

## **ROSE V. CHASE BANK – PREEMPTION OF STATE UDAP LAWS**

by

**ROBERT M. JAWORSKI**

In a decision of the Ninth Circuit Court of Appeals filed on January 23, 2008, Chase Bank, USA, N.A. (“Chase”) came out smelling like a rose. *Rose v. Chase Bank USA, N.A.*, 513 F.3d 1032 (9<sup>th</sup> Cir. 2008). That decision affirmed a lower court’s dismissal, on the pleadings, of a class action complaint filed against Chase by plaintiff, Denise Rose, and other similarly situated California residents, on grounds of federal preemption.

The complaint alleged that Chase violated California’s Unfair Competition Law, Ca. Bus. & Prof. Code § 17200 *et seq.* (the “UCL”), in three separate regards in connection with Chase’s practice of mailing “convenience checks” (which can be immediately cashed by the recipient) to its credit card holders. Specifically, plaintiffs alleged that, when Chase sent the convenience checks to them, it failed to make disclosures required by Cal. Civ. Code § 1748.9(a)(1) and (a)(3) (the “CA Convenience Check Law”); and that this failure constituted (1) an “unlawful” business practice, (2) a “fraudulent” business practice and/or “deceptive or misleading advertising,” and (3) an “unfair” business practice, each a violation of the UCL.

In support of its motion to dismiss the complaint, Chase argued that, as a national bank, it was empowered under the National Bank Act (“NBA”) and applicable regulations of the federal Office of the Comptroller of the Currency (“OCC”) to “make, sell, purchase, participate in, or otherwise deal in [non-real estate secured] loans . . . , subject to such terms, conditions, and limitations prescribed by the [OCC] and any other applicable Federal law.” 12 C.F.R. § 7.4008(a). It further argued that, with regard to the applicability of state law to a national bank engaged in non-real estate lending, OCC regulations provide that state laws which “obstruct, impair, or condition a national bank’s ability to fully exercise its Federally authorized non-real estate lending powers are not applicable to national banks,” and, more specifically, that national banks may make non-real estate loans without regard to state laws concerning “[d]isclosure 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.” 12 C.F.R. § 7.4008(d).

The district court found Chase’s argument compelling and dismissed the complaint in its entirety. In affirming the district court’s dismissal, the Ninth Circuit first determined that Chase could not be found to have violated the UCL by having committed an “unlawful” business practice. In this regard, it found that the CA Convenience Check Law was clearly preempted by the NBA and applicable OCC regulations and, hence, a violation of that law by Chase could not be deemed to be “unlawful.”

Plaintiffs tried to salvage its other claims, arguing that they should survive because they were not predicated upon a finding that Chase’s failure to provide the disclosures required by the CA Convenience Check Law was “unlawful.” Those claims, they said, alleged that Chase’s failure to provide the required disclosures constituted a “fraudulent” or “deceptive and unfair” business practice which, considered by itself and without regard to the CA Convenience Check Law, violated the UCL. Although not articulated in the decision, plaintiffs presumably asserted that in these regards at least the UCL is a law of general applicability with which all businesses in California, not just lenders or banks, must comply, and that it does not significantly impair Chase’s ability to exercise its lending powers. It would therefore follow that plaintiffs second and third claims under the UCL should not be deemed preempted by the NBA..

However, the Ninth Circuit rejected this argument, finding that “the proper inquiry is whether the ‘legal duty that is the predicate of’ Plaintiffs state law claim falls within the preemptive power of the NBA or [the OCC’s] regulations ....” Here, the legal duty that underlies plaintiffs’ claims of “fraudulent” or “deceptive and unfair” business practices is the duty to provide the disclosures required by the CA Convenience Check Law, which the Court already determined was preempted as to Chase.

The decision in *Rose* seems clearly correct. Since all of plaintiffs’ claims were predicated upon a violation of the CA Convenience Check Law, and further, since that law is not a law of general applicability but one which specifically seeks to regulate lending, it would appear to be clearly preempted by the NBA and applicable OCC regulations. Plaintiffs’ attempt to “end run” federal preemption by simply recharacterizing its claims as violations of the UCL was therefore properly rejected.

It is interesting and perhaps instructive, however, to contrast the Ninth Circuit’s decision in *Rose* with another recent California district court decision involving Chase. *See Jefferson v. Chase Home Mortgage*, 2007 WL 4774410 (N.D. Cal. Dec. 14, 2007). In this decision, the court was faced with claims that Chase (1) committed an unfair business practice under the UCL by misrepresenting and/or systematically breaching its promises about how it would credit prepayments to plaintiff’s loan account, and (2) violated California’s False Advertising Act, Cal. Bus. Prof. Code § 17500 *et seq.*, by disseminating false or misleading statements about its services.

The court held that plaintiff’s claims were not preempted by the NBA, stating that:

The duty to refrain from misrepresentation falls on all businesses. It does not target or regulate banking or lending, and it only incidentally affects the exercise of banks’ real estate lending powers.

The court also pointed out that

Plaintiff does not claim that California consumer protection laws require Chase to service or process loans, include specific content in its disclosures, or handle repayment of loans in any particular manner – requirements that would be preempted .... Instead, Plaintiffs claim that the laws require Chase to refrain from misrepresenting the manner in which it *does* service loans.

Assuming that the decisions in both *Rose* and *Jefferson* are correct, it would seem that in California at least UCL-based claims against national banks will likely be held preempted unless based on general allegations of misrepresentation or breach of contract (as opposed to specific allegations of failure to comply with a state law designed to regulate lending or banking).

Whether this result strikes a fair balance between the needs of national banks to operate uniformly across state lines and the needs of states to take action to protect their citizens against unfair and deceptive business practices by national banks is debatable. However, it would seem to be a given that what is judicially determined in one state to constitute misleading, deceptive or misrepresentative behavior may not be so determined in another state. The consequence is that national banks would be forced to adopt different practices in different states (or to alter their practice nationwide to comply with the most restrictive states) – a distinctively non-uniform approach.

**Robert M. Jaworski** is a partner in the Financial Services Regulatory Group of Reed Smith, LLP in Princeton, New Jersey and a former Deputy Commissioner of the New Jersey Department of Banking. He is also Co-Chair of the RESPA and Housing Finance Subcommittee of the American Bar Association's Consumer Financial Services Committee; the former Editor of Pratt's Mortgage Compliance Letter, a national publication on mortgage compliance issues; and a member of the Board of Directors of the New Jersey Bar Association's Banking Law Section. He has also developed and teaches a course to prepare individuals to take and pass the New Jersey mortgage license qualifying examinations. Mr. Jaworski provides compliance and regulatory advice to banks and other lenders, and regularly assists Reed Smith litigators in defending lenders in individual and class actions.