

RECORD NO. 06-3132

**UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT**

IN RE OCWEN FEDERAL BANK FSB
MORTGAGE SERVICING LITIGATION

Interlocutory Appeal From
The United States District Court
For The Northern District of Illinois
Case No. 04-C-02714
MDL. No. 1604
The Honorable Charles R. Norgle, District Judge

**BRIEF OF AMICUS CURIAE
THE MORTGAGE BANKERS ASSOCIATION
IN SUPPORT OF APPELLANTS AND REVERSAL**

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Fed. R. App. P. 29(c), the undersigned counsel of record for *amicus curiae*, The Mortgage Bankers Association (“MBA”) certifies that: (a) MBA is an Illinois not-for-profit corporation; (b) MBA has no parent company; and (c) no publicly held company has a 10% or greater ownership interest in MBA. The general nature and purpose of MBA’s business, as a trade organization, is to represent the interests of the real estate finance industry on a variety of issues. Powell Goldstein, LLP is appearing on behalf of *amicus curiae* The Mortgage Bankers Association.

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IDENTITY OF AMICUS CURIAE

MBA is a trade association representing the real estate finance industry. MBA respectfully submits this amicus brief in support of Appellant, Ocwen Loan Servicing, LLC (“Ocwen”).¹

INTEREST OF AMICUS CURIAE

MBA is a national trade association representing the real estate finance industry. Headquartered in Washington D.C., the association works to ensure the continued strength of the nation’s residential, multifamily and commercial real estate markets, and to extend access to affordable housing to all Americans through the residential and multifamily real estate markets. MBA promotes fair and ethical lending practices and fosters excellence and technical know-how among real estate finance professionals through a wide range of educational programs and technical publications. Its membership of approximately 3,000 companies includes all elements of real estate finance: mortgage banking companies, mortgage brokers, commercial banks, thrift institutions, life insurance companies, investment banks, conduit lenders, real estate investment trusts and others in the mortgage lending field. The MBA wishes to ensure the continued strength of the real estate finance industry.

Due to the vital interest of federally-chartered savings associations and banks in the appropriate resolution of this matter, we welcome this opportunity to provide our legal analysis and to provide our views on the impact to the banking and home loan industry if the opinion of the court below is not reversed.

¹ Ocwen Loan Servicing, LLC is the successor-in-interest to Ocwen Federal Bank FSB, a federally-chartered savings association.

SOURCE OF AUTHORITY TO FILE

Counsel for all parties have consented to MBA filing this amicus brief, and therefore filing is appropriate pursuant to Rule 29(a), Federal Rules of Appellate Procedure.

STATEMENT OF ISSUE ON REVIEW

Whether, contrary to the decision below, the Home Owners Loan Act of 1933, 12 U.S.C. § 1461 (“HOLA”), and its implementing regulations, 12 C.F.R. Parts 500 through 591, preempt Plaintiffs’ state law claims challenging the mortgage servicing practices of, and loan-related fees allegedly assessed by, a federal savings association.

SUMMARY OF ARGUMENT

The court below ignored the extensive federal interests that preempt state regulation of federal savings institutions, applied an incorrect presumption to find that Plaintiffs' claims were not preempted by federal law, and misapplied the operative regulations promulgated by the Office of Thrift Supervision ("OTS") to reach that result. Not surprisingly, these errors compel reversal.

It is particularly appropriate to grant relief here given the devastating impact the decision below could have on literally thousands of federal savings institutions. In addition, because national banks operate under a virtually identical preemption regulation, an adverse court decision would have a similarly negative effect on thousands of national banks. This devastating effect would permeate the home loan industry and limit the availability of home loans. In addition, the lower court has opened the floodgates of litigation for disgruntled customers to bring a wide variety of state law claims against federal thrifts, a result which is directly inconsistent with express Congressional intent to subject these institutions to uniform federal regulatory requirements.

HOLA was enacted at the height of the Great Depression to address "congressional dissatisfaction with state law and practice in the financing of home construction." *Conference of Federal Savings and Loan Associations v. Stein*, 604 F.2d 1256, 1257 (9th Cir. 1979). The enactment of HOLA was followed quickly by the creation of the Federal Housing Administration in 1934, and by the launching of a federally-insured mortgage with standard features and standard underwriting criteria that could be purchased by another new entity, the federally-chartered Federal National Mortgage Association. These Congressional efforts of the 1930s to establish uniformity

in home mortgage lending -- through preemption, standard loan product, and a federally supported secondary market entity – are the cornerstones of the modern secondary mortgage market.

The secondary mortgage market operates primarily through mortgage securitization, which depends on standardization and uniformity in the loan origination and loan servicing process. Securitization attracts capital from all across the globe, helping to fund the U.S. mortgage market today. Without the preemption provided by federal law for thrifts and the resulting uniformity in lending and loan servicing practices, the securitization market would suffer and, with it, funding for mortgages, availability of home financing, and the Country's economy.

In enacting HOLA, Congress exercised its power to provide for federally-chartered savings associations and to authorize the Federal Home Loan Bank Board (the "FHLBB," subsequently replaced by OTS) to issue regulations providing for the organization, incorporation, examination, operation, and regulation of federal savings associations and federal savings banks (collectively, "federal thrifts"), "giving primary consideration of the best practices of thrift institutions in the United States." 12 U.S.C. § 1464(a). To provide for a uniform, federally-regulated thrift industry and thus to ensure that federal thrifts would not be subject to a "hodgepodge" of inconsistent state laws and regulations, Congress, exercising its powers by enacting HOLA, delegated to the FHLBB (now the OTS) plenary and exclusive authority to regulate the lending-related practices of federal thrifts and to preempt state laws affecting their operation. *See Eureka Fed. Sav. & Loan Ass'n v. Kidwell*, 672 F.Supp. 436, 439 (N.D. Cal. 1987) and *Fidelity Fed. Sav. & Loan Ass'n v. de la Cuesta*, 458 U.S. 141, 161-162 (1982).

Under its congressionally delegated authority, the OTS issued comprehensive regulations governing all aspects of federal thrifts' operations. One of these regulations, 12 C.F.R. § 560.2 ("Section 560.2"), makes clear that the OTS occupies the field of lending-related regulation for federal thrifts:

OTS hereby occupies the entire field of lending regulation for federal savings associations. OTS intends to give federal savings associations maximum flexibility to exercise their lending powers in accordance with a uniform scheme of regulation. Accordingly, federal savings associations may extend credit as authorized under federal law, including this part [560], without regard to state laws purporting to regulate or otherwise affect their credit activities.

12 C.F.R. § 560.2(a).

Given the extensive federal interests and regulatory scheme, as well as the express pronouncements of OTS, state laws are preempted by virtue of both field preemption and express preemption. Rather than recognize this principle, the lower court applied an erroneous presumption that state laws are not preempted. Although such a presumption may be valid in other circumstances, in the area of federal regulation of federal thrifts the *contrary presumption* applies – state laws are presumed *to be preempted*.

Moreover, the lower court compounded its error by misapplying Section 560.2 to conclude that Plaintiffs' claims were not preempted here. Section 560.2(b) provides "illustrative examples" of preempted state laws, including without limitation, the ability of a thrift to require or obtain private mortgage insurance, the terms of credit, late charges and other loan-related fees, escrow accounts, disclosure and advertising, and processing, origination and servicing of mortgages. 12 C.F.R. § 560.2(b). The regulation also permits state laws in certain limited categories to the extent "they only incidentally affect the lending operations" of the institution or "are otherwise consistent with the purposes of paragraph (a)." 12 C.F.R. § 560.2(c).

Plaintiffs attempt to recharacterize their claims as based on “contract and commercial law” and “tort law” so as to fall within two of the exceptions listed in Section 560.2(c) and outside of the preempted classes of laws. However, the OTS has made clear that, when considering whether a particular state law is preempted, the first question is whether the state law is among the specifically preempted laws listed in 12 C.F.R. § 560.2(b). Only if the state law in question is not listed in subparagraph (b) of Section 560.2, is it appropriate even to consider whether the state law in question might also be listed in subparagraph (c). 61 Fed. Reg. 50951, 50966-67 (Sept. 30, 1996).

When the district court considered the preemptive effect of HOLA and the OTS regulations, it erroneously reversed this framework and first considered whether Plaintiffs’ claims might be considered contract claims or tort claims. Such an approach ignores the fundamental aspect of OTS preemption: in those areas that fundamentally govern a savings association’s lending and loan servicing operations, state law is always preempted.

In addition, placing inappropriate emphasis on whether a state or plaintiff characterizes a particular law or claim as a “tort” or “contract” matter would allow these narrow preemption exceptions to swallow the rule. The charging of an excessive fee, an ambiguous disclosure, the mishandling of a loan customer’s payments – all could be characterized as “torts.” Clearly Congress and the OTS did not intend that someone could simply claim that he was “wronged,” and thus avoid preemption, especially when, as with Plaintiffs’ claims, the alleged “wrongs” all relate to the fundamental operations of a federal savings association.

In addition to being contrary to years of federal regulation and case law, the decision below needs to be reversed to avoid imposing a plethora of additional burdens on federally-chartered savings associations and national banks, in a manner directly contrary to the express federal regulatory framework. The lower court's apparent view that federal preemption can be circumvented through the simple recharacterization of a claim as involving a tort or a contract claim, when in fact the claims go to the fundamental operations of such federally-chartered institutions, should not be allowed to stand.

ARGUMENT

I. HOLA’S HISTORY AND ITS VITAL IMPORTANCE TO HOME OWNERSHIP AND THE HOME LENDING AND LOAN SERVICING INDUSTRY.

The federal statutory and regulatory framework at issue in this case compels the conclusion that Plaintiffs’ claims are preempted by state law and that the lower court incorrectly analyzed the issues and consequently reached the wrong decision. However, before we present our analysis of this legal question, we should first explain why federal preemption and the resulting uniformity of laws affecting lending and loan servicing by federal thrifts is so important.

For nearly 75 years, since the enactment of HOLA, federal thrifts have depended on federal preemption of state laws. In the last 30 years alone, the OTS and the FHLBB issued in the range of 300 formal opinions reaffirming preemption of state laws governing savings associations.²

HOLA was enacted at the height of the Great Depression to address “congressional dissatisfaction with state law and practice in the financing of home construction.” *Conference of Federal Savings and Loan Associations v. Stein*, 604 F.2d 1256, 1257 (9th Cir. 1979).

The enactment of HOLA was followed quickly in 1934 by the creation of the Federal Housing Administration (“FHA”). In addition to recognizing the need for federal preemption in home lending, Congress dealt with the collapse of the housing market by launching a federally-insured mortgage with standard features and standard underwriting criteria that could be purchased by another new entity, the federally-chartered Federal

² FHLBB and OTS preemption opinions are available on the FFIN-OTSL data base of WestLaw, using the term “preempt!” to conduct the search. This will retrieve 370 opinions and letters. There are more than 300 unique (not duplicated) preemption decisions.

National Mortgage Association.³ These efforts of the 1930s to establish uniformity in home mortgage lending -- through preemption, standard loan product, and a federally supported secondary market entity -- are the cornerstones of the modern secondary mortgage market, which operates now primarily through mortgage securitization.

Securitization thrives on standardization and uniformity – both in the loan origination process and the loan servicing process. Securitization attracts capital from all types of investors from across the globe into the U.S. mortgage market today because of the federal government’s continuing commitment to a strong secondary mortgage market. This commitment is evidenced by current policies supporting the continuation of preemption under HOLA; loan standardization through FHA, the Department of Veterans Affairs, and the Rural Housing Service; and the operation of government-sponsored enterprises, among other policies. These policies have successfully combated what commentators have referred to as “the parochialism of the mortgage.” K.G. Lore, *MORTGAGE-BACKED SECURITIES Developments and Trends in the Secondary Mortgage Market*, at 1-9 (WEST 2000).

[Before securitization,] the mortgage historically was not an appealing investment to the large or institutional investor who preferred Treasuries or federal guaranties or the certainties of the traditional blue chips. Mortgages, even when aggregated in large pools, initially were perceived as having lesser value than these other instruments. This negative view of mortgages in the investment market stemmed from the fact that mortgages were not only tied to a property, but also to a place. ***Mortgages were viewed as being riskier investments because they were regulated by local and state laws that vary from state to state***, and because an isolated downturn in a local economy or a natural disaster could affect the payments on mortgages or the underlying property itself.

Id. (emphasis added).

³ This entity is a direct ancestor of today’s government-sponsored enterprise (“GSE”), Fannie Mae. Freddie Mac was created in 1970 to provide a secondary market outlet to thrifts. Its charter was expanded in the 1980s to accept loans from non-supervised institutions. Today, the GSEs each buy conventional mortgage loans meeting statutory criteria from all types of lenders.

Likewise, without the uniformity provided through federal preemption, loan servicers would be burdened by a multitude of varying state laws and documentation practices. This in turn would undermine the secondary market for home loans, reducing available capital for lending, and reducing the ability of all Americans to finance the purchase of a home. Secondary market players would be required to undertake extensive, and costly, due diligence analysis, reach detailed conclusions relating to specific loan originations as part of an expanded due diligence process, and implement costly operating systems to comply with varying laws. The increased costs and operational burdens would lead directly to higher rates and fees on loan products. In such an environment, secondary market operations would be in disarray as questions of compliance and enforceability would drown efficient flows of mortgage capital.

Since the early 1970s when mortgage-backed securities (“MBS”) were first issued, the market has grown tremendously. This development can be seen indirectly through the number of mortgage loans purchased by participants in the secondary mortgage market and directly through the increase in the number and value of mortgage loans securitized in the single-family and the multi-family/commercial mortgage markets.

Based on data collected on mortgage lending transactions at more than 8,100 financial institutions covered by the Home Mortgage Disclosure Act in metropolitan statistical areas throughout the nation, MBA has determined that, in 2004 alone, the major players in the secondary market purchased more than 10 million loans totaling approximately \$1.78 trillion. *As of December 2005, more than 54 percent of all single-family mortgages outstanding -- more than \$5.4 trillion in single-family mortgages -- were securitized.* Similarly, 26 percent of all multi-family and commercial mortgages

outstanding – approximately \$682 billion in multi-family and commercial mortgages -- were securitized. Securitization is now the largest source of funding for multi-family mortgage debt, with approximately \$225 billion in apartment buildings debt outstanding as of the end of 2004, which was approximately 33 percent of all mortgage debt on multi-family buildings. The securitization market depends on uniformity, which in turn depends on the ability of thrifts and national banks to preempt state laws that would affect their lending and loan servicing operations. The MBS market has grown by more than 1,200 percent in a little over two decades.

In the past decade, securitization of single-family mortgages grew by more than 200 percent, from approximately \$1.8 trillion to approximately \$5.4 trillion. Today, nearly 70% of families own their home, according to a White House press release on May 24, 2006. George W. Bush, *National Homeownership Month, 2006, A Proclamation by the President of the United States of America*, Office of the Press Secretary (May 24, 2006) at <http://www.whitehouse.gov/news/releases/2006/05/20050524-6.html>. This is in contrast to 1940, when only 43.5% of families owned their homes. K.D. Vandell, *FHA Restructuring Proposals: Alternatives and Implications*, Table 2 (1995).⁴ This tremendous growth is attributable in large part to the ready availability of capital through securitization.

At the same time, the success of HOLA and the home loan industry is due in significant part to the federal preemption provided by HOLA, allowing savings associations to operate without the costs and burdens of complying with varying and inconsistent state laws and interpretations of state laws. “[I]nstead of being subject to a

⁴ This publication is available on the Internet at www.fanniemae.foundation.org/programs/hpd/pdf/hpd_0602_vandell.pdf.

hodgepodge of conflicting and overlapping state lending requirements, federal thrifts are free to originate loans under a single set of uniform federal laws and regulations.” 61 Fed. Reg. 50951, 50965 (Sept. 30, 1996). This furthers the “objectives of the HOLA by enabling federal thrifts to deliver low-cost credit to the public free from undue regulatory duplication and burden.” *Id.* Allowing the District Court’s ruling below to stand will return the market to the “parochial” mortgage to the disadvantage of those seeking credit.

Because national banks operate under a preemption regulation that is virtually identical to Section 560.2, any undermining of the OTS’s preemption authority would have a similarly negative impact on the lending and loan servicing activities of national banks. *See* 12 C.F.R. § 7.4009(c)(2).

The national banking system is a “venue for testing and evaluating the efficiencies and benefits that flow from uniform national standards.” Office of the Comptroller of the Currency, *National Banks and the Dual Banking System*, (September 2003), at 10.⁵ These benefits of the national system are not realized if federally-chartered banking institutions, including thrifts, “are unable to realize the efficiencies and benefits of operating under uniform national standards.” *Id.* (discussing national banks, but the observation is equally applicable to federal thrifts).

The importance of uniformity in lending and loan servicing regulation and practices also is demonstrated by the creation of the Federal Financial Institutions Examination Council (“FFIEC”). The FFIEC is a “formal interagency body empowered to prescribe uniform principles, standards, and report forms for the federal examination of financial institutions” by the federal regulatory agencies. *See*, FFIEC web site at www.ffiec.gov. The FFIEC thus helps ensure that all federally-charted thrifts and banks

⁵ This publication can be obtained on the Internet, at www.occ.treas.gov/DualBanking.pdf.

operate under uniform standards, as intended by Congress in enacting HOLA and the National Bank Act.

In summary, if the decision of the court below is allowed to stand, both federal thrifts and national banks will suffer, and with that the strength of the United States banking system, including the country's residential and commercial real estate finance system, which is so dependent on securitization. Without reversal, the resulting benefits to home buyers and other borrowers, and the nation's economy will be seriously undermined. The great successes brought about by HOLA through the wider availability of home loans and other banking services could be lost or significantly undermined. We therefore urge this Court to reverse the district court's decision.

II. PLAINTIFFS' STATE LAW CLAIMS ARE PREEMPTED BY FEDERAL LAW, BOTH BY THE OTS'S OCCUPATION OF THE FIELD OF REGULATION OF THE OPERATIONS OF FEDERAL SAVINGS ASSOCIATIONS AND EXPRESSLY BY THE APPLICABLE REGULATION.

As noted by the court below, there are three ways in which a federal law can preempt a state law: express preemption, field preemption, and conflict preemption. Here, OTS regulation preempts state law through, at minimum, both field preemption and express preemption. Field preemption occurs when a state law "regulates conduct in a field Congress intended the Federal Government to occupy exclusively" or "the federal interest is so dominant that the federal system will be assumed to preclude enforcement of state laws of the same subject." *English v. General Elec. Co.*, 496 U.S. 72, 79 (1990) (internal quotations and citations omitted). As its name implies, express preemption occurs whenever a federal scheme expressly provides for federal preemption. *See, e.g., Gracia v. Volvo Europa Truck, N.V.*, 112 F.3d 291, 294 (7th Cir. 1997). Express

presumption may be created by statute or regulation. *Fidelity Fed. Sav. & Loan Ass’n v. de la Cuesta*, 458 U.S. 141, 154 (1982) (federal regulations “have no less preemptive effect than federal statutes”).

A. The all-encompassing federal regulation of thrifts constitutes field preemption, barring any state attempts to regulate lending related activities.

HOLA and regulations implemented thereunder have always preempted state laws with respect to all aspects of the operations of federal savings associations. The very broad preemption of state laws by federal laws and regulations governing savings associations has been established since federally-chartered savings associations were first authorized by HOLA in 1933.

In enacting HOLA, Congress exercised its power to provide for federally-chartered savings associations and to authorize the FHLBB (and subsequently OTS) to issue regulations providing for the organization, incorporation, examination, operation, and regulation of federal thrifts, “giving primary consideration of the best practices of thrift institutions in the United States.” 12 U.S.C. § 1464(a). To provide for a uniform, federally-regulated thrift industry and thus to ensure that Federal thrifts would not be subject to a multitude of inconsistent state laws and regulations, Congress, exercising its powers enacted in HOLA, delegated to the FHLBB plenary and exclusive authority to regulate the lending-related practices of Federal thrifts and to preempt state laws affecting their operation. *See Eureka Fed. Sav. & Loan Ass’n v. Kidwell*, 672 F.Supp. 436, 439 (N.D. Cal. 1987) and *de la Cuesta*, 458 U.S. at 161-162.⁶ As the Supreme Court has

⁶ As discussed in more detail above, HOLA was enacted in response to the widespread failure of state savings and loans during the Depression. In analyzing the extent of federal preemption here, it is critical to keep in mind HOLA’s origins and the Congressional aim of increasing home ownership in the country.

recognized, HOLA “gave the [Federal Home Loan Bank] Board plenary authority to issue regulations governing federal savings associations.” *de la Cuesta*, 458 U.S. at 160.

Consistent with its statutory mandate, OTS has regulated virtually every aspect of the operations of federal thrifts. Beginning at 12 C.F.R. Part 500 and continuing through 12 C.F.R. Part 591, OTS regulation addresses all matters affecting the formation, operation and dissolution of each federal thrift from “its cradle to its corporate grave.” *Id.* at 145 (citation omitted). These regulations address, without limitation, unfair credit practices (12 C.F.R. § 535.2), late charges in connection with collecting debts (12 C.F.R. § 535.4), loan prepayments (12 C.F.R. § 560.34), and general home loan terms (12 C.F.R. § 560.35).⁷ In short, it would be difficult to imagine any aspect of the operations of a federal savings association that is not regulated by the OTS.

In light of the pervasive federal regulatory scheme, numerous courts have recognized that the federal interest in the regulation of savings associations is dominant and pervasive, and that Congress left no room for the states to supplement laws governing the operations of federal thrifts. *See, e.g., Conference of Fed. Sav. & Loan Ass’ns v. Stein*, 604 F.2d 1256, 1260 (9th Cir. 1979) (“regulation of federal savings associations by the OTS has been so pervasive as to leave no room for state regulatory

⁷ OTS regulations also govern, among other things; discrimination in lending and other services (12 C.F.R. Part 528); consumer protection in the sales of insurance, including anticoercion and antitying rules, prohibitions on misrepresentations, prohibitions on domestic violence discrimination, and disclosures and advertising (12 C.F.R. Part 536); formation of savings associations (12 C.F.R. Parts 543 and 544); funds transfer services (12 C.F.R. § 545.17); branches and other banking offices (12 C.F.R. §§ 545.91 through 545.101); fiduciary activities (12 C.F.R. Part 550); requirements for securities transactions (12 C.F.R. Part 551); procedures for incorporation, organization, and conversion of federal stock associations (12 C.F.R. Part 552); electronic operations, including automated teller machines, automated loan machines, the Internet, and even telephone operations (12 C.F.R. Part 557); subsidiary organizations (12 C.F.R. Part 559), and consumer privacy (12 C.F.R. Part 573).

control”), cited with approval in *Bank of Am. v. City & County of San Francisco*, 309 F.3d 551, 558 (9th Cir. 2002).

B. HOLA’s regulatory history expressly preempts any state attempts to regulate lending-related activities.

As the FHLBB explained in 1982, regulations promulgated under HOLA expressly preempt conflicting state laws:

The regulations in this Part 545 governing real estate loans are promulgated pursuant to the plenary and exclusive authority of the Board to regulate *all aspects* of the operations of Federal associations, as set forth in § 5(a) of the Home Owners’ Loan Act of 1933, as amended. *This exercise of the Board’s authority is preemptive of any state law purporting to address the subject of a Federal association’s ability or right to make, sell, purchase, participate or other deal in the mortgage loan instruments set forth in this Part, or directly or indirectly to restrict such ability or right.*

12 C.F.R. § 545.6(a)(2) (1982) (emphasis added).

Later that same year, federal savings associations were granted new powers by the Garn-St. Germaine Depository Institutions Act of 1982. Because this new preemption regulation was part of the OTS’s effort to more clearly address all of its new powers, it is stated more broadly than in 1982:

The regulations in this Part 545 are promulgated pursuant to the plenary and exclusive authority of the Board to regulate *all aspects* of the operations of Federal associations, as set forth in section 5(a) of the Home Owners’ Loan Act of 1933, 12 U.S.C. 1464, as amended. *This exercise of the Board’s authority is preemptive of any state law purporting to address the subject of the operations of a Federal association.*

12 C.F.R. 545.2 (1983) (emphasis added). This regulation still exists today, changed only to reflect the OTS as the successor to the Board.

In 1996, the OTS reorganized and streamlined its regulations, and created what is now 12 C.F.R. § 560.2, which is identical to today’s regulation.⁸ Subsection (a) of the

⁸ The full text of 12 C.F.R. § 560.2 is found within the addendum *infra*.

regulation expressly provides that “OTS is authorized to promulgate regulations that preempt state laws affecting the operations of federal savings associations” and that “OTS hereby occupies the entire field of lending regulation for federal savings associations.” 12 C.F.R. § 560.2(a). Subsection (b) lists thirteen examples of state laws that would be preempted, including “laws purporting to impose requirements regarding ... [p]rocessing, origination, servicing, sale or purchase of, or investment or participation in, mortgages.” 12 C.F.R. § 560.2(b)(10). Subsection (c) of the regulation specifically provides that certain state laws “are not preempted to the extent that they only incidentally affect the lending operations of Federal savings associations or are otherwise consistent with the purposes of paragraph (a) of this section.” 12 C.F.R. § 560.2(c). In promulgating this regulation, the OTS made clear that notwithstanding the fact that the regulation had been amended to acknowledge that a limited number of state laws are not preempted, the revised regulation did not change its view of preemption:

None of the changes implemented today should be construed as evidencing in any way an intent by OTS to change this long held position: OTS still intends to occupy the field of lending regulation for federal savings associations. OTS believes that the new lending preemption regulation is clearer and should significantly reduce the instances in which institutions need to request interpretive guidance from OTS.

61 Fed. Reg. 50951, 50952 (Sept. 30, 1996).

Thus, it is clear that the doctrines of field and express preemption both apply to bar any state attempts to regulate lending-related activities.

III. THE LOWER COURT ERRED IN FINDING A PRESUMPTION AGAINST FEDERAL PREEMPTION; THE PRESUMPTION AGAINST FEDERAL PREEMPTION IS INAPPLICABLE IN THE REALM OF REGULATION OF FEDERAL SAVINGS ASSOCIATIONS.

The court below concluded that Plaintiffs' state law claims were not preempted by HOLA or OTS regulation due in large part to the court's view that there is a presumption against federal preemption. Although that result might be appropriate in some areas of law, as discussed below, both years of court decisions and the OTS regulations make clear that such a presumption is not applicable with respect to regulation of the operations of federally-chartered banking institutions, including thrifts.

In fact, the appropriate presumption is that federal law and regulation *do preempt* state law. The Supreme Court has stated that powers granted to federal thrifts are interpreted as "not normally limited by, but rather ordinarily pre-empting, contrary state law." *Barnett Bank of Marion County, N.A. v. Nelson*, 517 U.S. 25, 32 (1996). As stated in the *Bank of America* case, "because there has been a history of significant federal presence in national banking, the presumption against preemption is inapplicable." *Bank of Am. v. City & County of San Francisco, supra*, 309 F.3d at 559. More recently, the Second Circuit agreed that "[t]he presumption against federal preemption disappears, however, in the fields of regulation that have been substantially occupied by federal authority for an extended period of time. Regulation of federally chartered banks is one such area." *Wachovia Bank, N.A. v. Burke*, 414 F.3d 305, 314 (2d Cir. 2005) (quoting *Flagg v. Yonkers Sav. & Loan Ass'n, FA*, 396 F.3d 178, 183 (2d Cir. 2005)). Finally, as OTS explained in implementing C.F.R. § 560.2(c): "Any doubt should be resolved in favor of preemption." 61 Fed. Reg. 50951, 50966 (Sept. 30, 1996).

If for no other reason, MBA respectfully submits the case should be reversed and remanded as a result of the lower court's application of an incorrect legal standard. *See, e.g., Gile v. United Airlines, Inc.*, 95 F.3d 492 (7th Cir. 1996) (reversing decision based on an erroneous conclusion of law).⁹

IV. THE LOWER COURT MISAPPLIED 12 C.F.R. § 560.2 AND ERRED IN FAILING TO FIND FEDERAL PREEMPTION OF CLAIMS RELATED TO LENDING-RELATED ACTIVITIES.

A. The lower court failed to follow the applicable regulatory guidelines.

After applying the wrong preemption presumption, the lower court compounded its error by misapplying Section 560.2(c), without first giving proper deference to Section 560.2(a) and (b), and by failing to find federal presumption.

When OTS promulgated Section 560.2 in 1996, it specifically contemplated that courts would look to the regulation for guidance, and provided a roadmap for interpretation:

*When confronted with interpretive questions under §560.2, we anticipate that courts will, in accordance with well established principles of regulatory construction, look to the regulatory history of §560.2 for guidance. In this regard, OTS wishes to make clear that the purpose of paragraph (c) is to preserve the traditional infrastructure of basic state laws that undergird commercial transactions, not to open the door to state regulation of lending by federal savings associations. **When analyzing the status of state laws under §560.2, the first step will be to determine whether the type of law in question is listed in paragraph (b). If so, the analysis will end there; the law is preempted. If the law is not covered by paragraph (b), the next question is whether the law affects lending. If it does, then, in accordance with paragraph (a), the presumption arises that the law is preempted. This presumption can be reversed only if the law can clearly be shown to fit within the confines of paragraph (c). For these purposes, paragraph (c) is intended to be interpreted narrowly. Any doubt should be resolved in favor of preemption.***

⁹ *Gile* was decided on an abuse of discretion standard. As noted in Appellants' Opening Brief, the appropriate standard of review here is *de novo*. *Toney v. L'Oreal USA, Inc.*, 406 F.3d 905, 907-908 (7th Cir. 2005); *Moran v. Rush Prudential HMO, Inc.*, 230 F.3d 959, 966 (7th Cir. 2000).

61 Fed. Reg. 50951, 50966 (Sept. 30, 1996) (emphasis added).

The lower court ignored OTS's directions. Had it followed them, it first would have concluded that Plaintiffs' claims are preempted under Section 560.2(b), which provides "illustrative examples" of preempted state laws, including without limitation, the ability of a thrift to require or obtain private mortgage insurance, the terms of credit, late charges and other loan-related fees, escrow accounts, disclosure and advertising, and processing, origination and servicing of mortgages. 12 C.F.R. § 560.2(b). Plaintiffs' claims fall squarely within the regulation's list of laws that are expressly preempted. The table on pages 23 and 24 of Appellants' Opening Brief nicely illustrates this.

When the district court considered the preemptive effect of HOLA and the OTS regulations, it erroneously reversed this framework and first considered whether Plaintiffs' claims might be considered contract claims or tort claims. Such an approach ignores the fundamental aspect of OTS preemption: in those areas that fundamentally govern a savings association's lending and loan servicing operations, state law is always preempted.

The error of the court below is exactly the type of mistake that the OTS strove to avoid when it explained the two-part test for determining when a state law would not be preempted. Responding to concerns that "states seeking to avoid federal preemption of their laws or regulations might attempt to characterize those laws as falling within" the state laws listed in Section 560.2(c), the OTS described the two-part test under which Section 560.2(c) would be considered only after determining that the particular state law did not address the matters expressly preempted in Section 560.2(b). 61 Fed. Reg. 50951, 50966 (Sept. 30, 1996).

In addition, placing inappropriate emphasis on whether a state or plaintiff characterizes a particular law or claim as a “tort” or “contract” matter would allow these narrow preemption exceptions to swallow the rule. As defined by Black’s Law Dictionary, a tort is a “civil wrong, other than breach of contract, for which remedy may be obtained.” Black’s Law Dictionary, (8th Ed. 2004). Thus, the charging of an excessive fee, an ambiguous disclosure, the mishandling of a loan customer’s payments – could all be considered torts in this dictionary sense. Clearly Congress and the OTS did not intend that someone could simply claim that he was “wronged,” and thus avoid preemption, especially when, as in the case of all Plaintiffs’ claims, the alleged “wrongs” all relate to the fundamental operations of a federal savings association.

In many respects the exceptions stated in Section 560.2(c) are self-evident. If a bank teller assaults a customer, that is a matter for criminal law enforcement, not the OTS. If a bank employee has an automobile accident that would be subject to state tort laws, not federal banking regulation. If a bank contracted for office space and then stopped paying rent, resolving the bank’s dispute would be a matter of state contract law. But if any of these laws are used to circumvent federal preemption of matters relating to the operations of a federal savings association, then the analysis is quite different and federal law would preempt to that extent.

B. Caselaw and OTS Opinions both compel a finding of preemption.

A central question in this appeal is what state laws are preempted under HOLA and the regulations promulgated thereunder. Phrased another way, when does a state law of general applicability cross the line and constitute an impermissible regulation of federal thrift activities? Both the case law discussed below and several recent OTS

formal opinions make clear that any attempted state regulation of federal thrift lending-related activity is preempted.

Pages 27-31 of Appellants' brief describe in detail numerous cases in which courts have found preemption of state claims that affect lending-related activities. *See, e.g., Boursiquot v. Citibank FSB*, 323 F. Supp. 2d 350, 356 (D. Conn. 2004) (claims for unfair trade practices based on lender's conduct and fees charged preempted; court specifically rejected claim that Connecticut's Unfair Trade Practices Act fell within commercial law exception of Section 560.2(c) because the Act's "effects are not merely incidental, they have a direct bearing [on] the lending operations of federal savings associations"); *Haehl v. Washington Mutual Bank, F.A.*, 277 F. Supp. 2d 933, 942 (S.D. Ind. 2003) (various state claims based on allegedly improper reconveyance fees preempted; tort exception under Section 560.2(c) inapplicable because "applying tort law in this case would more than 'incidentally affect' lending operations by imposing substantive requirements on lending operations, specifically the types on loan-related fees that a bank could charge."); *Moskowitz v. Washington Mutual Bank, F.A.*, 768 N.E.2d 262, 266 (Ill. Ct. App. 2002) (claims for deceptive business practices and breach of contract based on undisclosed mortgage payoff statement fee preempted; Section 560.2(c) does not exempt from preemption a deceptive trade practices claim that is based on an allegation of improper charging of loan-related fees, and "use of contract law here would more than 'incidentally affect' the lending operations"). *See also Rosenberg v. Washington Mutual Bank, F.A.*, 849 A.2d 566 (N.J. Super. Ct. App. Div. 2004) (state claims related to allegedly misleading mortgage billing statement preempted); *Chaires v. Chevy Chase Bank F.S.B.*, 748 A.2d 34 (Md. Ct. App. 2000) (state claims for unfair and

deceptive trade practices based on allegedly improper loan-related fees preempted); *Monroig v. Washington Mutual Bank*, 800 N.Y.S.2d 416 (App. Div. 2005) (common law claims related to allegedly improper mortgage spread premium preempted).

The recent decision in *WFS Financial, Inc. v. Superior Court*, 140 Cal. App. 4th 637 (Ct. App. 2006) further supports preemption. In *WFS*, the plaintiff sought to collect a deficiency owed on an automobile loan after the car was repossessed and sold. The defendant alleged that the plaintiff had not complied with state law disclosure requirements and filed a class action counter-complaint asserting that the plaintiff's practice of seeking a deficiency after issuing defective notices was an unfair business practice. After a lengthy analysis of preemption, HOLA, and Section 560.2, the court concluded that the "statutes, regulations, and comments of the OTS make abundantly manifest and clear the congressional intent to expressly preempt state law in the area of lending regulation of federal savings associations." *Id.* at 649. The court concluded that "post-repossession debt collection activities" are part of "lending operations" and therefore the plaintiff's claims were preempted. The court also noted that the "laudatory purpose of the state statute is not the point and does not preclude preemption." *Id.* at 651.

In addition to this compelling caselaw, OTS has provided ongoing guidance in the form of literally hundreds of opinions with respect to federal preemption of specific state laws.¹⁰ These opinions also confirm that Plaintiffs' claims are preempted. In at least three instances the OTS has opined that general consumer protection laws cannot be used to compel a savings association to comply with laws that otherwise are preempted. For example, the New Jersey Home Ownership Security Act of 2002, N.J. Stat. §§ 46:10B-22

¹⁰ FHLBB and OTS preemption opinions since 1976 can be accessed through the FFIN-OTSL data base of WestLaw, using the term "preempt!" to conduct the search.

et seq. (the “New Jersey HOSA”), purported to regulate the terms of credit, late fees and other loan-related fees, disclosures, loan acceleration and other loan servicing matters, all of which the OTS determined to be preempted by federal law. This New Jersey HOSA also provided that a violation of the law constituted an unlawful practice under the New Jersey Fraud Act, which allows for legal and equitable relief, treble damages, and costs and attorneys’ fees. N.J. Stat. §§ 56:8-1 *et seq.* A violation of the New Jersey HOSA also would be a foreclosure defense against the creditor or any subsequent holder or assignee of the loan. The OTS concluded that this “compliance scheme” could not be applied to federal savings associations in a manner that would compel them to comply with the preempted provisions of the New Jersey HOSA, adding:

Such a result would have more than an incidental effect on the lending operations of federal savings associations and would run contrary to HOLA’s purpose of allowing federal savings associations to exercise their lending powers in accordance with a uniform federal scheme.

OTS Opinion P-2003-5 (July 22, 2003). *See also* OTS Opinion P-2003-2 (Jan. 30, 2003), concerning a New York law that required a lender to prove compliance with preempted laws as a prerequisite to foreclosure, and Opinion P-2003-6 (Sept. 2, 2003), making violation of the preempted New Mexico laws an unfair and deceptive trade practice.

Among other things, Plaintiffs’ Consolidated Class Action Complaint filed on August 23, 2004 (the “Complaint”) alleges that Ocwen inappropriately charges late fees and force places insurance. Complaint, ¶ 48, 58. Numerous OTS Opinions confirm preemption of state laws governing late fees, including OTS Opinion P-2003-6 (Sept. 2, 2003) regarding New Mexico law; OTS Opinion P-2003-5 (July 22, 2003), regarding New Jersey law; and OTS Opinion P-2003-1 (Jan. 21, 2003), regarding Georgia law. Similarly, in 1999, the OTS opined that state law could not be applied either to limit the

ability of federal savings associations to force place insurance on properties securing homes or to limit thrifts' choice of insurers or the premiums charged on the forced placement of insurance. OTS Opinion P-99-3 (Mar. 10, 1999).

The OTS's interpretations of HOLA and its regulations are entitled to broad deference under *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984) and *United States v. Mead Corp.*, 533 U.S. 218 (2001). Cases in which the court granted the *Chevron* deference to the OTS include *National Home Equity Mortgage Association v. Office of Thrift Supervision*, 373 F.3d 1355 (D.C. Cir. 2004); *Rapp v. U.S. Dept. of Treasury, Office of Thrift Supervision*, 52 F.3d 1510, 1518 (10th Cir. 1995); and *Far West Federal Bank, S.B. v. Director, Office of Thrift Supervision*, 951 F.2d 1093, 1099 (9th Cir. 1991).

Finally, it should be noted that, as the OTS said in its recent opinion preempting certain local lending regulations, preemption "does not create a regulatory vacuum." OTS Opinion P-2006-2 (Mar. 7, 2006). The OTS conducts regular examinations of thrift lending operations, and thrifts are subject to numerous federal laws restricting abusive practices, such as those found in the Home Ownership Equity Protection Act and its implementing regulations (15 U.S.C. § 1639, 12 C.F.R. Part 226, subpart E). *Id.* In fact, the conduct alleged by Plaintiffs was specifically addressed in the Supervisory Agreement entered into between Ocwen Federal Bank FSB and the OTS on April 19, 2004 (available at <http://www.ots.treas.gov/docs/9/93606.pdf>). That agreement directly governs the mortgage practices Plaintiffs challenge here.

CONCLUSION

For the foregoing reasons, MBA respectfully submits this Court should reverse the decision below and find that all of Plaintiffs' state law claims are preempted as a matter of law.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

Counsel for amicus curiae, MBA, hereby certifies that this brief complies with the type-volume limitation set forth in Fed. R. App. P. 32(a)(7)(C) and Fed. R. App. P. 29(d). This brief contains 6,970 words, including headings, footnotes, and quotations, and excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii) as reported by the word count function of Microsoft Word.

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ADDENDUM

Reproduction of Statutes, Rules, Regulations, etc. as allowed by Fed. R. App. P. 28(f)

RELEVANT REGULATION

The OTS regulation at issue in this case is 12 C.F.R. § 560.2, which provides in full as follows:

(a) Occupation of field. Pursuant to section 4(a) and 5(a) of HOLA, 12 U.S.C. 1463(a), 1464(a), OTS is authorized to promulgate regulations that preempt state laws affecting the operations of federal savings associations when deemed appropriate to facilitate the safe and sound operation of federal savings associations, to enable federal savings associations to conduct their operations in accordance with the best practices of thrift institutions in the United States, or to further other purposes of the HOLA. To enhance safety and soundness and to enable federal savings associations to conduct their operations in accordance with best practices (by efficiently delivering low-cost credit to the public free from undue regulatory duplication and burden), OTS hereby occupies the entire field of lending regulation for federal savings associations. OTS intends to give federal savings associations maximum flexibility to exercise their lending powers in accordance with a uniform federal scheme of regulation. Accordingly, federal savings associations may extend credit as authorized under federal law, including this part, without regard to state laws purporting to regulate or otherwise affect their credit activities, except to the extent provided in paragraph (c) of this section or § 560.110 of this part. For purposes of this section, "state law" includes any state statute, regulation, ruling, order or judicial decision.

(b) Illustrative examples. Except as provided in § 560.110 of this part, the types of state laws preempted by paragraph (a) of this section include, without limitation, state laws purporting to impose requirements regarding:

- (1) Licensing, registration, filings, or reports by creditors;
- (2) The ability of a creditor to require or obtain private mortgage insurance, insurance for other collateral, or other credit enhancements;
- (3) Loan-to-value ratios;
- (4) The terms of credit, including amortization of loans and the deferral and capitalization of interest and adjustments to the interest rate, balance, payments due, or term to maturity of the loan, including the circumstances under which a loan may be called due and payable upon the passage of time or a specified event external to the loan;
- (5) Loan-related fees, including without limitation, initial charges, late charges, prepayment penalties, servicing fees, and overlimit fees;
- (6) Escrow accounts, impound accounts, and similar accounts;

- (7) Security property, including leaseholds;
 - (8) Access to and use of credit reports;
 - (9) Disclosure and advertising, including laws requiring specific statements, information, or other content to be included in credit application forms, credit solicitations, billing statements, credit contracts, or other credit-related documents and laws requiring creditors to supply copies of credit reports to borrowers or applicants;
 - (10) Processing, origination, servicing, sale or purchase of, or investment or participation in, mortgages;
 - (11) Disbursements and repayments;
 - (12) Usury and interest rate ceilings to the extent provided in 12 U.S.C. 1735f-7a and part 590 of this chapter and 12 U.S.C. 1463(g) and § 560.110 of this part; and
 - (13) Due-on-sale clauses to the extent provided in 12 U.S.C. 1701j-3 and part 591 of this chapter.
- (c) State laws that are not preempted. State laws of the following types are not preempted to the extent that they only incidentally affect the lending operations of Federal savings associations or are otherwise consistent with the purposes of paragraph (a) of this section:
- (1) Contract and commercial law;
 - (2) Real property law;
 - (3) Homestead laws specified in 12 U.S.C. 1462a(f);
 - (4) Tort law;
 - (5) Criminal law; and
 - (6) Any other law that OTS, upon review, finds:
 - (i) Furthers a vital state interest; and
 - (ii) Either has only an incidental effect on lending operations or is not otherwise contrary to the purposes expressed in paragraph (a) of this section.