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PROBLEMS OF FEDERALISM IN THE REGULATION OF CONSUMER FINANCIAL SERVICES OFFERED BY COMMERCIAL BANKS: PART I

Ralph J. Rohner*

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* Professor of Law, The Catholic University of America School of Law. A.B., 1960; J.D. 1963, The Catholic University of America.

This article is based on a report entitled Problems of Federalism in the Regulation of Consumer Financial Services Offered by Commercial Banks, prepared by the author in 1978-79 for the Task Force on State and Federal Regulation of Commercial Banks, Federal Deposit Insurance Corporation, Washington, D.C. Copies of the original report are available from the FDIC.
In this first half of a two-part article, the author reviews the complex structures through which federal and state consumer protection laws are enacted and enforced with respect to commercial banks. Problems arise from the multiplicity of law-making bodies, the dual banking system, unclear preemption standards, and expanding federal domination of the consumer credit field. The second part of the article, which will appear in the next issue of this Review, analyzes the actual enforcement activities of the federal and state banking agencies. It concludes with a series of recommendations for improving the combined federal-state consumer protection programs affecting commercial banks.

I. OVERVIEW

A. The Consumer Financial Services Marketplace — Federal and State Regulatory Roles

When the late Senator Paul Douglas first introduced his proposal for a federal Truth in Lending law in 1960, he could hardly have envisioned the profound impact that federal entry into the consumer credit arena would have over the ensuing two decades. The business of providing consumer financial services was at that time almost exclusively under state regulatory
domain, and the body of state "consumer protection" laws affecting cus-
tomer-bank transactions was skeletal at best.¹

In the single decade from 1968, when Truth in Lending was enacted, to 1978, the federal presence in the consumer credit regulatory field has grown enormously. Congress has enacted numerous laws with the result that federal laws protecting bank customers now outnumber state laws in scope, complexity, and probably in importance. The center of gravity in bank-customer protections has clearly moved from the state capitals to Washington. Yet many of the states remain actively interested in consumer protection on their own. A Uniform Consumer Credit Code was proposed for general enactment by the states in 1968, a revised version was published in 1974, and 11 states have adopted at least the substance of it. Other states have continued to enact laws of their own design affecting bank-customer transactions, and there is incorporated into existing federal laws a strong policy of assuring the states a continuing regulatory role. This explosion of consumer credit laws is paralleled by vast growth in the volume and sophistication of consumer credit transactions.

While the role of commercial banks as extenders of consumer credit is substantial, banks are, of course, not the only participants in that large market.² Thrift institutions, consumer finance and small loan companies, retail merchants, credit unions, and others all operate within the perimeter of a broadly defined consumer financial services market. This presence of institutions other than commercial banks is significant in several respects. It creates a measure of competition among all of them for the consumer's credit trade, and a similar measure of competition among banks, thrift institutions, and credit unions for the consumer's deposit accounts. Thus, any analysis of regulatory structures must take into account the competitive environment of commercial banks. In addition, laws designed to protect consumers in their financial dealings tend to be drawn along transactional lines rather than by category of credit grantor or deposit holder. The Truth in Lending Act, and the Equal Credit Opportunity Act, to cite two federal statutes, and the Uniform Consumer Credit Code, to cite an instance of comprehensive state legislation, are applicable to all forms of credit transactions involving all types of creditors. Thus, while consumer

¹. For a general discussion of the history and development of consumer credit legisla-
tion, see B. CURRAN, TRENDS IN CONSUMER CREDIT LEGISLATION (1965).

². Of the more than $282 billion in consumer installment credit outstanding in April, 1979, almost $140 billion, or 49%, was held by commercial banks. In addition, through the fourth quarter of 1978, more than $846 billion in 1-to-4 family residential mortgage credit was outstanding, of which $127 billion, or 15%, was held by commercial banks. See 65 FED. RES. BULL. A41, A42 (1979).
protections are usually legislated with a wide horizontal sweep, the existing regulatory and enforcement structures tend to segment the market vertically, along institutional and industry lines. \(^3\) Regulatory complexity is therefore compounded by the existence of two functionally independent levels of lawmaking and enforcement, one federal and one state.

Ordered complexity, of course, may be the characteristic of a well-designed, well-synchronized, and highly sophisticated piece of machinery, a fine Swiss watch, perhaps; but the complexity that pervades the consumer credit marketplace is almost totally unordered. The regulatory structures that presently affect the transactions between commercial banks and their customers are a jerry-built accumulation of historical tinkering, the result of political compromises regarding the respective roles of federal and state governments. The product of the present system is ineffective consumer protection caused either by duplicative legislation with overlapping enforcement responsibilities or by fragmented lawmaking and enforcement which permits gaps, contradictions, frictions, and grey uncertainties to exist in the network of consumer protection.

The factual bases for these conclusions and recommendations for improvement are developed in the following pages. This article takes as a "given" the existence of a substantial and growing body of federal and state consumer protection laws; it does not directly address the question of whether any of the present or proposed laws are substantively unwise, imprudent, or otherwise undesirable. Rather, the focus throughout is on problems arising from the bifurcated structures through which consumer laws are promulgated and enforced.

**B. Synopsis of Conclusions**

Both the federal and state governments have strong, legitimate interests in protecting individuals who are consumers of financial services. This market is largely comprised of a series of local markets where customers and creditors usually do not range far beyond the boundaries of their town, city, or metropolitan area. Such transactions are properly matters for state regulation. There is, however, a growing national scope to the

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\(^3\) At the federal level, consumer creditors are supervised by either the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation (FDIC), the Federal Reserve Board (Board), the Federal Home Loan Bank Board (FHLBB), the National Credit Union Administration (NCUA), the Federal Trade Commission (FTC), the Civil Aeronautics Board (CAB), the Farm Credit Administration (FCA), or other agencies. At the state level, enforcement responsibility may be held by bank commissioners, consumer finance administrators, state attorneys general, or statewide consumer protection offices. See *Consumer Credit in the United States, Report of the Nat'l Comm. on Consumer Finance* 48-53 (1972) [hereinafter cited as NCCF Report].
consumer financial services marketplace. Consumers move, shop across state lines, and utilize services provided by creditors operating nationwide or who are franchisees of nationwide systems. Furthermore, computerized information exchanges about consumers span the continent. Strong national policies such as fundamental fairness in contractual obligations, non-discrimination, community responsibility by financial institutions, and economic stabilization are reflected in the consumer protection laws as well as strong state policies such as the prevention of fraud and usury.

Given the certainty of a continuing dual regulatory structure, absolute uniformity of law and enforcement is probably unattainable. Nonetheless, there should at least be reasonably uniform application of laws to institutions and affected consumers. Duplication, overlapping, and uncertainties in the applicable substantive laws are undesirable, as are confusion, lack of coordination, or outright hostility among the various agencies charged with enforcement responsibilities. Inefficiency in consumer protection is undesirable because it inevitably leads either to higher compliance and enforcement costs, which are passed on to consumers, or to gaps in the regulatory and enforcement environment, resulting in less consumer protection.

Two broad general conclusions emerge. First, where federal and state lawmakers both have virtually unfettered authority to regulate the same aspects of the same transactions, undesirable results are almost certain to occur unless one level of government has a preeminent role. In fact, this balance can be modulated only by a clear and conscious choice by Congress as to the respective state and federal positions. Congress has not yet made that choice. Second, given a dual structure, the multiplicity of regulatory and enforcement bodies is itself a source of discordant, inefficient regulatory and enforcement policies. This unsatisfactory situation will continue unless those agencies are coordinated through consolidation or openly cooperative programs. Overall coordination of consumer protection can be achieved only through the mutual efforts of federal and state authorities.

II. Applicable Substantive Law and Enforcement Authority

The first source of difficulty in the regulation of consumer financial services is that substantive laws and rules issue from Congress, from a number

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4. This sentiment is hardly novel. In 1972, the National Commission on Consumer Finance expressed its belief that “[f]rom a consumer’s standpoint there is no persuasive reason why the governmental role in enforcing his rights under credit laws cannot be performed in a uniform, consistent manner by a minimum number of different agencies.” NCCF REPORT, supra note 3, at 45.
of federal agencies, from fifty state legislatures, and at times from local
governments. Each of these lawmaking bodies has its own legal authority
to regulate aspects of bank-customer transactions, but there is no structure
to assure that the resulting mass of regulatory provisions are coordinated
and complementary. Consumer spokespersons naturally want the oppor-
tunity to press their case for new laws in as many alternative forums as
possible, thus heightening their chances of having some success.\(^5\) Industry,
on the other hand, understandably objects to the proliferation of these
laws, to the "race to legislate" attitude that multiple lawmaking bodies
engender, and to the sometimes conflicting requirements imposed on their
members.\(^6\) The extent and nature of this proliferation of substantive rules
requires elaboration.

A. Federal Laws and Regulations

Beginning in 1968, the federal government has been increasingly active
in the field of consumer credit regulation. The growing number of federal
initiatives appears in statutes, in implementing regulations, and in agency
rules and guidelines. Despite the number of these laws and regulations,
they do not occupy the whole of the consumer credit field because the
original source of substantive laws was the states. Broad areas such as
usury and interest rate regulation, creditor rights and remedies, credit
insurance, and similar matters are still virtually exclusively matters of state
law.

This is not the place to dwell on the substantive provisions of the various
federal statutes. For convenient reference, all of these laws, along with the
regulatory and enforcement authority they contain, are set out in Appen-
dix A. What is important to appreciate is the wide-ranging coverage of
these laws, from credit cost disclosure, to discrimination in credit transac-
tions, debt collection, credit reporting, financial privacy, and the equally
diverse and asymmetrical allocation of enforcement and rule-writing au-
thority.

\(^5\) Thus, most of the federal consumer protection laws have a very limited preemptive
effect on similar state laws, preserving the state legislatures as alternative forums where con-
sumers can shop for stronger protections. See, e.g., 15 U.S.C. § 1610 (1976) (TIL preemp-
tion provision) and notes 113-26 and accompanying text infra.

\(^6\) These industry concerns are expressed constantly in congressional testimony, in
agency rulemaking comments, and in the industry press. A less rhetorical presentation of
those concerns, written by persons who represent banks, is Brandel & Danchuk-McKeithen,
The Relationship of Federal to State Law in Electronic Fund Transfer and Consumer Credit
1. Statutes

The existing federal statutory consumer protection laws constitute an eclectic set of rules dealing with part, but by no means all, of the consumer credit marketplace. These laws were drafted and enacted at different times, in response to particular needs then perceived by Congress.

This collection of federal laws can be generally grouped into two categories reflecting division in the enforcement operations of the federal banking agencies. One group of statutes are those principally addressing civil rights protections for bank customers and banks' community responsibilities in general. This group includes the Equal Credit Opportunity Act (ECOA), the Fair Housing Act (FHA), the Home Mortgage Disclosure Act (HMDA), and the Community Reinvestment Act (CRA).

7. Each of the three agencies, the Board, FDIC, and OCC, has reorganized its enforcement functions to give greater emphasis to enforcement in the consumer credit area. See Banking Regulatory Agencies' Enforcement of the Equal Credit Opportunity Act and the Fair Housing Act: Hearings Before a Subcomm. of the House Comm. on Government Operations, 95th Cong., 2d Sess. (1978).


9. 42 U.S.C. §§ 3601-3619 (1976). The Fair Housing Act of 1968 (FHA) prohibits banks and other lenders from denying mortgages or home improvement loans on the basis of race, color, religion, sex, or national origin. This legislation somewhat overlaps ECOA in the area of real estate credit. Although there is no general implementing regulation, the FDIC and FHLBB have each issued data-notation regulations drawing on the authority of both ECOA and FHA. See 12 C.F.R. §§ 338 (FDIC), 528 & 531 (FHLBB) (1979). The OCC has recently proposed similar regulations. See 44 Fed. Reg. 22,396 (1979).

10. 12 U.S.C. §§ 2801-2809 (1976). The Home Mortgage Disclosure Act (HMDA) is a limited congressional response to "redlining," a practice in which mortgage lenders decline to make mortgage loans in certain geographic areas, usually the inner city. HMDA requires financial institutions in metropolitan areas to compile annually and disclose to the public the location of all their residential mortgage loans by census tract or zip code. The Board has implemented the HMDA in Regulation C. See 12 C.F.R. § 203 (1979).

11. 12 U.S.C. §§ 2901-2905 (Supp. 1 1977). The Community Reinvestment Act (CRA), enacted in 1977, places responsibility on financial institutions to reinvest deposited funds in their respective communities through mortgage loans and other credit extensions. The CRA directs the Board, OCC, FDIC, and FHLBB, the federal supervisory agencies subject to CRA, to consider, when deciding on all requests for charters, branches, or insurance, the extent to which the institution complies with this public policy. Each of these four agencies has issued uniform regulations to implement the CRA. See 43 Fed. Reg. 47,144 (1978) (to be codified at 12 C.F.R. §§ 25, 228, 345, 563e).
other group of federal statutes, Truth in Lending (TIL), the Real Estate Settlement Procedures Act (RESPA), the Fair Debt Collection Practices Act (FDCPA), the Fair Credit Reporting Act (FCRA), and the Electronic Fund Transfer Act (EFTA), concerns disclosure and certain "un-

12. 15 U.S.C. §§ 1601-1667e (1976). The Truth in Lending Act (TIL), Title I of the CCPA, requires disclosure of credit costs and terms in both open-end and closed-end credit transactions. It also regulates the contents of credit advertising, id. §§ 1661-1665a, and requires a cooling-off period for certain credit transactions involving security interests in real property. TIL has been amended several times to add new substantive provisions. Certain credit card amendments were added in 1970, barring unsolicited mailings and limiting consumer liability for unauthorized use. Id. §§ 1642-1643. Additional amendments include the Fair Credit Billing Act and the Consumer Leasing Act. For a discussion of these acts, see note 23 infra.

13. 12 U.S.C. §§ 2601-2617 (1976). The Real Estate Settlement Procedures Act (RESPA) is a congressional attempt to alleviate problems with home mortgage settlements. Originally the Act required advance disclosure of actual settlement costs, but the amended Act now requires the mortgage lender to provide an informational booklet which includes an advance estimate of settlement charges, 12 U.S.C. § 2604(a)-(e) (1976), and to provide at the time of settlement disclosures of actual charges on a uniform settlement sheet, id. § 2603. Additionally, the Act prohibits kickbacks of settlement fees, id. § 2607, bars tied-in sales of title insurance, id. § 2608, and limits escrow accounts for taxes and insurance, id. § 2609. Regulations interpreting and implementing RESPA have been issued by the Secretary of Housing and Urban Development. See Regulation X, 24 C.F.R. § 3500 (1979).

14. 15 U.S.C.A. §§ 1692-1692o (Supp. 1979). The Fair Debt Collection Practices Act (FDCPA), Title VIII of the CCPA, sets out a number of prohibitions against abusive or coercive collection practices, id. §§ 1692d-1692f, and requires all collectors to provide debtors with certain information, including verification of the outstanding debt, id. § 1692g. FDCPA applies almost exclusively to independent debt collectors and generally does not apply to creditors who collect their own debts. The Act, however, clearly includes reciprocal bank collections, and banks engaging in that practice must comply. See id. § 1692a(6). In contrast to ECOA and TIL, the FDCPA explicitly prohibits any interpretive regulations. Id. § 1692(f).

15. 15 U.S.C. §§ 1681-1681t (1976). The Fair Credit Reporting Act (FCRA), Title VI of the CCPA, regulates the content, accuracy, and disclosure of credit reports and investigative reports furnished to creditors, employers, or insurers in connection with consumer transactions. Although the primary responsibilities under FCRA are imposed on credit reporting agencies, users and suppliers of information, including banks, are also bound by its provisions. There is no regulation-writing authority under FCRA. The only existing guides to compliance are Federal Trade Commission (FTC) interpretations.

16. 15 U.S.C.A. §§ 1693-1693r (Supp. 1979). The Electronic Fund Transfer Act (EFTA), was enacted as Title IX of the CCPA. "Electronic fund transfer systems" refers to various kinds of computerized systems for effecting paperless transfers of debits and credits. The systems range from automated teller machines to direct payroll deposit, to preauthorized transfers (as for regular monthly rent or utility bills), to point-of-sale terminals permitting immediate crediting of the merchant's account and debiting of the consumer's. The substantive provisions of the EFTA include mandatory disclosure of the terms of the customer's agreement with the system operator, id. § 1693c, required procedures for documenting transactions for the customer's records either at point of transaction or in monthly statements, id. § 1693d, error resolution procedures so that customers will not be unduly deprived of deposited funds, id. § 1693f, and limitations on consumer liability for
“fair” practices in consumer transactions.

Despite the joining of much of this legislation under the umbrella of the Consumer Credit Protection Act (CCPA), it is not a comprehensive or systematic body of law. It does not deal with credit pricing (usury), creditor security or collection practices, or credit insurance — except to the extent disclosure of these matters is required under TIL. Since Congress continues to leave the regulation of credit interest rates to the states, the various federal laws do not make any effort to relate compliance costs to prevailing rates, leaving creditors with the burden of absorbing those costs under whatever rate structure the state establishes. Furthermore, there is no consistent scope to the federal laws: TIL applies to “consumer credit” transactions; FCRA affects not only credit transactions but also employment, insurance, and other business transactions; ECOA applies to all credit transactions, whether consumer, commercial, or anything else, but not to other forms of customer financial services; the new EFTA affects only EFT transactions which by definition are not credit transactions at all.

2. Regulations, Rules, and Guidelines

The Federal Reserve Board (Board) has the largest role in issuing interpretive regulations under the existing federal consumer credit laws. It alone is specifically empowered to issue regulations and binding interpre-

unauthorized transfers, id. § 1693g. Additionally, the EFTA gives regulation-writing authority to the Board. Id. § 1693b.

17. Pub. L. No. 90-321, 82 Stat. 146 (codified in scattered sections of 12, 15, 18 U.S.C. (1976)). CCPA is the general name for the collection of nine statutory titles ranging from TIL through EFTA, titles adopted and amended at various times between 1968 and 1978. See Appendix A. In addition to TIL, FCRA, ECOA, FDCPA, and EFT, CCPA includes Title II, which proscribes extortionate credit transactions, those which charge an interest rate above 45% and involve collection by threats of violence. Criminal sanctions are applicable and are enforced by the Justice Department. Title II does not provide regulation-writing authority or other administrative enforcement. 18 U.S.C. §§ 891-896 (1976). Title III of the CCPA deals with garnishment of debtors’ wages. It establishes a minimum level of wages exempt from garnishment and prohibits an employer from discharging an employee for a single garnishment. The Secretary of Labor is charged with enforcement. See 15 U.S.C. §§ 1671-1677 (1976).

18. For example, a credit card issuer who charges the maximum 1 1/2% per month permitted by state law cannot simply raise its rate to 1 3/4% to cover the expenses of reprinting application forms, designing adverse action notices, and retraining personnel, all of which are necessitated by the federal ECOA. The creditor must seek its rate increase from the state legislature which is typically unsympathetic to burdens imposed by Congress.


20. See id. §§ 1681-1682.

21. See id. § 1691a.

tations under TIL — including the Fair Credit Billing Act (FCBA) and the Consumer Leasing Act (CLA) — ECOA, EFTA, and HMDA. The Board has dutifully issued regulations under each of these laws — Regulation Z for TIL, Regulation B for ECOA, Regulation E for EFTA, and Regulation C for HMDA.

In the case of TIL and ECOA, the Board's role is not limited to issuance of official "regulations." It also issues "interpretations" of those regulations which have the effect of insulating creditors from civil or criminal liability if their practices conform to the interpretations. In addition, the Board's staff has authority to issue official interpretations, without Board review, with a similar protective effect.

Furthermore, the Board has authority to issue regulations, similar to Federal Trade Commission (FTC) trade regulation rules, proscribing unfair or deceptive practices by banks. This authority, conferred in 1975 amendments to the Federal Trade Commission Act, is twofold. It requires the Board to issue parallel regulations whenever the FTC issues a trade regulation rule unless the Board can justify different treatment for banks; it also authorizes the Board to regulate deceptive banking practices on its own initiative.

The Board has proposed, but not yet adopted, certain regulations under

23. The Fair Credit Billing Act (FCBA), 15 U.S.C. §§ 1666-1666j (1976), and the Consumer Leasing Act (CLA), 15 U.S.C. §§ 1667-1667e (1976), were enacted as chapters four and five of TIL. The FCBA requires creditors to establish procedures for responding to credit billing disputes on open-end credit transactions. It also provides for regulating creditor remedies and limiting open-end creditors' ability to avoid consumer claims and defenses. The CLA requires disclosures comparable to those for credit transactions for the increasingly common long-term leases of consumer goods.


26. Allowing for some that have been superseded, there are about 58 Board interpretations of TIL currently in effect. See 12 C.F.R. §§ 226.101-.1503 (1979). There have been four interpretations issued under ECOA. See 12 C.F.R. §§ 202.801, 202.1101-.1103 (1979).

27. The Board has issued approximately 160 official staff interpretations ("blessed letters") under Regulation Z, see 12 C.F.R. § 226, App. (1979), but fewer than 15 under Regulation B, see 12 C.F.R. § 202, App. (1979). Additionally, Board staff have issued approximately 1400 unofficial opinions under Regulation Z, but fewer than 15 under Regulation B.


29. 15 U.S.C. § 57a(f) (1976). "Trade Regulation Rules" issued by the FTC or parallel regulations issued by the Board contain descriptions of practices found to be unfair or deceptive after quasi-legislative hearings by the issuing agency. Such FTC rules have the force of law, and the FTC can seek penalties of $10,000 per day for violations. Parallel Board regulations would be enforced against banks under the Financial Institutions Supervisory Act (FISA), 12 U.S.C. § 1818(b) (1976). For a discussion of FISA and its impact, see notes 58-69 and accompanying text infra.
Problems of Federalism

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this mandate.\textsuperscript{30}

(1) The FTC issued its celebrated “Holder” Rule in 1975,\textsuperscript{31} which effectively abolished holder-in-due-course protection for financers of consumer credit purchases by requiring sellers to incorporate specified language in all credit contracts. The compliance burden under the rule rests exclusively on sellers. At the same time, however, the FTC proposed an amendment to its own rule which would extend the compliance responsibility to any “creditor” (\textit{i.e.}, finance company or similar third party).\textsuperscript{32} The Board has therefore proposed a regulation which would impose parallel duties on banks which finance consumer sales.\textsuperscript{33}

(2) Also in 1975, the FTC proposed an extensive “Credit Practices” Rule\textsuperscript{34} which would prohibit or curtail a number of traditional creditor protections, such as cognovit notes, waivers of exemptions, wage assignments, non-purchase money security interests, attorney’s fees clauses, and co-signer agreements. The Board has proposed a virtually identical regulation for banks.\textsuperscript{35}

(3) In 1976 the FTC proposed a rule requiring disclosures in connection with the sale of used cars: a seller could be required to reveal, among other things, the prior use of the vehicle, its mileage, any known defects, and the identity of seller’s chief executive officer.\textsuperscript{36} The Board has not proposed a companion rule, although it seems clear they will have to issue one to apply to banks as repossessors, and thus sellers, of automobiles.

The Board has not yet used its authority to deal with unfair or deceptive practices without following the FTC’s lead.\textsuperscript{37}

The Board is not the exclusive regulator of consumer credit transactions involving commercial banks. The other bank supervisory agencies, the Office of the Comptroller of the Currency (OCC) and the Federal Deposit Insurance Corporation (FDIC), have some independent regulatory authority under their own organic statutes. For example, the OCC has issued regulations concerning credit insurance practices by national banks.\textsuperscript{38} The

\textsuperscript{30} It is likely that some modified form of each proposed rule will be issued by the FTC. Accordingly, the Board will have 60 days within which to publish its own version or justify the lack of need for such rules for banks. \textit{See} 15 U.S.C. \textsection 57a(f)(l) (1976).

\textsuperscript{31} 16 C.F.R. \textsection 433 (1979).


\textsuperscript{34} 40 Fed. Reg. 16,347 (1975).

\textsuperscript{35} Id. at 19,495.


\textsuperscript{37} As noted in note 29 \textit{supra}, this authority is granted under 15 U.S.C. \textsection 57a(f) (1976).

\textsuperscript{38} 12 C.F.R. \textsection 2 (1979). As promulgated, this regulation is directed at bank safety rather than consumer protection. Essentially, it prohibits bank directors from retaining the
OCC has also issued interpretive letters responding to requests from national banks, thus duplicating the advisory functions performed by the Board. All three agencies have joined in efforts to promulgate Uniform Enforcement Guidelines for TIL and ECOA which are not formal regulations but rather joint statements of enforcement policy implemented if necessary by cease and desist orders. The banking agencies and Federal Home Loan Bank Board (FHLBB) have also issued parallel regulations and enforcement guidelines for the CRA. The FTC, although it has no authority to regulate banks directly, has issued several trade regulation rules which affect banking practices. By affecting the dealer-consumer contract, these regulations indirectly bind the banks which purchase consumer paper from retail dealers whose practices are directly regulated by the FTC's rules.

One such trade regulation rule applies to door-to-door sales, requiring sellers to give consumers a three-day cooling-off period in which they can rescind any purchase made elsewhere than the seller's regular place of business. Banks can safely purchase such "rescindable" paper only if the FTC rule has been complied with by the seller. A second rule with even more impact on banks is the so-called "Holder" Rule. This rule requires sellers to include a notice preserving all the consumer's claims and defenses in retail credit sales. It also requires sellers to decline to accept the

proceeds of credit insurance commissions or rebates. The explanatory statement by OCC, however, indicates that consumers may receive indirect benefit from lower insurance premiums. See 42 Fed. Reg. 48,518, 48,525 (1977).

39. See [1976] 5 CONS. CRED. GUIDE (CCH) ¶¶ 42,091-96 (OCC Interpretive Staff Letters interpreting Regulation B).


42. See 16 C.F.R. § 429 (1979).

43. There has been no case law involving an assignee's rights on consumer paper where the FTC rescission notice has been improperly omitted, but at least one court has concluded that omission of the required notice entitles the consumer to court-ordered cancellation of the contract. Donnelly v. Mustang Pools, Inc., 84 Misc. 2d 28, 374 N.Y.S.2d 967 (1975).

proceeds of certain direct loans — from banks or other lenders — unless a similar notice has been included in the loan agreements. Banks, as holders of consumer obligations containing the notice, are exposed to vicarious liability for the dealer's sins.

These divisions of regulatory functions among several federal agencies not only mean that there is no single federal consumer credit regulator, but also that there is a second level of lawmaking below Congress but still at the federal level. Within that second level of agency rulemaking, the multiplicity of regulatory voices is a cause for concern, not so much as a matter of principle but because of the inconsistent regulatory pattern that has emerged.

Multi-agency rulemaking may theoretically be a good practice. A measure of competitiveness among agencies may lead to healthy experimentation or provide useful marketplace options for consumers. Discrete industry segments or differing transactional patterns may justify differing regulatory approaches. Certainly it is true that each of the federal agencies has its unique relationship with its segment of the credit industry, and thus its unique perception of the need for regulatory measures in that segment. Therefore, divided rulemaking authority is not inherently irrational.

Multi-agency rulemaking becomes undesirable, however, when it produces confusion and uncertainty for consumers or creditors, when it unjustifiably treats like transactions differently, and when it causes one agency's rules to intrude on the regulatory domain of another. The resulting inefficiencies outweigh the theoretical good of permitting variations in regulatory approaches.

While there may be instances of “healthy” divergence in agency rulemaking, there have also been instances of what seems to be undesirable uncoordinated rulemaking. The FTC's “Holder” Rule technically applies only to retail dealers, yet it exposes banks to the risk that dealer-generated paper may be uncollectable! Although issuance of the Rule brought a strong complaint from the then-Chairman of the Federal Reserve Board, the banking agencies were powerless to affect its drafting or promulgation. Similarly, the FTC has expressed its serious unhappiness at regulatory proposals from the Board affecting non-bank creditors, where the FTC had no authoritative role in preparing those proposals. The

45. See Letter from Arthur F. Burns, Chairman, Board, to Calvin J. Collier, Chairman, FTC (May 5, 1976). This story has been retold in the trade press. See, e.g., Consumer Trends, May 18, 1976, at 2-3.

46. For example, the FTC petitioned the Board to suspend recent amendments to Regulation Z, 12 C.F.R. § 226.9 (1979), concerning rescission of open-end credit transactions secured by real estate. See Washington Credit Letter, Oct. 16, 1978, at 6.
tension between the regulatory roles of the Board and the FTC has heightened recently. At the FTC's suggestion, the Board amended its procedures for issuing staff interpretations so that proposed interpretations would be published for public comment and suspended pending consideration of those comments. The Board had been chagrined when the FTC challenged nearly every proposed Board staff interpretation, even the most innocuous. On the other hand, the FTC cried "foul" when Sears, Roebuck & Co. petitioned the Board for protective amendments or interpretations of Regulation B at the very time when the FTC was investigating the company for possible violations of that regulation.

An agency also may introduce some "regulatory" confusion through its enforcement function if its cease and desist orders mandate compliance duties in addition to, or inconsistent with, those required under another agency's basic regulation. This has occurred in recent FTC cases involving credit insurance disclosures pursuant to the Board's Regulation Z. Even among the agencies regulating financial institutions, there are examples of inefficient rulemaking which are not justifiable on grounds of regulatory competition or experimentation. For example, the FDIC and the FHLBB have issued expansive data-notation regulations to implement the FHA and the ECOA, but the Board has not done so for its supervised institutions. Additionally, the FHLBB has adopted a disclosure requirement for variable rate mortgages at variance with that generally required under the Board's Regulation Z. In short, substantive rulemaking authority divided among so many federal agencies is neither logical, efficient, nor consumer protective.

3. Enforcement Responsibilities for Federal Laws
   a. Allocation of Responsibility

Not only is regulatory authority for consumer transactions of commercial banks divided among several agencies, but the responsibility for actually enforcing compliance with consumer laws and regulations is also frag-

47. Typical of the FTC's requests to suspend a Board official staff interpretation is that reported in 43 Fed. Reg. 55,746 (1978). The Board's "chagrin" is the author's perception.
49. See In re USLIFE Credit Corp., [1978] 5 CONS. CRED. GUIDE (CCH) ¶ 97,938 (FTC Final Order); id. at ¶ 97,871 (Reconsidered Final Order). The FTC's order was reversed by the Fifth Circuit, which held that the FTC could not demand more of creditors than the Board's Regulation Z specifically required. USLIFE Credit Corp. v. FTC, 599 F.2d 1387 (5th Cir. 1979).
50. See note 9 supra.
mented among a number of agencies, and not necessarily those with rulemaking authority. For example, with respect to consumer compliance, commercial banks are supervised by either the FDIC, the Board, or OCC depending on the bank's charter or membership status. Yet the scope of the agencies' supervisory responsibility includes federal statutes, regulations promulgated exclusively by the Board or by HUD, regulations promulgated by the agency itself, state laws, and, arguably, FTC trade regulation rules.

Administrative enforcement responsibilities under the various federal consumer protection laws are generally divided along traditional jurisdictional lines: OCC for national banks, the Board for state member banks, and FDIC for state non-member insured banks. The degree of explicitness with which these agencies are charged to enforce the laws, however, varies with each law. TIL, for example, expressly directs the agencies to enforce it under the Financial Institutions Supervisory Act (FISA); the FHA contains a general directive to all federal agencies to share in its implementation. RESPA, on the other hand, does not assign direct enforcement duties to any agency. Other agencies have an enforcement role under certain laws, a role that may involve them in enforcement actions against banks regularly supervised by other federal agencies.

Except for the consistent assignment of enforcement duties under the CCPA, the division of overall consumer protection responsibilities is haphazard. In some instances responsibility is allocated along industry lines, at other times allocated by function to a single agency, and, as in the case of RESPA, not specifically allocated to anyone. The recent establishment of the Financial Institutions Examination Council may provide a vehicle for coordination of these enforcement duties among the five regulatory agencies supervising depository institutions. But even the Council has no clear mandate to determine the extent and priority of bank agency en-

52. The agencies' authority is ultimately as broad as the language of the FISA, see 12 U.S.C. § 1818(b) (1976), which authorizes administrative cease and desist proceedings whenever an institution is violating any law or regulation. See notes 58-72 and accompanying text infra; Appendix A.
57. The Council was created by the Federal Financial Institutions Examination Council Act of 1978, Pub. L. No. 95-630, tit. X, 92 Stat. 3694 (codified at 12 U.S.C.A. §§ 3301-3308 (Supp. 1979)). Its mandate is to "prescribe uniform principles and standards for the Federal examination of financial institutions by the [OCC], [FDIC], [FRB], [FHLBB], and [NCUA],
forcement duties under FTC rules, state laws, or federal laws with no internal enforcement allocation.

b. The Scope of the FISA

Even absent explicit directions, the Board, the OCC, and the FDIC have broad authority under the FISA\textsuperscript{58} to oversee bank compliance with all applicable federal and state consumer credit laws by initiating cease and desist proceedings against banks on findings of unsafe or unsound practices, or on findings of violations of laws or regulations.\textsuperscript{59} This enforcement authority is not limited to conventional bank solvency laws and can be read to include all federal or state laws which are binding on banks, an interpretation consistent with the traditionally dominant concern for the safety and soundness of banks. Patterns of violations of consumer credit laws could expose banks to judgments for damages or civil penalties, or might jeopardize the collectability of consumer obligations or the enforcement of security interests. Therefore, compliance with applicable consumer credit laws and regulations may be viewed as a dimension of safety and soundness.\textsuperscript{60}

The report of the National Commission on Consumer Finance (NCCF) in 1972 went even further, asserting that the FISA "provides Federal agencies with the authority and power to require financial institutions under their jurisdiction to comply with all applicable laws, including existing state consumer credit protections laws."\textsuperscript{61}

\begin{footnotesize}
59. The critical text of FISA provides that the Board, OCC, and FDIC may initiate cease and desist proceedings:

If in the opinion of the appropriate Federal banking agency, any insured bank . . . is engaging or has engaged, or the agency has reasonable cause to believe that the bank is about to engage, in an unsafe or unsound practice in conducting the business of such bank, or is violating or has violated, or the agency has reasonable cause to believe that the bank is about to violate a law, rule or regulation, or any condition imposed in writing by the agency in connection with the granting of any application or other request by the bank, or any written agreement entered into with the agency . . .


60. The view that compliance may be seen as a dimension of bank safety and soundness has been recognized in congressional oversight reports on federal bank agency enforcement authority. See Report on Consumer Protection Enforcement Activities, S. REP. NO. 1388, 94th Cong., 2d Sess. (1976).
61. See NCCF REPORT, supra note 3, at 53 (emphasis supplied).
\end{footnotesize}
The NCCF Report noted that the language of the FISA is written in the disjunctive — cease and desist orders may be directed at unsound practices or violations of law — and concluded that "violations of law are per se an adequate basis for agency action irrespective of the possible impact of the violations on institutional soundness."\(^{62}\) Thus, it is not necessary to demonstrate that violations of consumer laws jeopardize a bank's solvency in order to justify agency enforcement action.

For example, RESPA does not allocate explicit enforcement authority to any agency, though it does provide certain private remedies for consumers who encounter violations.\(^{63}\) This risk of potentially numerous private law-suits makes it both necessary and proper for the bank regulatory agencies to examine for compliance with RESPA. Similarly, where state laws applicable to banks set maximum interest rates, place limitations on permissible security, or prescribe prepayment rebate practices with penalties or forfeitures applicable to creditors who do not comply, it would seem appropriate for the federal agencies to consider compliance with those laws as part of their supervisory responsibility.

The legislative history of the FISA supports this construction of the agencies' role. The pertinent reports are chiefly concerned with corrupt practices by banks and bank officials but indicate a broad fear that "improperly conducted institutions could cause public concern that might extend to the entire industry."\(^{64}\) The legislative history also assumes that the "corrupt practices" which would jeopardize the bank's soundness or cause public concern may consist of violations of state criminal and civil laws.\(^{65}\)

The FISA antedates the now-substantial federal presence in the consumer credit regulatory arena, and it is therefore possible to argue that the Act does not constitute a general mandate for the federal banking agencies to become universal consumer protection agencies. It is true that the FISA grew out of concern for depositor protection, not borrower protection, but it may not be easy to separate the two. In addition, even if the FISA did not originally contemplate borrower protection, Congress has consciously and specifically expanded its scope by incorporating its enforcement powers into the CCPA and other consumer legislation.

Under the present dual enforcement system, the allocation of enforcement responsibilities to federal and state officials does not depend solely on whether the laws to be enforced are federal or state enactments. Ac-

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62. Id.
65. Id.
According to the NCCF report and to agency staff, the FDIC and the Board continue to believe that the primary responsibility for enforcement of state consumer laws rests with the state supervisors. This view may be attributable to the agencies' recognition that state law enforcement would be a heavy burden on their resources and their expertise. The attitudes of the FDIC and the Board, however, may be somewhat ostrich-like. Because of their deference to state responsibility, these federal agencies appear to be doing little to assure bank compliance with state consumer laws, even where it is readily apparent that the state supervisors are not enforcing those laws either.

At OCC the Comptroller's examiners have not been reviewing national banks for compliance with state laws, except for reviews of finance charges. At the same time, the Comptroller has vigorously defended his exclusive visitorial powers over national banks and has generally refused state officials access to bank records for purposes of determining compliance with state consumer laws. The result is an enforcement vacuum which has brought strong criticism from congressional oversight committees. OCC has now publicly acknowledged its responsibility to enforce state laws and has begun a process of gathering and identifying those laws. But OCC's approach is cautious: it has stated its intention to enforce state laws to the extent that state officials enforce them for state banks. This may leave some enforcement vacuum in any state where local officials are conducting only limited compliance examinations of their own.

As a matter of pure policy, therefore, each of the three federal bank agencies is free to utilize the extraordinary authority of the FISA to police bank compliance with state as well as federal consumer protection laws. Not having done so up to now reflects agency judgment as to feasibility and deference to the primary authority of the states. It is noteworthy that the NCCF Report, which concluded that the federal agencies had this

66. See NCCF REPORT, supra note 3, at 53-55.
69. See Letter from Comptroller Heimann to State Bank Supervisors (Aug. 2, 1977) (requesting officials to identify which state laws were enforced against state banks by the state agencies).
70. To conduct compliance examinations with respect to state laws in more than fifty different jurisdictions would require substantial training programs for the OCC examiners, including the preparation of new and expanded training materials and examiner handbooks. Additionally, expanded compliance reviews would also require more time for each examination, necessitating either a larger number of examiners or a truncated exam format, both unattractive options.
power and observed that substantive state law rights "appear to be of mini-
mal concern to federal banking agencies, if, indeed, they are any concern 
at all,"71 did not contain an explicit recommendation that the federal agen-
cies launch state law enforcement programs. It did recommend that state 
oficials be allowed limited access to federally chartered institutions to ex-
amine for compliance with state laws. The Report also stated the Commis-
sion's view that safety and soundness should be primarily a federal respon-
sibility.72 Implicit in these suggestions is the notion that state law 
compliance should continue to be the state's responsibility.

In conclusion, much of the criticism which has been leveled at federal 
agency enforcement efforts by congressional committees, state bank super-
visors, and others, and much of the inefficiency of these existing enforce-
ment programs is rooted in a fragmented enforcement structure, without 
any significant coordinating devices. This results in uncertain expectations 
on all sides as to which agencies are to perform which regulatory func-
tions.

c. Private Enforcement

Most of the federal laws under discussion also contain private enforce-
ment provisions intended to compliment enforcement by public agencies, 
although there are differences among the various provisions. For example, 
section 130 of TIL permits an aggrieved consumer to recover twice the 
finance charge in the transaction with a minimum recovery of $100 and a 
maximum of $1,000 regardless of the creditor's intentions or due care.73 
These inducements have led to a large volume of TIL private litigation.74 
Under the FCRA a consumer may recover actual or punitive damages but 
only upon a showing of negligence or intentional noncompliance.75 Pri-
ivate litigation under this title has been modest. The ECOA sets a maxi-
mum $10,000 recovery in addition to any actual 
damages,76 while the 
FDCPA has a $1,000 maximum, but no minimum recovery provision.77 
The FHA also permits a private suit for damages up to $1,000 per viola-

71. NCCF REPORT, supra note 3, at 54-55.
72. Id. at 57-59.
74. TIL cases filed in the federal courts alone have numbered around 2,000 per year 
on Truth in Lending, 1977 U. ILL. L.F. 669; Miller, Annual Survey of Consumer Law Develop-
76. Id. § 1691e.
77. Id. § 1692k (Supp. I 1977).
The significant point is that there are similar but not identical private enforcement mechanisms for most of these federal laws, supplementing whatever agency enforcement they specify.

To the extent violations of consumer protection laws expose banks both to agency enforcement and to civil liability, the banks' risks multiply. Those risks increase further when private class action or multiple class action judgments are considered. Private enforcement is not synchronized with agency activity, even though it is aimed at the same goal as agency policing. Private lawsuits are not subject to agency control, and hence are not useful as part of a coordinated, prioritized enforcement effort. It is therefore possible that vigorous agency enforcement can have the additional benefit of reducing overall compliance costs by eliminating the need for some of the cost-inefficient private litigation.

B. State Laws

1. Types and Scope

State laws in the consumer credit area are an utter hodgepodge. One reason is that virtually every state has had usury laws and other rate regulatory provisions for many decades. The number of these rate laws in any given state tended to grow as the legislature carved out special rate ceilings for various classes of transactions or for different types of creditors. These laws were uniquely local responses to the demand for consumer credit and to the political environment in the jurisdiction. Other state consumer credit legislation has evolved because of particular abuses occurring in those jurisdictions or because of the activism of consumer organizations.

One significant reason for the crazy-quilt pattern of state laws is the lack of a readily acceptable uniform state act. The Uniform Consumer Credit Code (UCCC) promulgated in 1969 was generally unacceptable to con-

79. Concern over large class action judgments for civil penalties prompted Congress to set statutory ceilings on class action recoveries for TIL, 15 U.S.C. § 1640(a)(2)(B) (1976), ECOA, 15 U.S.C. § 1691e(b) (1976), and FDCPA, 15 U.S.C. § 1692k(a)(2)(B) (Supp. I 1977), not to exceed $500,000 or one percent of the net worth of the creditor, whichever is less. The possibility remains, however, that separate class actions might succeed against each of a large creditor's retail outlets. See Barber v. Kimbrell's, Inc., 577 F.2d 216 (4th Cir. 1978) (appellate court ordered trial court to review entry of maximum award in favor of class consisting of customers of one of 48 stores in a chain). The pending Truth in Lending Simplification and Reform Bill, S. 108, 96th Cong., 1st Sess. (1979), would make the class action ceiling applicable to any class action "or series of class actions arising out of the same failure to comply."
80. See generally NCCF REPORT, supra note 3, at 91-108.
81. See [1976] 1 CONS. CRED. GUIDE (CCH) ¶¶ 5001-5703 for the text of the 1969 version of the UCCC.
Problems of Federalism

Consumer representatives and to part of the credit industry as well. Though six states adopted a version of the UCCC, it drew nowhere near the consensus support that the Uniform Commercial Code had almost twenty years earlier. A revised UCCC was promulgated in 1974, but no state has adopted the revised version intact. The prospects for further widespread enactment of the UCCC are dim because many states, particularly the large commercial and population centers, have raced ahead with nonuniform enactments of their own.

The nationwide mass of state consumer credit laws can be divided into three broad categories. One group consists of those laws that parallel federal legislation such as TIL and ECOA. A second category of immense complexity consists of those state laws setting maximum rates creditors may charge in consumer transactions. A third category is composed of those state laws regulating contract terms and creditor remedies.

Into the first of those categories would fall state “little Truth in Lending Acts” regulating the basic disclosure of credit terms. A number of states have enacted laws requiring cooling-off periods in door-to-door sales or in credit transactions which create security interests in the debtor’s residence. Similarly, a number of states have enacted laws dealing with credit billing dispute procedures, and these laws continue despite enactment of the FCBA as a chapter of TIL.

Recent years have also seen widespread enactment of state laws barring credit discrimination and “redlining” mortgage practices. Some of these laws closely resemble the federal ECOA or HMDA; others are more lim-


86. For a listing of these state statutory provisions, see Monograph No. 8, A Compilation of Federal and State Laws Regulating Consumer Financial Services 94-106, 512-16 (Cred. Res. Center, Purdue Univ. 1977) [hereinafter cited as Purdue Study].
ited or more expansive in their categories of protected applicants. There are also a number of states which have laws dealing with credit reporting, debt collection, and real estate settlements, and a few states have laws protecting the users of EFT systems.87

Laws setting maximum rates for credit transactions range from traditional usury laws to special laws permitting higher rates for mortgage transactions, special small loan laws, industrial loan laws, laws permitting special rates for revolving credit such as bank credit cards or other open-end plans, and laws limiting the time-price differential in credit sales of goods. Usually this array of rates within a particular state is embodied in legislation, but occasionally the state constitution inhibits the legislature's ability to adjust rates. At other times, there may be no general usury law, but a regulatory board may be authorized to set maximum rates for certain categories of small transactions.

Incidental to the question of what percentage rate may be charged for various transactions is the question of what additional charges that creditor may impose in the transaction. Thus, state laws contain almost countless differences in their approach to such matters as permissible extra service charges, broker's fees, credit investigation fees, filing fees, credit insurance premiums, and computational methods for the stated applicable rate. For revolving credit transactions, several states have specified which of the various balance assessment methods are permissible and which are unlawful.88

Except in those few states which have adopted the UCCC, there are absolutely no standardized categories for the types of transactions to which the various rates apply. The matter of rate regulation is wholly ad hoc within each state. It is, therefore, impossible to speak, for example, of the rates for “mortgage loans,” “personal loans,” or “home improvement loans,” and have these categories mean the same thing from one state to another. The complexity of this body of law is enhanced by the fact that however the rate is expressed or permitted to be computed under state law, all such rates must ultimately be translated into annual percentage rates for TIL disclosure purposes.89 Further complexity is introduced by the possibility that transactions involving consumers within a particular state

87. Id. at 28-69, 75-80, 107-14, 928-41.
88. Id. For a listing of state laws regarding rates for credit transactions, see id. at 115-279; for a listing of state laws pertaining to additional charges, see id. at 293-507.
89. For example, a recent revision to the Virginia rate laws specifies that the permissible rate is 7% add-on but that the creditor must communicate this as an Annual Percentage Rate (APR). See VA. CODE ANN. § 6.1-330.17 (Supp. 1978).
may in fact be governed by the laws, including the rate of ceilings, of another state.

The third large category of state law provisions contains all those matters limiting the contractual protections and remedies the creditor might otherwise assert. These typically would include prohibitions against oppressive contract remedies such as confession of judgment clauses or cognovit notes, restrictions on collateral available as security, restrictions on deficiency judgments following repossessions, prohibitions or limitations on the use of negotiable instruments or waiver of defense clauses, prohibitions of abusive collection practices, and limitations on cosigner agreements.\(^9\)

As in the case of the federal consumer credit laws, what is significant is not the precise provisions in effect in each state but the depth and array of each state's legislative interventions.\(^1\)

2. Applicability to Banks

The preceding summary of state laws does not differentiate between laws directly applicable to banks and those imposing primary responsibilities on retailers, consumer finance companies, and other creditors. At times, state law provisions may be universally applicable to all creditors. Much of the UCCC is of this scope. But more often the volume of state law applicable to sales credit is larger and more detailed than that applying directly to bank loans. Disclosure requirements are more comprehensive, limitations on security and default procedures are more likely to be imposed on retail merchants than on bank lenders, proscriptions against unfair and deceptive practices are generally directed at retailers and not at direct lenders. Thus, the provisions of state law that are usually of immediate concern to banks are rate limits and attendant restrictions on charges, computations, penalties, and rebates, credit insurance limitations, and some limitations on collection and foreclosure practices.

But that body of state consumer protection laws which applies to retail dealers in the first instance has a very significant indirect impact on banks in their capacities as assignees or holders of discounted dealer paper. By virtue of the widespread state abolition of holder in due course protec-


\(^1\) The FDIC study on which this article is based focused on the law and enforcement activity in seven states: Kansas; Massachusetts; New York; North Carolina; Texas; Utah; and Virginia. These jurisdictions proved to be broadly representative of state activity elsewhere. Subsequent references to state laws concentrate on these seven states.
tions,\textsuperscript{92} and even more by virtue of the FTC Holder Rule,\textsuperscript{93} banks as assignees hold dealer paper subject to all claims and defenses the consumer could assert against the original seller. Under the FTC Holder Rule Notice, for example, a consumer whose automobile turned out to be a total lemon might successfully recover from the bank all monthly payments made plus the amount of the down payment and trade-in value.\textsuperscript{94}

Although the scope of the FTC Rule has not yet been tested in reported case law, it is virtually certain that the courts will read it as exposing assignee/holders to claims of statutory violations by the dealer — violations which could include usury, impermissible contract terms, disclosure inaccuracies, and the like. Indeed, this pattern of subjecting assignees to liability for statutory violations by assignors has already emerged under TIL,\textsuperscript{95} and there is no reason to doubt that the pattern will expand under the FTC Rule. Both consumer credit laws directly applicable to banks and those applicable primarily to retail dealers must be considered in order to measure the bank's potential exposure to liability, and both sets of laws are the proper concern of bank agency enforcement programs.

State laws applicable directly to small loan and consumer finance companies may also have an indirect impact on banks. For example, banks may ultimately hold consumer finance company paper through rediscount or as collateral for bank loans. Additionally, the operations of consumer finance companies as bank holding company subsidiaries are subject to Board examination powers, and unlawful small loan practices could, in theory, affect the safety and soundness of the corporately related bank.

3. Territorial Reach of State Laws

At a time when consumer credit transactions increasingly have multi-state contacts, banks and bank supervisors should be aware that the statutes of a particular state are not necessarily the controlling substantive law for a particular contract which is signed, performed, or litigated within the state. In classic creditor-debtor contract cases, the substantive law to be applied was that of the jurisdiction where the contract was executed or the law invoked by the parties in the contract instrument. A court would, therefore, enforce the contract if it was valid and enforceable in the state

\textsuperscript{92} See Rohner, \textit{Holder in Due Course in Consumer Transactions: Requiem, Revival or Reformation}, 60 \textit{Cornell L. Rev.} 503 (1975).

\textsuperscript{93} See note 44 & accompanying text \textit{supra}.


where it was executed. Many states still have statutes, particularly in the small loan area, which permit enforcement of a contract against a resident debtor provided the contract is valid under the law of the state where it was signed.

Under traditional doctrine, therefore, a contract would be considered valid and enforceable in a given state even though the interest rate or other charges would be usurious under that state's own law. This rule provided reassurance to creditors who could safely contract on the basis of their home-state law without reference to or concern for where the consumer debtor lived or where the contract was solicited or performed.

Recently, however, some states, including those which have adopted the UCCC, have enacted legislation to protect resident consumers from overcharging or other prohibited practices by out-of-state creditors. In some instances this has been done by strict licensing statutes covering creditors who merely solicit within the state without maintaining an office there. For example, in two recent cases, Maryland and New York courts refused to enforce contracts between resident debtors and out-of-state finance companies for failure of those companies to maintain or obtain state lender's licenses.

Other states provide that contracts executed in another state by a resident consumer are valid and enforceable only if the charges and creditor's rights are valid under the consumer's home-state law. Most of these statutes expressly apply local law to creditors who solicit business within the state through advertising and catalogs. In a recent series of cases involving Aldens, Inc., a Chicago-based mail-order firm, the statutes of Oklahoma, Wisconsin, and Pennsylvania were upheld by three separate federal courts of appeal.

In all three cases, Aldens' contract conformed to Illinois law, the loca-
tion of the company's only office. The rate of interest, however, was usurious under Oklahoma, Wisconsin, and Pennsylvania law, respectively. Statutes in all three of those states specifically applied local law to mail-order solicitations within the state, and in all cases the contracts were signed by the consumers in their respective home states. The courts found that the state interest in protecting resident consumers by limiting the cost of credit outweighed any constitutional due process, commerce clause, and full faith and credit objections. Each decision affirmed the power of state legislatures to regulate those charges with respect to resident consumers.

The decisions in these cases may have significant ramifications for banks whenever they operate across state lines. It is possible for courts of the consumer's jurisdiction to apply these holdings to invalidate or modify contracts which provide the creditor with greater rights than are permitted under the law of the consumer's home state. There are also implications for the examination and enforcement process. To be absolutely thorough, an examiner would need to check separately the accounts of non-resident customers for compliance with the laws of neighboring states. Banks would need to institute monitoring programs to assure that loan officers know and apply the appropriate state law.

4. Allocation of Enforcement Responsibility Within States

Within any given state, there is some fragmentation of regulatory and enforcement responsibility comparable to that at the federal level. Although the state bank supervisor has primary enforcement authority for consumer credit laws in all seven states, other offices shared enforcement responsibilities in some cases. In New York, for example, a separate Commission on Human Rights has regulatory authority in the credit discrimination area. In Kansas, a Commission on Civil Rights enforces the anti-discrimination laws, and in Massachusetts, a Commission Against Discrimination has primary regulation-writing authority.

In addition, the state attorney general may be responsible for "interpreting" state laws through published opinions. More significantly, the state

103. For example, the decisions in the Aldens cases will affect banks when they operate as purchasers of dealer paper, as credit card issuers through out-of-state loan production offices, or through regional advertising campaigns.
104. See A PROFILE OF STATE-CHARTERED BANKING 19-21 (Conf. of State Banking Supervisors 1977 ed.). For a listing of the seven states referred to in the text, see note 91 supra.
attorney general may be authorized to initiate prosecutions for violations of various consumer protection laws applicable to banks. In Massachusetts, when the bank commissioner's attempts at administrative settlement of alleged violations fail, the commissioner's established practice is to refer those cases to the attorney general for suit.108 Similarly, a Texas court recently held that the state's "Deceptive Trade Practices - Consumer Protection Act,"109 enforced by a division of the state attorney general's office, is fully applicable to banks.110

The separation of regulatory and enforcement powers within specific states has not generated the degree of difficulty that the separation of agency powers has produced at the federal level partly because many state bank supervisors have responsibility for other creditors in addition to banks.111 This combined structure tends to minimize interagency friction since a single official oversees the entire operation.112

C. Federal-State Friction Points

1. Preemption of State Laws

The existence of a large and growing body of federal consumer credit laws, juxtaposed on the traditionally near-exclusive regulatory role of the states, presents a question of fundamental and profound importance: to what extent do these federal laws and regulations occupy the field and preclude or displace state legislation on the same subject matter? The question is intensely political, for it encapsulates the continuing debate over the proper roles for federal and state governments. It is also an intensely pragmatic question to consumers who want the strongest protections, to industry members who must sort out their compliance burdens from the mass of federal and state laws, and to supervisory agencies and courts which must eventually distinguish the controlling rules.

With the rapid growth of consumer laws over the past decade at both the


111. Of the seven states in this study, the bank commissioner in New York, Massachusetts, North Carolina, Virginia, and Utah, also supervised finance companies, thrift institutions, and other creditors.

112. Three of the seven state bank supervisors, those in Massachusetts, North Carolina, and Virginia, operated within a larger governmental entity, thus providing an additional level of administrative coordination.
federal and state levels, the preemptive effect of federal laws on state enactments should be clearly delineated. Unfortunately, most federal laws contain very limited preemption rules permitting much state law on the same general subject to coexist in an uneasy and ambiguous relationship.\(^\text{113}\)

While there are minor variations in language, the basic preemption approach is the same. Federal law preempts state law only to the extent that state law is inconsistent with any provision of the federal law,\(^\text{114}\) and the chief enforcing agency is authorized to determine whether inconsistencies exist.\(^\text{115}\)

Several federal statutes provide that the enforcement agency cannot determine that state law is inconsistent if the state law "gives greater protection to the consumer."\(^\text{116}\) This is troublesome because it may require difficult judgment calls about what affords consumers greater protection.\(^\text{117}\)

States, therefore, remain free to enact legislation very similar to, and indeed duplicative, of federal law. They are free to embellish requirements of the federal statutes, and, by virtue of the "more protective" limitations, are almost invited to try to outdo Congress in consumer protection.

The regulations implementing these various preemption provisions differ somewhat, but the basic policy remains intact. For example, state

\(^{113}\) See id. \(\S 1691d(f)\) (Board determines whether state law is inconsistent with ECOA).

\(^{114}\) See id. \(\S 1691d(f)\) (Board determines whether state law is inconsistent with ECOA).

\(^{115}\) See id. \(\S 1691d(f)\) (Board determines whether state law is inconsistent with ECOA).
credit disclosure laws, otherwise similar to TIL, are inconsistent and are preempted to the extent they require creditors "to make disclosures or take actions different from the requirements of this part with respect to form, content, terminology, or time of delivery." For chapters four and five of TIL, however, the basic test is whether the creditor can comply with the state law without violating Regulation Z.

The Federal Reserve Board staff has issued only a handful of letters or interpretations on the TIL preemption rules. This may indicate that the general standards of consistency stated in the regulation are not workable. At the same time, the Board’s Regulation Z temporizes on inconsistent state disclosure requirements by permitting such disclosures so long as they are clearly segregated from those required under federal law. This anomalous permission to make preempted state disclosures was apparently thought to be necessary so that creditors would not be barred from using state law terminology necessary to create binding contracts. Under ECOA, the revised Regulation B lists five separate criteria for consistency of state law with federal and further provides that determinations about preemption of state law will be made only by formal Board interpretations. The Board has issued three such interpretations to date.

121. See 12 C.F.R. § 226.6(c)(1)-(2) (1979). Using this provision to avoid violations of either state or federal law may cause even greater trouble for the creditor. See, e.g., Mason v. General Fin. Corp., 542 F.2d 1226 (4th Cir. 1976).
122. See 12 C.F.R. § 202.11(a)-(b) (1979). A state law is deemed inconsistent if it meets one of the following five criteria:
   (i) requires or permits a practice or act prohibited by the Act [ECOA] or this Part;
   (ii) prohibits the individual extension of consumer credit to both parties to a marriage if each spouse individually and voluntarily applies for such credit;
   (iii) prohibits inquiries or collection of data required to comply with the Act or this Part;
   (iv) prohibits asking age or considering age in a demonstrably and statistically sound, empirically derived credit system, to determine a pertinent element of credit worthiness, or to favor an elderly applicant; or
   (v) prohibits inquiries necessary to establish or administer a special purpose program as defined by section 202.8.
In light of this limited preemption approach and the few Board interpretations or rulings on preemption questions, state and federal laws on the same general subject maintain an uneasy coexistence. Where state and federal laws genuinely overlap or where state law is not preempted because of its more protective nature, there may be enforcement inefficiencies. Either both federal and state officials will supervise compliance with their respective statutes, thus largely duplicating each other's efforts, or one agency will defer to what it perhaps mistakenly believes is adequate supervision of that general area by the other.\textsuperscript{124}

The question of preemption of state consumer laws has been rehashed recently in the context of the Senate-passed Truth in Lending Simplification and Reform Act.\textsuperscript{125} Industry generally would prefer strong preemption provisions in federal law, that is, more complete displacement of similar state laws. Even the industry, however, recognizes the difficulty of totally preempting state laws on the disclosure of information in consumer credit agreements. At times, the use of certain terminology or descriptions is necessary as a matter of state law in order to create a binding contract or to conform to state usury laws. Here, complete preemption would put the creditors automatically in violation of state law or leave them without enforceable contracts. At the other extreme, recognizing the inevitable political compromises that go into federal laws, consumer representatives tend to prefer the present limited preemption approach which enables individual states to continue to act on perceived abuses.

The problem of preemption ultimately becomes one of line drawing. Assuming the states are to continue to have some lawmaking function in the consumer area, they should be free to legislate in areas untouched by federal law or touched by federal law in only a very limited way. It is difficult, however, to justify altogether duplicative federal and state laws or laws which are substantially the same but for technical, procedural, or semantic variations. Given the current federal dominance in this lawmaking

\textsuperscript{124} A further aspect of the preemption problem not directly related to federal or state agency enforcement, is whether an affected consumer might recover twice for the same violation, one under the federal statute and one under state law. Such a result is apparently possible under TIL but is expressly prohibited under ECOA. \textit{See} 15 U.S.C. § 1691d(e) (1976).

\textsuperscript{125} Section 9 of the Truth in Lending Simplification and Reform Act, S. 108, 96th Cong., 1st Sess. § 9 (1979), would require the Board, upon its own motion or upon the request of a creditor, state, or interested party, to make essentially line-by-line analyses of state disclosure laws to determine whether they are preempted. If so, creditors would be barred from using the preempted disclosure law and would incur no liability under state law for a good faith failure to use a term or form that is inconsistent with federal law.
arena, the only realistic solution is the development of stronger preemption rules placing a greater burden on the states to justify the applicability of local law to aspects of consumer transactions within the scope of the federal regulations.\(^{126}\)

2. **State Law Exemptions**

The reverse of the preemption idea is the notion that states may seek specific "exemptions" from otherwise applicable federal laws if they have equivalent laws of their own. This technique has the potential utility of avoiding duplication in applicable law and also accords the exempted state a measure of autonomy in its regulation and enforcement of consumer protection laws. Several of the federal laws specifically permit states to apply to the Board for an exemption from the federal law,\(^{127}\) which the Board must grant on a showing of substantially similar state law and adequate provision for state-level enforcement. Where exemptions are granted, the federal law no longer applies, and the parallel state law provisions are the controlling rules. Thus, exemptions amount to a substitution of state law and state enforcement for federal law and federal enforcement—a kind of reverse preemption.

Presently, only a handful of exemptions have been granted by the Board.\(^{128}\) The small number of exemptions is undoubtedly due to the con-


128. The only exemptions granted have been under TIL and HMDA. Maine, Massachusetts, Oklahoma, Connecticut, and Wyoming have been exempted from TIL, see Regulation Z, Supp. III, 12 C.F.R. § 226.55 (1979). Idaho was the only state whose application was formally denied. Congress' apparent hope that states would generally seek TIL exemptions in order to apply and enforce local law has not materialized.

The pattern of exemptions under HMDA has been somewhat different. HMDA requires banks to assemble annual data on the location of their residential mortgage portfolios. Comparable state enactments are usually part of a broad state anti-redlining law containing substantive provisions beyond the statistical data gathering requirements of HMDA. The states, therefore, have more reason to seek HMDA exemptions so as to be able to enforce their overall state law as an integrated whole. California, Illinois, Massachusetts, New York, see 41 Fed. Reg. 55,581 (1976), New Jersey, see 43 Fed. Reg. 7,476 (1978), and Connecticut, see 43 Fed. Reg. 35,394 (1978), have received exemptions. Each has certain limitations and conditions; all are limited to state chartered institutions. Illinois' exemption, however, has
straints and burdens involved in such a move. In the case of TIL, for instance, the exemption rules insist that the state enact and maintain rules virtually identical to TIL, to Regulation Z as periodically amended, and to prevailing Board interpretations. In addition, the state must assume the burden of enforcement otherwise borne by federal agencies. This can be a substantial undertaking, as is demonstrated by the commitment of resources in Massachusetts which has a TIL exemption. It is therefore likely that states generally lack interest in seeking exemptions because they receive little practical benefit.

The exemption mechanism, as presently constituted, is little more than a states-rights gesture. It may contribute to avoiding duplicative state and federal laws, for absent the exemptions those states might well have enacted parallel but separate state laws. However, this consideration is counterbalanced by other less desirable effects. There is no condition that the grant of an exemption in any way improve the level of consumer protection — only that the state law be "substantially similar" with "adequate" state enforcement. The adequacy of state supervisory programs is gauged only at the time the exemption is sought and apparently does not take into account any dislocation of state resources that may be required to handle the new enforcement responsibility. It also increases enforcement fragmentation, for, other than what may be disclosed in an annual state report to the Board, there is no coordination between the federal agencies which enforce the law in most states and the bank supervisors who enforce it in the "exempt" states. There is no provision for real inducements to states — through technical assistance or other aid — to assume an active, aggressive posture on consumer enforcement.

3. The Special Problems of the Applicability of State Laws to National Banks
   a. Generally

Although banks holding state charters are clearly subject to the legislative power of the states issuing those charters, the power of state legislatures to regulate the conduct of federally chartered banks is curtailed by

been annulled by the Board because of the state supreme court's declaration that the Illinois law was unconstitutional. See 43 Fed. Reg. 35,100 (1978). Under TIL, the exemptions granted by the Board exclude federally chartered institutions from the scope of the exemption because the Board cannot find the necessary assurance of state enforcement so long as OCC has exclusive visitatorial powers with respect to national banks. Additionally, an aggrieved customer in an exempt state has the right to bring a damage suit in federal court. See Ives v. W.T. Grant Co., 552 F.2d 749 (2d Cir. 1975).

the National Bank Act\textsuperscript{131} and its preemption of state laws through the supremacy clause of the United States Constitution.\textsuperscript{132} It is well established that the states cannot exercise control over national banks except insofar as Congress permits.\textsuperscript{133} Attempts by states to define the duties of national banks or to control the conduct of their affairs are deemed void not only when the state laws expressly conflict with the National Bank Act but also whenever the state laws frustrate the purposes of the federal act or "impair the efficiency" of national banks to discharge their charter functions.\textsuperscript{134}

This broad preemption arises out of the uniquely federal nature of national banks, which are both chartered and regulated by federal authority. The displacement of state laws which flows from their status as "federal instrumentalities," is distinguished from the state law preemption built into substantive federal consumer credit laws like TIL. The latter preempts state laws in certain circumstances by virtue of the supremacy of the CCPA on matters of credit disclosure. National banks may separately avoid the burden of state law under the aegis of the National Bank Act.

While it is therefore true that national banks may not be subjected to all the vagaries of state consumer protection laws, national banks do not operate wholly independent of state laws. The National Bank Act does not contain substantive provisions comparable to the mass of state statutory and common law rules on contract formation, acquisition, and transfer of property, and the right to sue and be sued on obligations. As the Supreme Court has noted in \textit{McClellan v. Chipman}:

\textsuperscript{135}

National banks are subject to the laws of the State, and are governed in their daily course of business far more by the laws of the State than of the nation. It is only when the state law incapacitates the banks from discharging their duties to the government that it becomes unconstitutional.\textsuperscript{136}

The distinction then is between state laws which unduly interfere with the operations of national banks as such and those state laws which other-

\begin{itemize}
  \item \textsuperscript{131} Act of June 3, 1864, ch. 106, \S 5, 13 Stat. 99 (codified at 12 U.S.C. \S\S 21-215b (1976)).
  \item \textsuperscript{132} U.S. Const., art. VI, cl. 2.
  \item \textsuperscript{135} 164 U.S. 347 (1896).
  \item \textsuperscript{136} Id. at 356 (quoting National Bank v. Commonwealth, 76 U.S. (9 Wall.) 355 (1869)).
\end{itemize}
wise affect the bank’s transactions and operations. The mere fact that state law may create an inconvenience for the national bank would not result in its preemption. Thus state escheat laws, state check collection rules, and state laws requiring national banks to post a bond subjecting their assets to a lien as a condition to receiving deposits of state funds have been applied to national banks. Of particular significance is the Court’s recognition that state law may impose affirmative reporting or disclosure duties on national banks where the information would be used to obtain compliance with other aspects of the state law. In Anderson National Bank v. Luckett, for example, the Supreme Court approved the application of state escheat laws to national banks and added the observation that the state “may . . . require the banks to file reports of inactive accounts, as the [state] statute directs.” The extent to which this kind of reporting requirement can be analogized to data on state consumer credit law compliance is unclear, but the Court does seem to have indicated that national banks may be required to aid in the enforcement of applicable state laws. There would appear to be no reason why most current state consumer credit laws should not apply to national banks under these ground rules, and the OCC has acknowledged as much in recent opinion letters. State laws restricting creditor remedies, requiring a certain contract format, limiting security interests or deficiency judgments, or restraining collection practices, for example, would seem to be equally applicable to national banks as to other creditors.

The general applicability of state consumer credit laws to national banks has obvious ramifications for the compliance and enforcement activities of the OCC. On one side, the FISA would seem clearly to authorize enforcement proceedings by the Comptroller based on violations of state laws and perhaps to require such proceedings where the state law violations amount to unsafe or unsound practices. On the other side is the

137. Roth v. Delano, 338 U.S. 226 (1949); Alaska v. First Nat’l Bank, 22 F.2d 377 (9th Cir. 1927).
139. Lewis v. Fidelity & Deposit Co., 292 U.S. 559 (1934).
140. 321 U.S. 233 (1944).
141. Id. at 252-53.
142. The notion that national banks are bound by state law reporting requirements goes back as far as Waite v. Dowley, 94 U.S. 527 (1876). As recently as 1976, however, the OCC advised national banks that they did not have to comply with the reporting provisions of the Massachusetts interest-on-escrow accounts statute. See Letter from John E. Shockey, Acting Chief Counsel, to Charles E. White, Regional Counsel (July 14, 1976).
143. See, e.g., Letter from John E. Shockey, supra note 142.
145. See notes 67-69 and accompanying text supra.
question whether, when state laws are applicable to national banks, the Comptroller’s visitorial and enforcement authority exclude any enforcement role by state officials. Unless the Comptroller, in fact, examines for state law compliance, or permits state officials to do so, a vacuum is created in which there is no administrative enforcement of those state laws.  

b. Interest Rates

(i) “Most Favored Lender”

One aspect of national bank participation in consumer credit transactions controlled more exclusively by the National Bank Act is the question of the maximum permissible finance charge, or interest rate, the bank may impose. Section 85 of the National Bank Act explicitly provides that national banks may charge:

[i]nterest at the rate allowed by the laws of the State . . . where the bank is located . . ., and no more, except that where by the laws of any State a different rate is limited for banks organized under State laws, the rate so limited shall be allowed for associations organized or existing in any such State . . . .

This terse provision has been amplified both in regulations of the OCC and in litigated cases.

The first portion of this statutory language, permitting national banks to use the rate of the state where it is located, reflects what has been called “most favored lender” status for those banks. National associations may charge the highest rate permitted any class of lender in the state and are not tied to the rate permitted competing state banks. The ostensible purpose for this preferred position for national banks is twofold: first, to assure that state legislatures cannot discriminate against national banks and favor state chartered institutions with respect to rates; and second, to assure national banks “competitive equality” with other lenders in the state.

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146. This was the burden of criticism directed at OCC by the Senate Banking Committee following oversight hearings in 1976. See S. Rep. No. 1388, 94th Cong., 2d Sess. (1976).
148. 12 C.F.R. § 7.7310 (1979). This regulation clearly indicates the extent of the OCC’s favoritism towards national banks: “For example, a national bank may lawfully charge the highest rate permitted to be charged by a state-licensed small loan company or morris plan bank, without being so licensed.” Id.
149. See, e.g., Acker v. Provident Nat'l Bank, 512 F.2d 729 (3d Cir. 1975) (national bank permitted to charge 15% interest under the installment sales law for credit card plans rather than 12% maximum rate for installment loans); Hiatt v. San Francisco Nat'l Bank, 361 F.2d 504 (9th Cir. 1966), cert. denied, 385 U.S. 748 (1967) (national bank in California could collect interest in excess of the 10% per annum maximum permissible to most lenders under California law); Northway Lanes v. Huckley Union Nat'l Bank & Trust Co., 334 F. Supp. 723 (W.D. Mich. 1971), aff'd, 464 F.2d 855 (6th Cir. 1972) (national bank permitted to charge highest rate allowed to state licensed savings and loan).
in the event state banks are disadvantaged or disfavored under the state's rate structure.

The strength of this most favored lender policy is underscored in several recent cases affirming the right of national banks to choose rates available to non-bank lenders. In United Missouri Bank v. Danforth,\textsuperscript{150} for example, the court approved the practice of national banks using, in their bank card plans, the rate permitted small loan companies in Missouri despite an explicit state law limiting state banks to a lower rate and despite the fact that no small loan company actually offered revolving credit similar to the banks' credit cards.\textsuperscript{151}

The availability of the highest state rate may not be an unqualified license for a national bank to charge the highest rate that local lenders may charge borrowers. The national bank must take the state rate as it exists and as it may be limited to certain classes of transactions. Thus, in Deak National Bank v. Bond,\textsuperscript{152} a New York court refused to allow a national bank on a loan for more than $20,000 to charge the rates permitted certain licensees for loans under $2,500. Similarly, in First National Bank v. Nowlin,\textsuperscript{153} the Eighth Circuit rejected the bank's contention that it could use the numerical rate permitted by state law but disregard the state's ban on discount computation of that rate. The gist of this holding is that, within its state of "location," a national bank may take advantage of the highest effective rate permitted to any state lender for particular classes of transactions.

An extension of the holding in Nowlin, therefore, would seem to require a national bank to use state law rules regarding what items must be included in the finance charge, as well as state law rules on mathematical computation methods. A national bank in a UCCC state, for example, could not impose a service charge or similar fee on top of the maximum statutory rate. Nowlin suggests that when national banks purchase dealer paper, the maximum rate permitted is that set by state law\textsuperscript{154} since the initial credit extension was from the dealer to the customer.\textsuperscript{155}


\textsuperscript{151} United Missouri Bank v. Danforth, 394 F. Supp. at 784.

\textsuperscript{152} 89 Misc. 2d 95, 390 N.Y.S.2d 771 (1976).

\textsuperscript{153} 509 F.2d 872 (8th Cir. 1975).

\textsuperscript{154} \textit{See also} City Nat'l Bank v. Brown, 251 Ark. 33, 471 S.W.2d 347 (1971) (installment contract between buyer and car dealer assigned to national bank).

\textsuperscript{155} The holding in Nowlin, however, does not necessarily represent the controlling view. The Nowlin court had to finesse Evans v. National Bank, 251 U.S. 108 (1919), which had approved the traditional practice of discounting short term loans at the maximum state
(ii) Interstate Transactions

With the proliferation of interstate banking activities, especially through credit card plans, it was inevitable that questions should arise about the rates permitted national banks outside their home states. Must the bank charge the rates permitted in its home state, or may it impose the higher charge authorized in the consumer's locale? May it charge its home-state rates where there are lower limits in the consumer's domicile, or must it charge the rates in the consumer's state? There has been a recent flurry of litigation on these questions, and in 1978, the Supreme Court in *Marquette National Bank v. First of Omaha Service Corp.*,\(^{156}\) permitted a Nebraska national bank to impose the higher Nebraska rates on its Minnesota cardholders. Additionally, in *Fisher v. National Bank of Chicago*,\(^{157}\) and *Fisher v. National Bank of Omaha*,\(^{158}\) the Seventh and Eighth Circuits concluded that a national bank located in one state may charge its home-state rates to customers living elsewhere despite lower rate limits in those customers' jurisdictions. *Meadowbrook National Bank v. Recile*\(^{159}\) seems to be the only court opinion holding that national banks are bound by the rates in the debtor's domicile.\(^{160}\)

The Supreme Court's decision in *Marquette National Bank* is instructive on the conflicting contentions and policies. The Court concluded that, by virtue of its "location" in Nebraska, First of Omaha was entitled under section 85 of the National Bank Act to charge Nebraska rates to its credit card customers wherever those customers may reside.\(^{161}\) The Court reached this conclusion despite the fact that First of Omaha solicited and serviced accounts in Minnesota through local agents and despite the fact that Minnesota had enacted a statute specifically subjecting out-of-state

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\(^{157}\) 538 F.2d 1284 (7th Cir. 1976), cert. denied, 429 U.S. 1062 (1977).

\(^{158}\) 548 F.2d 255 (8th Cir. 1977).


\(^{160}\) The court's questionable holding was that §85 of the National Bank Act fixed the maximum interest charge only with respect to loans made in the state where the national bank was located. According to the court, state law, not the National Bank Act, controlled the maximum interest charge for loans "made" elsewhere. *Id.* at 75.

card issuers to Minnesota rates under those circumstances. The Court's decision, therefore, is an explicit application of the federal supremacy doctrine in the face of contrary state policy.

The holding in *Marquette* raises numerous issues of consumer protection, states' rights, and federal banking policy — issues whose full exploration is beyond the scope of this article. Although it enhances the independence of federally chartered banks from state regulations, it arguably exalts national banks over all other state lenders in a way that creates inequitable competitive advantages for them. It quite clearly frustrates efforts by states to control the rates imposed on their citizens. The Court itself acknowledged this consequence but suggested that any remedial action should be done by Congress rather than by judicial rewriting of the National Bank Act. It is not surprising that at least one bill has already been introduced to reverse the *Marquette* decision.

4. Enforcement Authority of State Officials Over National Banks

A corollary to the question whether state substantive laws apply to national banks is whether state bank supervisors have authority to exercise "visitorial" (i.e., bank examination) powers or other enforcement techniques against national banks. State bank supervisors historically have been excluded from any enforcement role against national banks and other federally chartered institutions. But sometimes-caustic debate has erupted in recent years over whether that limitation on state enforcement powers should continue.

The National Commission on Consumer Finance, in 1972, reviewed the exclusive enforcement powers of the federal chartering agencies and recommended "that federal law be expressly changed to authorize state officials to examine federally chartered institutions for the limited purpose of enforcing state consumer laws." Bank supervisors in several states have objected strongly to the combination of lax enforcement of state laws by federal officials and denial of enforcement access to state officials.

166. NCCF REPORT, supra note 3, at 60.
These objections have come most vigorously from states with exemptions from the Federal Truth in Lending Act, but the objections have concerned other aspects of state laws as well.

The reasons why particular state bank supervisors should want enforcement access to federally chartered institutions are not altogether clear. Logically, an aggressive state agency would seek to insure equal application of all state laws to all credit granting institutions regardless of charter. On the other hand, the assumption of responsibility for supervision of federal institutions would place an immense burden on the enforcement resources in most state agencies, thus diluting their overall enforcement efforts. In Massachusetts, for example, national banks hold fifty-six percent of all the consumer obligations held by commercial banks. For the state bank commissioner to begin enforcing state laws against those national banks would either dilute its effectiveness by half or require doubling the expenditures now committed to commercial bank supervision. It may be, therefore, that some of the professed desire by state supervisors to undertake enforcement against federal institutions is a ploy to induce more vigorous efforts by the federal supervisory agency.

Although there has not been much recent litigation on the Comptroller's visitorial powers, OCC has vigorously denied access to state officials. OCC's unwillingness to authorize Massachusetts examiners to check national bank compliance with the state TIL law caught that state in a Catch-22 situation. Without OCC's authorization for state examiners to enter, the Board was not convinced that the state had "adequate provisions for enforcement," an essential criterion for an exemption from federal law. More recently, OCC has advised its regional counsel in New England that, although national banks there are subject to the Massachusetts interest-on-escrow-accounts law, they are not bound to supply the state banking commission with specified reports required under that law.

At the same time, the Comptroller's position has not been absolutely

168. For the raw data used to compile this 56% figure, see Assets and Liabilities, 1976 Report of Income Commercial & Mutual Savings Banks (FDIC, December 31, 1976).
169. This somewhat cynical view is apparently not true in Massachusetts, however, for the Commissioner there has pressed the Board to extend the state's TIL exemption to national banks. See Federal Bank Agency Enforcement of Truth in Lending Act, Hearings Before a Subcomm. of the House Comm. on Government Operations, 94th Cong., 2d Sess. 39 (1976) (testimony of Commissioner Greenwald). Most recently the Massachusetts commissioner obtained an agreement from the NCUA to permit state enforcement access to federally chartered credit unions within the state. An application to the Board to extend the Massachusetts TIL exemption to state institutions was promptly approved by the Board. See 43 Fed. Reg. 49,973 (1978).
170. Letter from John E. Shockey, supra note 142, at 4-5.
intransigent with respect to accommodating state desires to enforce state laws. When the Pennsylvania Insurance Department recently expressed the desire to verify national bank compliance with insurance rebate laws, OCC and the state officials were able to develop a collaborative arrangement in which federal bank examiners would utilize state forms and state training sessions but conduct the compliance visitations themselves.171 Similar cooperative arrangements are underway in several other states.172

The source of the enforcement authority problem is the 115 year-old provision of the National Bank Act, which provides that the OCC has exclusive visitorial powers over national banks, except for those powers authorized by law, vested in the courts of justice or as exercised or directed by Congress.173 This right has been guarded by both the national banks and the OCC from its inception. Although there was some litigation concerning this authority in the years following its enactment, the early litigation did not involve challenges to the basic grant of authority; rather it concerned the interpretation of what constituted “visitorial” powers as well as what types of activity were covered by the stated exceptions.174

The rationale for the enactment of section 484 and its subsequent judicial interpretations is twofold. First, those cases expressed concern over the need for confidentiality with respect to bank records. Confidentiality is required not only to protect the rights of individual customers (and stockholders) but also to preserve the stability of the financial structure by maintaining public confidence in banks and the banking system. Second, it was believed that state supervision of national banks could impair the ability of national banks to perform the federal functions they were designed to serve.175

172. For example, national bank examiners in California check for compliance with a variety of state laws, using the checklist form “Examination Procedures-CA State Law.”
174. See First Nat’l Bank v. Hughes, 6 F. Supp. 737 (C.C.N.D. Ohio 1881) (court defined visitorial powers as those of inspection, supervision, regulation of business, or enforcement of laws or regulations; visitorial powers did not include compelling national bank by court order to disclose depositors and amounts to determine taxes owing). See also Guthrie v. Harkness, 199 U.S. 148 (1905) (used Hughes definition of visitorial powers to hold that National Bank Act did not deny shareholders common law right to inspect corporation’s books); Bank of America Nat’l Trust & Sav. Ass’n v. Douglas, 105 F.2d 100 (D.C. Cir. 1939) (supervisor of national bank was not exercising visitorial powers by furnishing the SEC, but not the public, with copies of examiners’ reports on bank under investigation); Cravens v. United States, 62 F.2d 261 (8th Cir.), cert. denied, 289 U.S. 733 (1932) (Justice Department agents’ presence during bank examination not exercise of visitorial powers).
175. See cases cited in note 174 supra.
A narrow construction has also been used to permit state officials to inspect records. In *Clovis National Bank v. Callaway*, the Supreme Court of New Mexico held that a state escheat statute permitting the state treasurer to demand bank records on abandoned property can constitutionally be applied to national banks, notwithstanding section 484. The court reasoned that when there is a "right to obtain information there must be a means of enforcing valid demands," and so long as the demands "are reasonable and do not interfere with the purpose of the bank’s creation, or impair or destroy its functioning and are not in conflict with some paramount federal law," then there can be no valid objection.

This reasoning, if extended, might justify permitting state banking officials, acting pursuant to a valid state consumer statute, to inspect the pertinent records of a national bank or at least to inspect the reports of those records made by OCC examiners. The reasons asserted for not permitting state banking officials access to national bank records — the need for confidentiality and noninterference with the bank's efficient operation — may not justify the absolute exclusion of the state banking officials. This is particularly true in the area of consumer credit where many of the consumer's protections derive from state laws and where the Comptroller has not shown an interest in examining broadly for fifty different sets of state law.

Unless section 484 was intended to deny certain citizens the equal protection of state laws depending on where they choose to do their banking, allowing state officials limited access to records in the consumer credit area for on- or off-premise inspection would not seem to be violative of the intent of section 484. So long as state officials must also maintain bank records in confidence, there is no reason to fear a confidentiality problem in regard to these records. Nor need there be any significant disruption of the operations of national banks. State examinations limited to checking compliance with specific state laws would add little burden to the banks beyond that involved in the OCC's own compliance exams.

In sum, the current stand-off between OCC and state officials with respect to enforcement access to national banks seems neither necessary nor desirable, especially at a time when OCC acknowledges the very limited scope of its review of state law compliance. If OCC were to demonstrate an ability to supervise all state law compliance, denial of state access might be justified either on the ground that state access would be unnecessarily

177. 69 N.M. at 131, 364 P.2d at 756.
duplicative and intrusive or on the ground that OCC simply did a better job. It is doubtful that either ground can be sustained at the present time.

III. ENFORCEMENT ISSUES ON THE HORIZON

Implicit in the prior discussion is that consumer protection in the banking area is not static; the momentum of the past ten years promises only to continue and to grow. In this process there will be both substantive and procedural innovations: substantive in that there will be new areas of federal and state lawmaker; procedural in the recognition of new enforcement needs and techniques. The direction of some of these trends is fairly clear; other areas of future activity can be perceived only dimly.

A. Noncredit Transactions

New and pending substantive laws and regulations are emerging in several areas, mostly at the federal level. For example, the passage of EFTA marks a major government intervention in the regulation of depositor services. It is likely that legislators and regulators in the years ahead will expand the federal web into other aspects of those services. One can visualize a Federal Truth in Savings law legislation requiring disclosure concerning automatic transfer services or even regarding disclosure and other protections for conventional checking account customers. Proposals concerning depositor services have already arisen in Congress and at the Board which is authorized by section 18(f) of the FTC Act to deal broadly with “unfair or deceptive” practices.

Similarly, in American Bankers Association v. Connell, the United States Court of Appeals for the District of Columbia declared NOW accounts, share draft plans, and similar interest-earning deposit account arrangements to be ultra vires for thrift institutions, credit unions, and banks, respectively. The decision has spurred both House and Senate banking committees to consider legislation authorizing those attractive customer services, and such authorizing legislation must be enacted by the end of 1979 if financial institutions are to continue offering those services.

B. Customer Informational Privacy

In the post-Watergate concern for protecting the confidentiality and privacy of personal records, several areas of legislative action have emerged. One is the protection of bank customer records from unwarranted access by governmental agencies, which is addressed in the Right to Financial Privacy Act of 1978 (RFPA). Under earlier legislation, banks were required to maintain records of customer transactions. It became commonplace for government agencies to obtain access to these records either informally or on the strength of routinely issued administrative subpoenas. Although bank customers asserted that they had the right to keep these records private to preserve constitutional due process and self-incrimination protections, the Supreme Court in *United States v. Miller* ruled that customer records were the property of the bank and not of the individual customer. The result was a flurry of legislative proposals to reverse that case and accord privacy protections to bank records, culminating in passage of the RFPA. More recently, President Carter has promised a series of legislative proposals concerning the protection of customer financial records from unwarranted dissemination in the private sector.

Another legislative battlefield will involve the FCRA which regulates the collection and dissemination of information about prospective applicants for credit, insurance, and employment. Its provisions require accurate procedures on the part of credit bureaus and other “consumer reporting agencies” in gathering and reporting consumer information, require notification to consumers when adverse action is premised on a consumer report, and establish certain rights for the consumer to learn the contents

187. In general, under RFPA, government agents may obtain access to bank customer records only on the customer's authorization, or judicial subpoena, or search warrant, or on the basis of a formal written request. In each case, the customer is notified, either before or after the records are sought, and has the opportunity to challenge the government's right to those records. Advance notification is not required if there is reason to believe it would result in flight from prosecution, tampering with evidence, intimidation of witnesses, or other disruption of an official investigation proceeding.
188. At this writing, the Administration's proposals have not been formally released but have been circulated for comment from interested parties. *See, e.g.*, [1979] C.B.A. REPORTS 14-16 (June 11, 1979).

of his or her file and to correct inaccuracies. Its primary application to banks, therefore, is in their capacity as credit grantors who use credit reports, or in their capacity as suppliers of information about their customers to credit bureaus or directly to other creditors.

The 1977 Report of the Privacy Protection Study Commission made extensive recommendations for strengthening the FCRA. Dominant among those recommendations was the imposition of a greater responsibility for accuracy on the suppliers of information. The recommendations of the Privacy Commission received no serious attention in the Ninety-fifth Congress but are reflected in President Carter's current privacy initiatives and will certainly receive support from Senator Proxmire, who has sought several times to amend the FCRA.

Extensive new legislation in the privacy area will do more than merely add to the quantum of the banking agencies' enforcement duties. Although compliance with the present FCRA can largely be determined by a review of documents, the impending expansion of bank customer privacy protection will require considerable sensitivity on the part of bank examiners and other agency personnel in evaluating "reasonable" procedures and "reasonable" care. In the area of FCRA, where there is some tension between the desires of the bank and its customer, agency personnel will need to orient themselves to the delicate balance between consumer privacy expectations and the institution's need-to-know.

C. "Simple English" Customer Contracts

One of the by-products of the movement toward TIL simplification has been a recognition of the often arcane and obstruse language commonly used in bank-customer agreements. Consumer advocates, for example, argue that TIL should be simplified not by reducing the amount of information disclosed but by rewriting those disclosures in direct and readily understandable language.

This notion has gained some momentum. The state of New York has passed a "Plain Language Act" applicable to all consumer installment con-
tracts effective November 1, 1978.196 Numerous other state legislatures have considered similar laws.197 The Truth in Lending Simplification bill which passed the Senate in 1979 would direct the Board to prepare model disclosure forms in “readily understandable language.”198 Several banks around the country have received publicity for themselves by instituting “simple English” credit contracts.199

The “simple English” requirement presents both regulatory and enforcement difficulties. Unless the appropriate federal or state regulatory agencies promulgate form contracts or disclosure statements which are universally adopted, the examiners and other enforcement personnel will have to grapple with an amorphous statutory standard. This could place an enormous burden on the examiners if they must become semanticists and lexicographers with respect to bank forms. Some alternative enforcement would almost certainly need to be derived, for example, by regional office staff rather than by field examiners.

If these laws become more commonplace at the state level, a new preemption problem will arise. If “simple English” terms were inconsistent with specified terminology under TIL or other federal legislation, the state law would have to give way. At the same time, the premise of these plain-language laws is that they afford the consumer more meaningful information and thus better protection, a criterion which Congress has indicated should not result in state law preemption.200 Thus, state enactment of “simple English” laws could put great pressure on Congress to “simplify” existing federal disclosure laws.

D. Alternative Mortgage Instruments (AMI’s)

In recent decades, home mortgage financing in this country has utilized

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199. For example, the National Bank of Washington’s “common language” consumer loan note was reported in Washington Credit Letter, Sept. 5, 1977, at 10. Simplified forms used by Citibank in New York were discussed in the 1977 hearings in the Truth in Lending Simplification bill. See Simplify and Reform the Truth in Lending Act, Hearings on S.1312, S. 1301, and S. 1653 Before the Subcomm. on Consumer Affairs of the Senate Comm. on Banking, Housing and Urban Affairs, 95th Cong., 1st Sess. (1977).
200. Many of the recent additions to federal consumer legislation contain language similar to that found in FCBA. See 15 U.S.C. § 1666j(a) (1976) (“Board may not determine that any state law is inconsistent with any provision of this part if the Board determines that such law gives greater protection to the consumer”).
almost exclusively the fixed amortization mortgage, in which the duration, rate, and periodic payments are set at the outset and do not change during the term of the loan. The current housing shortage and prevailing high interest rates have generated considerable interest in alternative forms of home mortgages. These include variable rate mortgages, where the interest rate may be adjusted from time to time, graduated payment mortgages, where the monthly payment increases over time, and reverse annuity mortgages, where a homeowner with a large equity draws out that equity in periodic increments, increasing the loan obligation over time. Variations of these have also been discussed.\(^\text{201}\)

Some states, notably California, have approved some of these alternative mortgages for state chartered lenders,\(^\text{202}\) and in 1979 the FHLBB approved AMI's for federally chartered savings and loans\(^\text{203}\) despite objections from some members of Congress.

The merits and dangers of these novel mortgage forms continue to be debated,\(^\text{204}\) but it seems likely that experiments with them will continue. While these recast mortgage arrangements are controversial for their impact on housing credit, they would not appear to present major new enforcement problems. Determining compliance with applicable limitations on the structure or disclosure of these mortgages should not be substantially different from reviewing compliance with present usury, TIL, and similar laws.\(^\text{205}\) Additionally, these mortgage alternatives could produce ECOA or FHA violations if they were used as subterfuges to impose more onerous terms on protected classes of applicants.

\section*{E. Access to Credit; Redlining}

Although substantial strides have been made in legislation attacking patterns of credit discrimination, particularly in the housing credit area, some further legislation and regulation lies ahead.

The four major federal financial institution supervisory agencies have promulgated regulations to implement the CRA.\(^\text{206}\) That legislation directs each supervisory agency to take into account the institution's record

\begin{itemize}
\item \textit{201.} For further description of these forms of variable rate mortgages, see 43 Fed. Reg. 59,336 (1978), expanded in 44 Fed. Reg. 32,199 (1979).
\item \textit{202.} See CAL. CIV. CODE § 1916.5 (West Supp. 1979).
\item \textit{205.} See, e.g., Landers \& Chandler, \textit{The Truth in Lending Act and Variable Rate Mortgages and Balloon Notes}, ABF Res. J. 35 (1976).
\item \textit{206.} The regulations were published at 43 Fed. Reg. 47,144 (1978).
\end{itemize}
of serving community credit needs in passing on applications for charters, branches, and similar benefits. The regulations provide mechanisms through which the agencies can exercise that responsibility. Each institution must define its "local" and "entire" community, maintain a public file of CRA comments and publicly post a notice advising customers of their opportunities to file comments or examine the bank's CRA statement listing types of credit available and other pertinent information about the institution's efforts to meet community needs.

The regulations further state that each agency will assess the institution's record of performance in connection with its examination of that institution. Thus, front-line enforcement responsibility is placed with the bank examiners. This approach to implementing the CRA promises to add substantially to the enforcement duties of those examiners. Accordingly, the FDIC has projected greatly increased compliance expenditures for 1979, largely anticipating these CRA regulations.

These CRA regulations, of course, are not an isolated instance of increasing attention to assuring consumers' access to credit. Redlining — at least in the sense of racial redlining — already has been the target of several legislative measures. But there is emerging a broader concern about geographic redlining generally without necessary reference to its consequences for racial minorities. CRA, for example, addresses "community" needs without special focus on minority groups in those communities.

The Ninety-sixth Congress has before it bills to prohibit credit discrimination on the basis of geography (consumer's residence) and employment. Both Congress and the Board have expressed concern about the implications of statistically based credit-scoring systems, concerns that such systems may unfairly determine creditworthiness by class characteristics rather than by personal traits.

209. Id. at 47,145-46.
210. The FDIC predicted its enforcement costs in the Equal Lending — Fair Housing area would leap from $1,661,000 in 1978 to $3,910,000 in 1979, largely due to the added CRA responsibilities.
Much of the talk about redlining and discrimination is based on concern for protecting minority populations. But it is possible to perceive a more egalitarian sentiment in which every criterion used in the credit granting process will be subject to intense scrutiny for arbitrariness by the public and by supervisory agencies. Goals of assuring sources of credit to low-income individuals, regardless of race or ethnicity, of fostering urban redevelopment, or protecting small business or small farmers, can already be seen in the CRA regulations and may command increasing attention. Responsibility for policing such laws will impose potentially immense enforcement burdens on the banking agencies and will compel some drastic changes in the nature of enforcement strategies and tactics. There will be a sharper divergence of the consumer compliance function from the safety and soundness function which has presently dominated agency thinking.

IV. FEDERAL-STATE PROBLEMS IN THE FUTURE

The areas of imminent and future activity are almost all at the federal rather than state level. It is debatable whether the increasing dominance over the consumer credit field by Congress and the federal agencies is due to the activism of the federal legislators, to the relative conservatism of state legislators and regulators, or to the fact that the consumer credit market has become much more a national market whose participants include large chains of credit-granting retailers, consumer finance companies, and bankcard franchisees, and a highly mobile population. But it is clear that the mainstream of consumer regulation flows from Washington.

As noted above, that stream has tributaries other than Congress and the banking agencies. Most noticeable is the FTC. Within the next year, the FTC may issue three new trade regulation rules which will require parallel action from the Board affecting banks. One is the extension of the “Holder” Rule to creditors. With a parallel federal regulation for banks, those institutions will be subject to direct compliance actions for violations. A second is the “used car” rule which will affect banks in their capacities as repossessors. Even more significant is the FTC’s proposed “Credit Practices” Rule.214

Although some of the significance of this FTC activity lies in its de facto extension of FTC authority to banks, this activity also substantively affects the contracts of the parties in consumer credit transactions. It is not limited to disclosure as was TIL and other existing federal law. This substantive rulemaking by the FTC therefore has a more profound preemptive effect on state laws than has most of the present federal law. Consider, for

214. See notes 31-36 and accompanying text supra.
example, the existing FTC "Holder" Rule. While the FTC staff insists it does not formally preempt state laws on the rights of assignees, it reduces those laws to insignificance. In that setting, why should state officials or state bank examiners invest any time enforcing the technically applicable, but inconsequential, state requirements?

Couple this emerging federal dominance of substantive lawmaking with the expanding enforcement techniques of the federal agencies, and one can project an environment in which the consumer protection role of state legislatures and state bank supervisors will be minor, perhaps non-existent. Lost will be all initiative for state level responses to consumer problems, and the healthy tension that can spur both levels of government to better quality programs for consumer protection.

V. PRÉCIS TO PART II

A large part of the movement toward federal control of consumer credit regulation has already occurred, and cannot readily or politically be undone even if it were desirable. But it is important that the protection of consumers not become a totally monolithic enterprise. Thus, the second part of this article will evaluate the actual enforcement programs conducted by the federal and state banking agencies. It will also suggest adjustments to the rules on preemption and exemptions of state laws, and agency enforcement designed to define more sharply the respective areas of state and federal activity. While federal regulation and enforcement will inevitably predominate, the states should be free to (and encouraged to) respond to unique local problems and to utilize state enforcement resources where this will contribute to efficient, effective, and openly cooperative federal-state consumer protection programs.
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<tr>
<th>STATUTE</th>
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<th>REGULATION WRITING AUTHORITY</th>
<th>ASSIGNMENT OF AGENCY ENFORCEMENT</th>
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<tr>
<td>1. Consumer Credit Protection Act</td>
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<td>d. Title VI Fair Credit Reporting</td>
<td>15 U.S.C. §§ 1681-1681t (1976)</td>
<td>None</td>
<td>Same as TIL</td>
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<td>5. Fair Housing Act</td>
<td>42 U.S.C. §§ 3601-3619 (1976)</td>
<td>None</td>
<td>&quot;[All executive departments (and agencies)]&quot;</td>
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