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# Exorcising McCulloch: The Conflict-Ridden History of American Banking Nationalism and Dodd-Frank Preemption

Roderick M. Hills Jr.

*NYU School of Law*, [roderick.hills@nyu.edu](mailto:roderick.hills@nyu.edu)

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## ***Exorcising McCulloch***

### **Exorcising *McCulloch*: The Conflict-Ridden History of American Banking Nationalism and Dodd-Frank Preemption**

*Roderick M. Hills, Jr.*<sup>1</sup>

#### *Abstract*

*Conventional wisdom holds that federal law's conferring banking powers on national banks presumptively preempts state laws seeking to control the exercise of those powers. This conventional wisdom springs from a long-standing legal tradition, originating with *McCulloch v. Maryland*, that nationally chartered banks are federal instrumentalities entitled to regulate themselves free from state law, even when national law fails to address the risks that state law seeks to regulate. Incorporated into National Bank Act of 1864 by 19th century precedents but then abandoned by the New Deal Court, *McCulloch*'s theory of preemption is being revived today by the Office of the Comptroller of the Currency ("OCC") to preempt broad swathes of state law.*

*This article maintains that it is time to exorcise *McCulloch*'s theory from our preemption jurisprudence. Far from being sanctioned by legal tradition, *McCulloch*'s theory that national banks are federal instrumentalities offends a deeply rooted tradition in American political culture and law that I call the "anti-banker non-delegation principle. This principle has been manifest in campaigns against national banks' immunities from political oversight ranging from Andrew Jackson's 1832 veto of the charter of the Second Bank of the United States message to Louis Brandeis' 1912 campaign against the "House of Morgan" as a "financial oligarchy." Rather than accept *McCulloch*'s view of banks as impartial instruments of the federal government, the American political system and, since the New Deal, the federal courts, have adopted the view that federal law should not delegate unsupervised power to private banks to determine the honesty, safety, and soundness of their own operations. Accordingly, if federal regulators set aside state laws regulating banking practices, then those federal regulators must explain how federal law addresses the risks the state law attempts to control.*

*The most recent effort to eliminate *McCulloch*'s theory of preemption, according to this article, §1044(a) of the Dodd-Frank Act, which provides detailed standards governing the power of the OCC to preempt state law. This article argues that the OCC's 2011 rules mistakenly revive *McCulloch*'s theory of preemption, contradicting not only §1044(a) but also the more general tradition of distrusting unsupervised delegations of immunity from state law to national banks. In particular, like *McCulloch*, the OCC's rules draw irrational distinctions between states' general common-law doctrines and states' rules specifically directed towards banking practices, subjecting the latter to a sort of field preemption. Rather than accept such preemption, this article urges that courts ought to follow the ordinary principles of conflict*

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<sup>1</sup> William T. Comfort III Professor of Law New York University Law School. The author expresses his gratitude for the comments of the participants in the Conference on Administrative Law and the Dodd-Frank Act held by the Center for Business Law & Regulation Case Western University Law School and the comments of workshop participants at New York University's legal theory workshop. In addition, the author thanks Chris Asta, NYU Law School, Class of 2014, for first-rate research assistance.

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*preemption, barring preemption of state law unless the OCC has specifically approved the banking practice that state law forbids.*

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### I. Introduction

The federal courts seem to assume a long, unbroken historical consensus that nationally chartered banks ought to be governed by the federal government to the exclusion of the states. Since the U.S. Supreme Court handed down *McCulloch v. Maryland*, it has been common for judges and scholars to say “history” has somehow called for law governing nationally chartered banks to be centralized. As Justice Breyer described preemption of state law under the National Bank Act, writing for the Court in *Barnett Bank v. Nelson*,

In using the word "powers," the [National Bank Act] chooses a legal concept that, in the context of national bank legislation, has a history. That history is one of interpreting grants of both enumerated and incidental “powers” to national banks as grants of authority not normally limited by, but rather ordinarily pre-empting, contrary state law.<sup>2</sup>

This “history,” according to Justice Breyer, requires the presumption that “normally Congress would not want States to forbid, or to impair significantly, the exercise of a power that Congress explicitly granted.” Thus, there should be no judicial straining to figure out a way for state and federal law to co-exist: If a bank is authorized to do something so far as federal law is concerned, then that bank’s authorization preempts any state law that would interfere with a banking power “that Congress explicitly granted,” even if the state law in question does not single out national banks for discriminatory treatment. As Jamelle Sharp describes the doctrine, courts observe a “centralization default” where state regulation of national banks is concerned,<sup>3</sup> a default derived from some alleged jurisprudential tradition of regarding state control of nationally chartered banks with suspicion.

The idea that American history implies this sort of “centralization default” has been defended administratively as well as judicially. Consider, as an example of such administrative reliance on alleged historical consensus, the justification for the preemption rules issued by the Office of the Comptroller of the Currency (“OCC”) in the summer of 2011. The OCC’s 2011 rules construed the Dodd-Frank Act’s preemption clauses expressly codifying *Barnett Bank*’s preemption standard, a statutory standard providing that a “[s]tate consumer financial law” is preempted, even if such a law does not single out nationally chartered banks for discriminatory treatment, if the state law “prevents or significantly interferes with the exercise by the national bank of its powers....”<sup>4</sup> Despite the reference to *Barnett Bank*, one might reasonably infer that this clause was intended to cut back on preemption of state law. After all,

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<sup>2</sup> *Barnett Bank v. Nelson*, 517 U. S. 25 (1996).

<sup>3</sup> Jamelle Sharp, *Legislating Preemption*, 53 Wm. & Mary L. Rev. 163, 218 (2011).

<sup>4</sup> 12 U.S.C. section 25b(b)(1)(b).

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the clause contains unusual requirements that the OCC support preemption by making a “specific finding” on a “case-by-case basis”<sup>5</sup> and supported by “substantial evidence made on the record of the proceeding.”<sup>6</sup> Further, the clause calls for such agency preemption to be accorded only *Skidmore* deference, not *Chevron* deference, and the clause expressly bars field preemption.<sup>7</sup> How could such unusually specific statutory admonitions *not* be an effort to trim back on the preemption status quo?

OCC, however, re-issued their 2004 rules in the summer of 2011 in almost identical terms, declaring once more that nationally chartered banks may make loans “without regard to state-law limitations concerning” a broad array of topics.<sup>8</sup> In the bluntly critical comment of George W. Madison, the Department of Treasury’s General Counsel, “[t]he [2011] rule seems to take the position that the Dodd-Frank standard has no effect.” In response, the OCC predictably trotted out the argument from history: Broad preemption, according to the OCC, had been a “pillar[]” of banking law for “nearly 150 years,” providing uniformity of regulation necessary for a national market in financial services that guarantees prosperity and growth.<sup>9</sup>

In what follows, I will argue that, contrary to the OCC’s claim, the preemption of state banking law’s enforcement against national banks runs against a strong tradition in American political culture and legal doctrine that I call the “anti-banker non-delegation principle.” This principle opposes national preemption of state banking law if the preempting laws delegates general banking powers to private bankers without subjecting the exercise of those powers to any specific governmental oversight. This anti-banker non-delegation doctrine explains longstanding and frequently successful opposition to private banks’ preemption of state laws by the Anti-Federalists, Jeffersonian Republicans, Jacksonians, and post-Civil War Democrats. The point of such opposition was not so much to protect state rights or decentralized policy-making as to insist that, if federal regulators set aside state laws, then they should make some specific effort either to provide substitute national regulation or to explain why private bankers could be trusted to self-regulate themselves. The anti-banker non-delegation doctrine, in short, was not a theory of that subnational governments were especially trustworthy but rather that private bankers were

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<sup>5</sup> 12 U.S.C. section 25b(b)(1)(B).

<sup>6</sup> 12 U.S.C. 25b(c).

<sup>7</sup> 12 U.S.C. §25b(b)(5)(A).

<sup>8</sup> The topics for non-real estate loans included state-law requirements regarding (1) “(1) Licensing, registration (except for purposes of service of process), filings, or reports by creditors; (2) The ability of a creditor to require or obtain insurance for collateral or other credit enhancements or risk mitigants, in furtherance of safe and sound banking practices; (3) Loan-to-value ratios; (4) The terms of credit, including the schedule for repayment of principal and interest, amortization of loans, balance, payments due, minimum payments, 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) Escrow accounts, impound accounts, and similar accounts; (6) Security property, including leaseholds; (7) Access to, and use of, credit reports....” 12 CFR section 7.4008(d).

<sup>9</sup> “Uniform national rules across state lines,” according to the OCC, “has helped to foster the growth of national products and services and multi-state markets ... a powerful engine for prosperity and growth” that has been “the fundamental principle of Federal preemption as applied to national banks” and one of the “twin pillars of the national and state banking systems ... for nearly 150 years.” OCC, Statement of Basis and Purpose, Dodd-Frank Act Implementation, July 21<sup>st</sup>, 2011, at 19-20.

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especially untrustworthy. National law could supplant state law, but only if the national lawmakers (whether Congress or some executive official) actually set forth a specific national regulatory standard to replace state law. Absent such specific supervision, opponents of private bankers preferred the inefficiency of state law to the perceived corruption of bankers' self-regulation.

At the core of this conflict over the national government's duty to supervise private banking is the legitimacy and meaning of *McCulloch v. Maryland*. *McCulloch* relied on a theory of field preemption barring states from regulating or taxing nationally chartered banks impose taxes or regulations on nationally chartered banks even when such state law did not conflict with any specific federal statute or policy. In effect, such preemption allowed privately owned banks to adopt banking practices that were inconsistent with state law even when such practices had not been specifically reviewed or approved by either Congress or the OCC. Incorporated into National Bank Act of 1864 by 19<sup>th</sup> century precedents and adopted by the OCC, *McCulloch*'s field preemption allowed private decision-making to trump state law.

As I explain in Part II, *McCulloch*'s theory of field preemption has repeatedly run up against a deeply rooted "Country Party" theory of politics. On this theory, the national government is easily corrupted by financiers into delegating excessive powers to private banks, making such banks a sort of private and self-interested state within a state. National corporate charters that broadly preempted state regulation, therefore, were signs of a likely corrupt bargain between well-connected financiers and national politicians. Anti-Federalists, Jeffersonians, and Jacksonians, inspired by this Country Party theory, denounced national chartering of banking corporations in general and *McCulloch* in particular as political heresy. After President Andrew Jackson vetoed the Second Bank's charter in large part because it conferred immunity from state taxation, *McCulloch* was effectively buried until the Civil War.

Although *McCulloch*'s theory of field preemption was revived after the Civil War as a gloss on the National Bank Act ("NBA"), I explain in Part III that the U.S. Supreme Court soon found that the theory was untenable. Under the Court's interpretation of *McCulloch*, state laws specifically addressed to national banks' lending or deposit-taking were subject to a norm of field preemption, while state laws defining general rules of contract, tort, property, and corporate law were given broad deference. Following this distinction, postbellum courts initially held that banks' national charters preempted state laws on usury, criminal laws regulating bank officers' conduct regarding the bank's internal governance, and state banking rules on the forfeiture of abandoned bank accounts. But the same courts also held that national banks were pervasively subject to state common-law doctrines generally governing corporate law, contract, and tort. By the early twentieth century, however, the ideological underpinnings of *McCulloch* were being undermined by growing distrust of private bankers in the wake of the Panic of 1907 and the "New Freedom" campaign of Woodrow Wilson and Louis Brandeis against the power of banks – in particular, the "House of Morgan" – to regulate themselves free from governmental oversight. Starting in the 1920s, the United States Supreme Court gradually shifted preemption doctrine to allow state law to fill the gaps in the National Banking Act on specific banking issues

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like national banks' branching, misappropriation of deposits, or special security required for accepting deposits of state or local governments' revenue. By the end of the New Deal, the distinction between general state laws and specifically bank-related state laws was in shambles, replaced by ordinary principles of conflict preemption.

In Part IV, I will argue that the OCC's 2004 and 2011 rules are best understood as a third effort to revive *McCulloch*'s theory of field preemption. Under the OCC's rules, states' general common-law doctrines are given deference, while states' rules specifically regulating banking practices like deposit-taking or lending are presumed to be preempted. The OCC has justified these rules as an effort to secure scale economies of nationally uniform regulation for banking practices that take place on a national scale. But the OCC's rules, by exempting state common-law doctrines, seem far too under-inclusive for such an end. Instead, the OCC's rules seem better calculated to protect private banks' autonomy from state regulation even when national bank regulators have made no specific findings about the reliability of private banks' self-regulation. Such a rationale suffers from two flaws. First, the OCC never articulated any argument for special suspicion of states' banking-specific rules. Second, §1044(a) of the Dodd-Frank Act, defining the scope of banking preemption, seems to repudiate such an across-the-board preemption of state law. Both in its language and its legislative history, §1044(a) seems to express the same sort of anti-banker non-delegation principle as that pressed by Andrew Jackson in 1832 against Nicholas Biddle or Louis Brandeis in 1912, against the House of Morgan – the principle allowing state law to be set aside by federal regulators only if the latter specifically examine the risk controlled by the former to insure its adequate control by federal rules.

In Part V, I conclude by outlining a strategy for finally exorcising *McCulloch* from our preemption doctrine by applying ordinary rules of conflict preemption to state law. State law should govern banks unless the OCC has specifically approved the banking practice that state law forbids. There are good reasons rooted in scale economies in risk assessment and suppression of state protectionism to nationalize banking policy. But the traditional American suspicion of bankers' influence over the national government suggests that OCC ought to approve the specific banking practice that state common law forbids, making factual findings about the specific concerns of consumer deception, default risk, and the like, that form the basis of the state claims being preempted. This is not to say that OCC cannot simply deregulate some aspect of banking by relying on markets untrammelled by state common-law liability to insure good banking practices. Rather, it is to argue that the adequacy of markets is a topic on which the OCC ought to bring its expertise to bear rather than recite preemptive *ipse dixit* dating from *McCulloch*.

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### II. Country Party Ideology, Finance, and Federalism: The Anti-Banker Non-Delegation Doctrine in Antebellum American Banking Law

One cannot understand the equivocal position that *McCulloch*'s theory of banking immunity holds in American law and politics unless one also understands how deeply Americans feared and resented bankers during the 18<sup>th</sup> and 19<sup>th</sup> centuries. A standard theme of Anti-Federalist, Jeffersonian Republican, and Jacksonian Democratic rhetoric was that financiers could capture the national government through their inside connections and mastery of financial *arcana*. The antidote to this danger of capture was what I call the "anti-banker non-delegation doctrine" – the narrow construction of the national government's authority to delegate powers and immunities to private bankers. By broadly (albeit ambiguously) construing the immunities of the Bank of the United States, *McCulloch* ran up against this doctrine. As a result, it was a consistently marginalized decision until the Civil War – confusingly construed by lower courts, ignored by the U.S. Supreme Court, and despised by the Democratic Party, the dominant antebellum political organization.

#### A. Country Party fear of financiers' capturing the central government

The idea that high finance was inconsistent with the liberty of individual owners of property was a mainstay of so-called "Country Party" ideology, an interlocking set of British ideas about political economy developed in pamphlet literature between the "standing army controversy" of the late 1690s<sup>10</sup> and the South Sea Bubble of the early 1720s, a period in which England was developing its first sophisticated financial institutions like the Bank of England and a national debt. The occasion for this ideology was England's development of modern financial institutions – a public debt and a national bank – that seemed outside then power of England's squirearchy – the middling landed aristocrats outside of London – to control. During this quarter-century, a large pamphlet literature popularized the view that financial elites at the metropolitan center who purchased public bonds formed a corrupting class, manipulating the government to inflate the value of their paper holdings. This "paper aristocracy" of "fundlords" constituted a loyal cadre of support for the Crown, because they depended on the solvency of the government to re-pay the debts. The Crown could insure re-payment by using bond proceeds to bribe members of Parliament with lucrative executive "places" or offices in return for votes for taxes or monopolies profitable to bondholders. In general, the fear of "fundlords" and placemen

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<sup>10</sup> The occasion of the standing army controversy was King William III's efforts to fund a large peace-time army in the wake of the 1697 Treaty of Ryswick with France. Against this "standing army," an alliance of Old Whig opponents of the Stuarts and the Tory "country gentlemen" launched an attack between 1697-99 against the "Whig Junto" supporting William III. For a summary of this controversy, see Lois G. Schworer, *No Standing Armies! The Anti Army Ideology in Seventeenth-Century England* (1974).

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reduced to a more general fear that the modern state, requiring a specialized class of the financially astute, would deprive people of the capacity for independence and self-government.<sup>11</sup>

In theory, the small property holders' power to elect representatives to a unitary state could solve the problem of corruption by insuring that all public debt was examined for corrupt influence before the commitment to re-pay it was made by the state. But this solution would be ineffective if members of the Parliament themselves were corrupted by public creditors. The prospect of such corruption became the central theme of twelve dozen essays written by John Trenchard and Thomas Gordon between 1720 and 1723, collectively entitled *Cato's Letter* excoriated Parliamentary conflicts of interest during the scandal over the South Sea Company's financial collapse.<sup>12</sup> *Cato's Letters* became one of the most popular tracts in colonial North America<sup>13</sup> and the basis for much American revolutionary rhetoric against the British corporations like the East India Company.<sup>14</sup> Following the Revolution, westerners used Country Party rhetoric to challenge states' issuing charters to eastern corporations – in particular, banking corporations – invoking the danger of financial elites' corrupting politicians located on the

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<sup>11</sup> For examples of this rhetoric, see Jonathan Swift, *History of the last Four years* (1713) (“monied interest” opposed to “gentry of the kingdom”); Bolingbroke, *Reflections on the Present State of the Nation* (1749) (“Method of funding and trade of stock-jobbing” created “great companies” that were “the pretended servants, but in many respects the real masters of every administration”).

<sup>12</sup> The essence of the scandal was the joint-stock company's alleged bribing of government ministers and members of Parliament with stock in return for assistance in inflating the stocks' trading value. The company's value was based exclusively in the re-financing of public debt, as the Company re-financed £10 million of short-term public debt by securing a 6% annuity on this sum from the government and by persuading the private holders of the debt to exchange their government bonds for Company shares. The Company thereupon attempted with initial success to inflate the value of its stock through bribery of governmental officials and general spreading of rumors of secret governmental support.

<sup>13</sup> *Cato's Letters* were just a few of numerous tracts attacking alleged corruption from private access to public credit. But it was *Cato's Letters* that propelled Country Party ideology across the Atlantic to the North American colonies. For another prominent example, see Bolingbroke, *Craftsman* #5, Dec. 14<sup>th</sup>, 1726. Bernard Bailyn, *Ideological Origins of the American Revolution* 35-36 (1967)

<sup>14</sup> John Dickinson's *Essay on the Constitutional power of Great-Britain Over the Colonies in America* (1774) is representative of the anti-financier rhetoric that the colonists deployed against England. Dickinson's essay was attached by the Pennsylvania Committee of Correspondence to their instructions for the Pennsylvania Assembly as the moderate American revolutionary's understanding of the British Empire's constitution. In urging that the Pennsylvania Assembly rather than Parliament ought to be responsible for approving such a grant of money, the Committee observed that “[t]he attention of small states extends much more efficaciously and beneficially to every part of the territories, than that of the administration of a vast empire,” *Id.* at 21, note \*. because those “small states” detect and ferret out the corruption that an inattentive or corrupted Parliament ignores or even fosters. The leading examples of corruption are all the results of public finance familiar to the readers of *Cato's Letters* (the third of which the Committee cites): “Lending the crown at 8 per cent. Money which was raised at 5 or 6” or “[d]epreciating the public debts and funds, buying them of the holders at half their worth, and afterwards by interest getting them paid in full,” *Id.* at 23, n. \*. Continuing the theme of the corrupting power of public finance, the *Essay* argued that the liberties of England itself would be subverted by an imperial victory over the Americans, because “vast sums must be raised, and a prodigious army must be supported” for such a victory, creating an “influence” that would be “added to the power of the crown,” *Id.* at 58, note †, a point that Dickinson amplified in a footnote to the footnote by observing that it would generate Crown influence with the “immense revenue of almost seven millions sterling, which is annually paid to the creditors of the public.” *Id.* at 59-60, note ¶ to note †.

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Atlantic seaboard.<sup>15</sup> The antidote to capitalist domination of politics was a version of federalism -- either physical relocation of the state capital itself to small rural towns in the west<sup>16</sup> or enforcing what Dan Hulsebosch has called “the Marchland Constitution” -- that is, a localistic constitution basing title to land on occupancy and improvement and dispute resolution by a local jury.<sup>17</sup>

This western opposition to eastern banking corporations had its apogee in the successful opposition of western farmers to Pennsylvania Assembly’s chartering of the Bank of North America (the “BNA”). Led by William Findley, a “pugnacious Scotch-Irishman from western Pennsylvania” who embodied the westerners’ “middling aspirations, middling achievements, and middling resentments,”<sup>18</sup> the BNA’s western opponents resented Philadelphia financier Robert Morris’ proposal to pool large amounts of capital for investment by large-scale projects like mills or factories rather to give small farmers access to consumer credit.<sup>19</sup> But the legislative debates dripped with western anger that the bankers at the metropolitan center – in particular, Robert Morris, who embodied the elitism of financial sophisticates to his western opponents -- neglected the interests of the economic periphery on the western frontier.<sup>20</sup>

### [B. Opposition to a national power to charter banks in the ratification and early interpretation of the Constitution.](#)

The hostility to conferring powers on bankers located in distant major metropolises did not end with Morris’ defeat in 1786. The state-wide fight over the Bank of North America was merely a rehearsal for a continental struggle over whether the Constitution proposed by the

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<sup>15</sup> Pauline Maier, *The Revolutionary Origins of the American Corporation*, 50 Wm. & Mary Q. 51, 66-72 (1993). Unlike modern corporations formed under general legislation, 18<sup>th</sup> century corporations were individually chartered by the legislature and usually enjoyed some sort of monopoly as an inducement for investment. These sorts of special privileges inspired standard Country Party anxieties that well-connected insiders were reaping benefits from the legislature at the people’s expense.

<sup>16</sup> For a description of this struggle, see Rosemarie Zagarr, *The Politics of Size: Representation in the United States, 1776-1850*, at 8-35.

<sup>17</sup> In New York, Dan Hulsebosch has acutely distinguished between the “Marchland Constitution” of settlers who migrated towards the interior of the state and the “provincial constitution of improvement” embraced by the Anglo-Dutch elite of New York City. The latter rested their case on independence on the concept of a charter as a form of common-law property right (New York City having been granted the Montgomerie Charter of 1730 by New York’s royal governor). Daniel Hulsebosch, *Constituting Empire: New York and the Transformation of Constitutionalism in the Atlantic World, 1664-1830*, at 83-96(2005). The Marchland Constitution, by contrast, rested on natural rights of migration, title through possession and improvement, and local control protected by jury trial and the less formal but equally effective mechanism of the mob. *Id.* at 96-104.

<sup>18</sup> Gordon S. Wood, *Interests and Disinterestedness in the Making of the Constitution*, in *Beyond Confederation: Origins of the Constitution and American National Identity* 69, 94 (Richard Beeman, Stephen Boteihn, & Edward C. Carter II eds. 1987).

<sup>19</sup> On Robert Morris’ plan to pool capital with a permanently funded debt, see Janet A. Riesman, *Money, Credit, and Federalist Political Economy* in *id.* at 128, 147-48.

<sup>20</sup> The debate is available in *Debates and Proceedings of the General Assembly of Pennsylvania ....* (Mathew Carey ed. 1786).

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Philadelphia Convention should be construed to give Congress the implied power to charter corporations.

A substantial segment of the loose coalition opposing the ratification of this document, known as “Anti-Federalists,” were located further from centers of, and less deeply involved in, international trade, than the Constitution’s supporters.<sup>21</sup> Their ideological objection to the Constitution tended unsurprisingly to follow the Country Party script: By conferring power on a metropolitan elite of “natural aristocrats,” the Constitution would deprive persons farther from centers of power of genuinely democratic control.<sup>22</sup> The Anti-Federalist insistence on limiting national power, to this extent, was a rehash of the westerners’ position in the 1786 debates over the Bank of North America. Indeed, William Findley, the leader of the western Pennsylvanians’ opposition to Robert Morris, was also a leading Anti-Federalist opponent of the proposed Constitution, once more arguing that supporters of a strong national government were rooted in the financial class in big cities like Philadelphia —“the *speculating order* in the towns where they have the greatest influence....”<sup>23</sup>

To Anti-Federalists in the west, “states’ rights” was, in large part, merely an instrument for controlling financial elites presumed to be dominant at the metropolitan centers of the new continental government. The Anti-Federalist theory, often repeated throughout the ratification debates, was that money and reputation talked loudest to large populations that could not be canvassed personally.<sup>24</sup> The Anti-Federalists, therefore, strongly opposed giving the national government a power to charter corporations, on the theory that the national government would be elected by larger constituencies over which financial elites would have the greatest influence. To avoid antagonizing westerners, “Federalist” supporters of the proposed U.S. Constitution deliberately refrained from saying anything explicit on the topic of Congress’ power to charter corporations. When Madison proposed such an express corporation-chartering power at the Philadelphia convention, he was warned by his fellow Federalists that clarity on Congress’ power over corporations would simply antagonize western farmers, and the proposal was dropped.<sup>25</sup>

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<sup>21</sup> Jackson Main, *Political Parties Before the Constitution* 358, 388 (1973) (noting that Anti-Federalists tended to be “agrarian-localist” rather than “commercial cosmopolitan” leaders). Donald Lutz notes that Main’s anti-cosmopolitan explanation for Anti-Federalist opposition to the Constitution cannot explain the Constitution’s support among the inhabitants in some key frontier areas of the states. See Donald S. Lutz, *Federalist versus Antifederalist* in *Popular Consent and Popular Control: Whig Political Theory in the Early State Constitutions* 171, 175-86 (1980).

<sup>22</sup> James H. Hutson, *Country, Court, and Constitution: Antifederalism and the Historians*, 38 *Wm. & Mary Q.* 337, 340 (1981)

<sup>23</sup> A Citizen [William Findley], *Review of the Revenue System* at 12-13.

<sup>24</sup> For an overview of both the argument based on size of electoral districts and the frequency with which Anti-Federalists made it, see Saul Cornell, *The Other Founders*

<sup>25</sup> In response to Madison’s September 14<sup>th</sup> proposal “to grant charters of incorporation where the interest of the U. S. might require & the legislative provisions of individual States may be incompetent,” Rufus King, the Massachusetts ally of Alexander Hamilton, argued that “[t]he States will be prejudiced and divided into parties by [an express power to charter corporations] and reminding the Convention of the controversies over the Bank of North America by observing that “[i]n Philad[elphia] & New York, It will be referred to the establishment of a Bank,

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Despite their rejection of a corporation-chartering power as part of Article I's express enumeration, the Federalists pressed the power to charter a bank as an implied power of Congress almost immediately after ratification, when Alexander Hamilton proposed that the Congress confer a federal charter on the First Bank of the United States. The First Bank raised all of the Country Party fears about financiers' influencing government for private gain: Private investors would own 80% of the bank's shares, and the bank would enjoy the exclusive privilege of holding deposits of federal revenue without paying interest, using the revenue as security to make loans and create a *de facto* federal currency through such commercial paper. The proposal immediately mobilized old Anti-Federalist opponents of the Constitution suspicious of congressional support for large-scale finance. The Anti-Federalists' opposition was supported by three leading Virginian politicians' written legal opinions – a speech by James Madison (in the House of Representatives) and memos by Edmund Randolph (President Washington's Attorney General) and Thomas Jefferson (Washington's Secretary of State).<sup>26</sup> The gist of all three was that including the power to charter banks among the implied powers of Congress would destroy “the essential characteristic of the Government, as composed of limited and enumerated powers.”<sup>27</sup> Behind this general legal point, however, was an ideological and sectional motivation unmentioned in the legal arguments: Southerners in under-capitalized states like Virginia were opposing what they took to be special privileges for finance capitalists concentrated in the Northeast and Mid-Atlantic states. Unsurprisingly, the speeches in opposition to Madison all came from New England and Mid-Atlantic representatives (Fisher Ames, Elbridge Gerry, and Theodore Sedgwick, all of Massachusetts and Elias Boudinot of New Jersey). The debate over the First Bank of the United States was so tied up with long-standing pre-constitutional struggles over agrarian opposition to financiers that Jefferson later erroneously recollected that support for a corporation-chartering power at the Philadelphia Convention came from Robert Morris, the Philadelphia financier backing the BNA, rather than the actual proponent, James Madison, who

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which has been a subject of contention in those Cities. In other places it will be referred to mercantile monopolies.” When James Wilson, a Philadelphia Federalist who had supported the re-chartering of the Bank of North America, confidently asserted that federal banks would not “excite the prejudices & parties apprehended” and that “mercantile monopolies” were “already included in the power to regulate trade,” George Mason of Virginia, one of the few Anti-Federalists present at the Philadelphia Convention, quickly put him on notice that Country Party fears of banks and “mercantile monopolies” was alive and well, noting that “[h]e was afraid of monopolies of every sort, which he did not think were by any means already implied by the Constitution as supposed by Mr. Wilson.” Madison's proposal to grant Congress a power to charter corporations was thus quickly defeated in apprehensions that it would be the basis for a rehearsal of the fracas over the Bank of North America.<sup>26</sup> Jefferson's legal opinion can be found at 19 papers of Thomas Jefferson 275, 279-80 (1974). Randolph's opinion can be found in H. Jefferson Powell, *The Constitution and the Attorneys General* 3-9 (1999). Madison's speech on the floor of the House can be found in James Madison, *Writings* 480-490 (Jack Rakove ed. 1999). For a general account of the debate, see Stanley Elkins & Eric McKittrick, *The Age of Federalism: The Early American Republic, 1788-1800*, at 229-234 (1993).

<sup>27</sup> James Madison, at \_\_\_\_\_. In Jefferson's words, “to take a single step beyond the boundaries thus specially drawn around the powers of Congress is to take possession of a boundless field of power, no longer susceptible of definition.”

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was a nationalist back in 1787, converting to Jefferson's and Virginia's agrarian and localist cause only in 1791.<sup>28</sup>

Although the first Bank of the United States was eventually ratified by Congress over Jefferson's and Madison's opposition, Jefferson and Madison mobilized a "Democratic Republican" political party that was, in substantial part, devoted to the position that the First Bank of the United States was unconstitutional. That position was not merely an abstract interpretative position about "states' rights" divorced from an economic ideology. It was, instead, a byproduct of sectional opposition to high finance – in Madison's bitter phrase, "speculators and Tories."<sup>29</sup> "States' rights" was an antidote to the power of finance, simply because Jeffersonian republicans believed in the old Anti-Federalist theory that politicians elected from smaller constituencies would be less prone to the influence of "stockjobbers."<sup>30</sup>

### C. *McCulloch's* ambiguous and embattled defense of nationally chartered banks' immunity from state law

*McCulloch v. Maryland* could be viewed as the Federalist repudiation of the Anti-Federalist and Democratic Republican idea that state governments must control banks to prevent financiers from subverting democracy. *McCulloch* indeed endorses the idea of banks' immunity from state law. But, as explained below, *McCulloch* pulls its punches: Its brand of bank immunity was equivocal and ambiguous, expressly preserving state power over those "resources which [the states] originally possessed" while barring state control of those resources contributed by the Union as a whole. Malleable and muddy, this distinction allowed state courts to sidestep the doctrine. Despite the feebleness of *McCulloch's* immunity, the idea of insulating private banks from state regulation nevertheless inspired so much hostility from the Democratic

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<sup>28</sup> Jefferson later recounted hearing from Baldwin that it was Robert Morris who proposed conferring on Congress the power to charter a national bank, to which Gouverneur Morris, his ally and fellow Federalist, was supposed to have objected on the ground that

"it was extremely doubtful whether the constitution they were framing could ever be passed at all by the people of America; that to give it its best chance, however, they should make it as palatable as possible, and put nothing into it not very essential, which might raise up enemies; that his colleague (Robert Morris) well knew that 'a bank' was, in their State (Pennsylvania) the very watch-word of party; that a bank had been the great bone of contention between the two parties of the State, from the establishment of their constitution, having been erected, put down, and erected again, as either party preponderated; that therefore, to insert this power, would instantly enlist against the whole instrument, the whole of the anti-bank party in Pennsylvania."

T. J. Randolph, Memoir, 4 Correspondence...of Thomas Jefferson 506-507. Jefferson's substitution of Robert Morris for Jefferson's own ally, James Madison, only highlights the degree to which the corporation-chartering power was closely associated with the 1786 debate over the Bank of North America.

<sup>29</sup> See Elkins & Mckitrick, *The Age of Federalism*, at 234.

<sup>30</sup> On the centrality of hostility to speculation in federal bonds in Jefferson's and Madison's opposition to the Federalist Party, see Elkins & Mckitrick, *Age of Federalism* at 243-44.

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Congress and Presidents and the U.S. Supreme Court appointed by both that the doctrine lapsed into desuetude until the Civil War.

### *1. Opposition to the Second Bank of the United States*

By the time that the charter of the First Bank expired in 1811, Republican opposition to the general idea of a nationally chartered bank had softened. Madison was willing to concede that the question of the Bank's constitutionality had been settled by political precedent,<sup>31</sup> and the extinction of the Federalist Party had eliminated a source of organized partisan polarization over finance.<sup>32</sup> Accordingly, mainstream Democrats led by Calhoun in the House of Representatives granted the Second Bank of the United States a charter in 1816 without the fierce constitutional controversy of 1791.<sup>33</sup>

The Bank, however, soon became the victim of ferocious economic controversy, when deflating agricultural prices helped pop a bubble in land values, a bubble that had been inflated, in part, by the Bank's various branch offices' issuing excessive amounts of paper.<sup>34</sup> In the case of the Baltimore branch, the branch officers had engaged in outright corruption in issuing loans. When the Bank finally called in loans in late summer of 1818, the contraction helped sparked a series of bankruptcies and defaults that eventually become the Panic of 1819. The appointment of South Carolina's Langdon Cheves as Bank President to replace the disgraced William Jones in January of 1819 did not end the bank's policy of contraction, for Cheves' charge was to clear the Bank's books of questionable loans by placing the Bank's paper on a safe and sound ratio of loans to specie reserves.

The predictable reaction of state politicians was to denounce the Bank for depriving under-capitalized areas in the South and West of currency and rendering debtors incapable of paying off their loans. The Maryland tax at issue in *McCulloch v. Maryland* was a product of this hostile reaction to the Bank's contraction of credit. Although a facially neutral exaction imposed on all banks not chartered by the Maryland legislature, the tax was obviously a thinly disguised burden imposed only on the Second Bank of the United States by a state legislature incensed by allegations of corruption in the Baltimore branch. Three months' into Cheves' tenure as Bank President, when politicians' hunt for the Bank and its role in the Panic was in full

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<sup>31</sup> Letter to Mr. [Jared] Ingersoll, June 25, 1831.

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<sup>33</sup> The Bank's charter passed in the House of Representatives by a vote of 80 to 71 and, in the Senate, by a vote of 22 to 12, with the opposition in both cases coming from an odd alliance of New England Federalists led by Daniel Webster and "Tidewater Republicans" led by Virginia's John Randolph. Norman Gasque Raiford, *South Carolina and the Second Bank of the United States: Conflict in Political Principle or Economic Interest?* 72 S.C. Hist. Mag. 30, 31 (1971). "Tidewater Republicans" like Randolph opposed the Bank because of their austere narrow view of the Congress' powers and deep distrust of financial or mercantile elites who they believed corrupted national politics. Norman K Risjord, *The Old Republicans: Southern Conservatism in the Age of Jefferson*. The New England Federalists' opposition, however, was wholly inexplicable in terms of constitutional or economic principles and seems to be the last gasp of partisan opposition to a Southern and Democratic measure.

<sup>34</sup> On declining commodity prices' contribution to the Panic of 1819, see Clyde Haulman, *Virginia Commodity Prices during the Panic of 1819*, 22 J. Early Republic 675 (2002).

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cry, Chief Justice John Marshall announced the opinion insulating the Bank from state control for a unanimous Court in *McCulloch v. Maryland*.

### *2. McCulloch's supremacy-based theory of bank immunity from state law*

The Court's holding that the Bank was immune from Maryland's tax on its deposits could not have been better calculated to trigger Country Party apprehension that the Bank represented the capture of democratic government by financial elites. *McCulloch* reasoned that the Bank was an agent of the federal government – in his words, the “the means employed by the Government of the Union, in pursuance of the Constitution”<sup>35</sup> – despite the fact that the federal government did not, in fact, control the President of this private institution who was answerable only to the Bank's mostly private board of directors. For *McCulloch*, the Bank counted as a *de facto* federal agency because it acted as the federal government's exclusive fiscal agent, entitled to use federal revenue deposited in its vaults for private banking ventures such as redeeming state bank notes and thereby limiting the supply of paper currency. Such an argument, in the eyes of the Bank's Country Party opponents was perverse: It promoted private “stockjobbers” to the status of governmental officials immune from the states' democratic oversight on the perverse ground that they enjoyed exclusive privileges as a federal agent, even though the Bank was not directly controlled by the President or Congress. As one state court judge characterized the view of the Bank in the eyes of its opponents, “this is a great monied monopoly, which, in the hands of the General Government, will become a gulph in the *vortex* of which, every minor institution will be swallowed up.”<sup>36</sup>

*McCulloch's* reasoning implied that, despite being controlled by private financiers, the resources of the Bank – primarily, revenue produced by taxes, customs, receipts gathered by the federal government various tax receipts of the federal revenue were just as much beyond state control as the letters controlled by a federal postmaster, the customs receipts held by a customs official, or the damages won by a U.S. Attorney, because they were the product of the collective effort of the entire nation. “Those means are not given by the people of a particular State, not given by the constituents of the legislature which claim the right to tax them,” *McCulloch* reasoned, “but by the people of all the States. They are given by all, for the benefit of all -- and, upon theory, should be subjected to that Government only which belongs to all.”<sup>37</sup>

Taken literally, this theory of supremacy implied that the nationally chartered Bank should be immune not only from state taxation but also every other sort of state law – contract, tort, property, criminal, etc. In *McCulloch's* words, “the States have no power, by taxation *or otherwise*, to retard, impede, burden, or in any manner control the operations of the constitutional laws enacted by Congress to carry into execution the powers vested in the General

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<sup>35</sup> *McCulloch*, at 430.

<sup>36</sup> *Bulow v. City of Charleston*, 1 Nott & McC. 527 (Ct. App. 1819).

<sup>37</sup> *McCulloch*, at 429-30.

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Government.”<sup>38</sup> Such a literal reading, however, would make the Bank a law unto itself, as there was no federal code of tort, contract, crimes, or property to which its operations would otherwise be subject if state law were preempted.<sup>39</sup> *McCulloch*’s theory of immunity would plainly have to be constrained as a practical matter, regardless of *McCulloch*’s logical implications.

### 3. *McCulloch’s preservation of state power over “resources which [the states] originally possessed”*

*McCulloch*’s penultimate paragraph offered three confusing sentences that promised such constraint on its theory of bank immunity:

This opinion does not deprive the States of any resources which they originally possessed. It does not extend to a tax paid by the real property of the bank, in common with the other real property within the State, nor to a tax imposed on the interest which the citizens of Maryland may hold in this institution, in common with other property of the same description throughout the State. But this is a tax on the operations of the bank, and is, consequently, a tax on the operation of an instrument employed by the Government.<sup>40</sup>

This passage describes two permissible taxes (on the bank’s real property and on bank stock owned by private citizens), but it does not explain the basis for these taxes’ permissibility. One can safely infer from *McCulloch*’s emphasis that the taxes must be “imposed” on assets associated with the Bank “in common with other property of the same description throughout the State” that such permissible taxes must not discriminate against the federal government.

Non-discrimination against the federal government, however, cannot be a sufficient criterion to exempt state laws from *McCulloch*, because *McCulloch* adamantly declares that “the States have no power ... to ... *in any manner* control the operations of the constitutional laws enacted by Congress.” Such a categorical declaration seemed to leave little room for even a non-discriminatory tax on both state- and federal-chartered banks’ deposits, for surely such a tax would still “control the operations” of the nationally chartered bank. Ten years after *McCulloch*, Marshall confirmed that the non-discriminatory character of a state law did not suffice to satisfy

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<sup>38</sup> *McCulloch*, at 436 (emphasis added).

<sup>39</sup> Given *McCulloch*’s theory of immunity, state law would not apply to the Bank in federal court under section 34 of the 1789 Judiciary Act. Section 34 of the Judiciary Act of 1789, 1 Stat. 73, provided that “the laws of the several states, except where the constitution, treaties or statutes of the United States shall otherwise require or provide, shall be regarded as rules of decision in trials at common law in the courts of the United States in cases where they apply.” But *McCulloch* obviously declared that “the constitution ... shall otherwise require” that state laws *not* “be regarded as the rules of decision.” Under *Osborn v. Bank of the United States*, 22 U.S. (9 Wheat.) 738 (1824), federal courts could exercise “arising under” jurisdiction over disputes involving nationally chartered corporations and fashion rules of general common law pursuant to *Swift v. Tyson*, 41 U.S. 1 (1842) in cases involving disputes arising out of the Bank’s commercial transactions. But there was no federal common law of crimes: Was the Bank simply to be regarded as an imperio in imperium, governed neither by federal nor state law but instead only its own directors’ fiat, when it committed criminal fraud?

<sup>40</sup> *Id.*

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the demands of federal supremacy in *Weston v. City of Charleston*.<sup>41</sup> *Weston* held that the U.S. Constitution's principle of supremacy barred the City of Charleston from imposing a tax on all interest-bearing obligations, expressly including but not limited to certain bonds issued by the United States, even though, as Justice Johnson pointed out in dissent, the City's tax did not discriminate against the federal government.<sup>42</sup> The city tax was nonetheless forbidden, because, however non-discriminatory, it was nevertheless deemed to be a tax on the federal government's express Article I borrowing power.<sup>43</sup> By the same logic, a non-discriminatory tax on the bank's "operations" would also be an impermissible burden on the federal government's implied lending power. But, if non-discrimination was not sufficient to save a state law, then why were state taxes on the Bank's real estate or private citizens' Bank shares permissible?

The critical criterion is supplied by *McCulloch*'s concept of "resources which [the state governments] originally possessed." *McCulloch* explicitly declares the intention of preserving state control over such resources, defined as those sources of wealth not contributed by the collective efforts of the entire union but rather existing within the state independent of the federal government. Even absent the creation of the Bank, states would contain land and people. State law, therefore, did not control the operations of the Bank by asserting power over such land and people. When federal agencies like the Bank purchased real estate or sold shares of stock within a state, they took the private property rights to the seller's land or buyer's payment as they found them – defined by state law. In *Weston*'s characterization of *McCulloch*'s dicta, "property acquired by that corporation in a state was supposed to be placed in the same condition with property acquired by an individual." By contrast, state taxation of federal tax revenue or federal bond proceeds tapped a source of wealth that would not exist but for the special collective effort of the entire union – either the effort of bearing federal taxes or the pledge of the union's full faith and credit. As *Weston* puts it, "[t]he tax on government stock [*i.e.*, proceeds from sales of federal bonds] [was] thought by this Court to be a tax on the contract, a tax on the power to borrow money *on the credit of the United States*, and consequently to be repugnant to the constitution."<sup>44</sup>

In sum, there were two criteria for an acceptable state tax. First, the tax must not discriminate against the federal government; second, the tax must not be imposed on wealth

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<sup>41</sup> 27 U.S. (2 Pet.) 449 (1829).

<sup>42</sup> According to Justice Johnson, Charleston's exemption of "state stock, city stock, and stock of their own chartered banks" from the otherwise generally applicable tax could be explained by the state's desire not to impair the obligation of its own contracts or violate the immunity conferred on the state-chartered bank by the state legislature, and the good faith of the city could be inferred from its exemption of the stock of the Bank of the United States. The express specification of six and seven percent bonds, according to Justice Johnson, although "most clumsily worded," was simply an avoidance of "unequal and unjust" taxation of federal bonds bearing a lower interest rate. *Weston* at 472-73 (Johnson, J., dissenting).

<sup>43</sup> According to *Weston*, the Charleston tax was as "a tax upon the contract subsisting between the government and the individual" and, "bear[ing] directly upon that contract," because such a tax "operates upon the contract the instant it is framed, and must imply a right to affect that contract." In other words, although the tax was paid by a private bondholder, it was imposed on the federal government's act of borrowing money – in effect, a tax on one of "the various operations of government." *Id.* at 465.

<sup>44</sup> *Id.* at 469 (emphasis added).

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created by the union but rather be imposed only on wealth falling within the “original” possession of the states. For Marshall, this juridical effort to divide up the resources within the territory of the United States between state and federal governments was a salubrious way to avoid conflict. “[W]e have an intelligible standard, applicable to every case to which the power may be applied,” Marshall exulted with relief: “We are relieved, as we ought to be, from clashing sovereignty; from interfering powers; from a repugnancy between a right in one Government to pull down what there is an acknowledged right in another to build up; from the incompatibility of a right in one Government to destroy what there is a right in another to preserve.”<sup>45</sup>

One does not need to be a 20<sup>th</sup> Century Legal Realist, however, to see that Marshall’s distinction between “wealth created by the union” and the states’ “original” wealth rests on a legerdemain of what Daryl Levinson has called “constitutional framing.”<sup>46</sup> As counsel in *Weston* noted, all of the land contained in states formed after the ratification of the Constitution was once owned by the federal government as part of the public domain: Why were not all state taxes on real estate within such states an invasion of wealth created by the federal government? Chief Justice Marshall brushed this *reductio ad absurdum* aside by noting that the federal government did not continue to hold federal land after it is auctioned off to private citizens, whereas the federal government does maintain long-term relationships with federal bondholders until the bonds mature. But this response seems like a *non sequitur*: Why cannot the feds take credit for creating the states that entered the union after ratification? Such states, after all, had no “original” resources until brought into existence by a federal statute.

The distinction between state’s “original” resources and wealth created by the nation, then, could unravel as soon as one extended the “frame” within which one defined the beneficial effects of federal law. The arbitrariness of these lines is well-illustrated by the Taney Court’s decision in *Dobbins v. Commissioners of Erie County*<sup>47</sup>, in which the Court held that the income of a captain of a U.S. Revenue Cutter was exempt from a county tax imposed on “all offices and posts of profit.” The Counsel for the County noted that, unlike a hypothetical “tax upon the hull and apparel of the revenue-cutter,” the tax on Captain Dobbins’ income could be viewed as simply a tax on one of Erie County’s private citizens.<sup>48</sup> The federal government did not create Captain Dobbins, after all, even if the feds created his ship: Why was his labor not part of those “resources... which [the states] originally possessed” under *McCulloch*? But *Dobbins* reasoned that Congress appropriated the money that paid Dobbins’ salary: Taxing that salary would, therefore, vary the compensation of federal officers, affecting the operations of a federal statute. In *Dobbins*’ words, “the officer, as such” is no “less a means to carry into effect these great objects than the vessel which he commands, the instruments which are used to navigate her, or the guns put on board to enforce obedience to the law.” If “[t]hese inanimate objects ... cannot

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<sup>45</sup> *McCulloch* at 429-30.

<sup>46</sup> Daryl J. Levinson, *Framing Transactions in Constitutional Law*, 111 Yale L.J. 1311 (2002).

<sup>47</sup> 41 U.S. 435 (1842).

<sup>48</sup> 41 U.S. at 443.

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be taxed by a state, because they are means,” then the officer should also not be taxed.<sup>49</sup> Such reasoning invited formalistic distinctions between salaries that were directly defined by Congress by law and federal employees’ income that was not so specifically defined.<sup>50</sup>

Chief Justice Marshall had hoped that his efforts to divide the resources within the United States between state and federal governments would avoid fractious conflict over turf. “We are not driven to the perplexing inquiry, so unfit for the judicial department,” Marshall optimistically declared, “about what degree of taxation is the legitimate use and what degree may amount to the abuse of the power.” But *McCulloch*’s two-part test for federal agencies’ tax immunity turned out to be easy enough for lower courts to manipulate, if they were so inclined. At the same moment that *McCulloch* was being hand down, the South Carolina court of appeals upheld a tax imposed by the City of Charleston on all bank shares the taxation of which was not barred by the South Carolina legislature.<sup>51</sup> The state court overlooked the blatantly discriminatory character of the tax, apparently finding its facial neutrality sufficient. As for taxing the resources of the federal government, it was easy enough for the court to note that the tax applied only to shares owned by private citizens and not the federal government.<sup>52</sup> The dissent from Justice Abraham Nott, a former Federalist representative to the Sixth Congress who was thrown out of office when Jefferson was elected in 1800, suggested the partisan character of the decision. South Carolina again undermined *McCulloch* in 1832 when, in the throes of the Nullification crisis, Justice William Harper (fresh from serving in the South Carolina Nullification Convention) upheld a 1% tax imposed by the state legislature on “all dividends arising from stock, owned by any citizen of this State, in all banks not chartered by this State.” Although the tax again blatantly singled out the Second Bank of the United States (to which it exclusively applied), the state court reasoned that the state law was non-discriminatory because it was written “in general terms.” “If there be a peculiar species of property, owned only by a few individuals in a State,” Justice Harper stated with unflappable insouciance, “there is no reason why the legislature should not tax that as well as property which is more common: and circumstances may justify the taxing it more highly.”<sup>53</sup>

By 1832, *McCulloch*’s concept of bank immunity was in shambles, assaulted by angry Southerners no longer sympathetic to the nationalist project of the Bank. The immunity created by these doctrines inevitably was in tension with Country Party sentiment, because it inevitably created (in Thompson’s words) “a privileged class of public creditors, who, though living under

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<sup>49</sup>41 U.S. at 448.

<sup>50</sup>*Melcher v. City of Boston*, 50 Mass. 73 (1845), for instance, held that Boston *could* tax the income of a federal postal clerk, distinguishing *Dobbins* on the thin ground that the “office” of a revenue cutter captain, whereas “the act regulating the post office department, does not, in terms, create any such office.” 50 Mass. at 77.

<sup>51</sup>*Bulow v. City of Charleston*, 1 Nott & McC. 527 (Ct. App. 1819).

<sup>52</sup>In *Bulow*’s phrase, “the interest of the United States and the individual stockholders are distinct and independent.”

<sup>53</sup>*Tax Collector of St. Phillips & St. Michaels*, 18 S.C.L. 678.

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the protection of the government, are exempted from bearing any of its burthens.”<sup>54</sup> Bondholders and banks were hardly sympathetic figures in American political culture, and *McCulloch*’s immunity for both rankled, even as limited by *McCulloch*’s efforts to cabin the immunity by protecting the states’ “original” resources.

### D. Andrew Jackson’s antebellum burial of *McCulloch*

Southern opposition to *McCulloch* was nothing new: Virginians in Thomas Ritchie’s “Richmond Junto” had decried the doctrine at its birth in 1819<sup>55</sup> and South Carolinians had nullified it along with the Tariff of Abominations” in 1832. Southern opposition, however, was only loosely linked to the Country Party tradition of anxieties over domination by financial elites: Elite Southern plantation owners were moved just as much by purely sectional anxieties about slavery or Northern commercial power.<sup>56</sup>

Using Country Party rhetoric, Andrew Jackson would transform this essentially Southern movement against the Bank into a nationally dominant political party driven by his anti-elitist manifesto for the sake of popular sovereignty. Jackson made no secret of his borrowing from the old Country Party theory, in which he played the role of Bolingbroke’s “Patriot King” and the “Monster Bank” playing the role of the South Sea Company. “I do not dislike your Bank any more than all banks,” Jackson informed Nicholas Biddle in his famous rehearsal of Country Party rhetoric, “[b]ut ever since I read the history of the South Sea Bubble I have been afraid of banks.”<sup>57</sup> As Saul Cornell documents, Martin Van Buren, the architect of the Jacksonian party, self-consciously invoked the “Anti-Federalist Mind” as the basis for the Democratic Party’s ideology.<sup>58</sup> Between 1832 and 1861, this Country Party theme became the trademark rhetoric of the Democratic Party, which self-consciously styled itself as the defender of constitutional

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<sup>54</sup> *Weston*, at 480. Johnson used similar terms in decrying the Bank’s immunity as a cloak for wealthy coupon clippers: “why should one who enjoys all the advantages of a society purchased at a heavy expense, and lives in affluence upon an income derived exclusively from interest on government stock, be exempted from taxation?”

<sup>55</sup> It was greeted with indignant responses from the so-called “Richmond Junto” of Thomas Ritchie, Spencer Roane, and William Brockenbrough, all of whom wrote articles against *McCulloch* to which Marshall pseudonymously responded.

<sup>56</sup> Ritchie and his clique, for instance, stood for the “traditional system of planter elite domination” in eastern Virginia. William G. Shade, *Democratizing the Old Dominion: Virginia and the Second Party System, 1824-1861*, at 84. Indeed, some members of the Junto were deeply invested in a commercial system of exclusive commercial privileges: John Brockenbrough, brother of William, one of Marshall’s opponents on the Virginia supreme court, was the head of the state-chartered Bank of Virginia and managed a network that maintained state banknotes at par and mimicked the contractionist policy of the Bank of the United States at the state level. See John M. McFaul, *The Politics of Jacksonian Finance* 21 (1972). Ritchie and Brockenbrough opposed Jackson’s policy of “hard-money” radicalism that would limit the power of banks to issue paper and thereby affect the supply of currency. See Larry Schweikart, *Banking in the American South from the Age of Jackson to Reconstruction* 35-37 (1987)

<sup>57</sup> John Spencer Bassett, 2 *Life of Andrew Jackson* 599-9 (1911).

<sup>58</sup> Saul Cornell, *The Other Founders: Anti-Federalism and the Dissenting Traditional in American, 1788-1828*, at 299-300 (1999).

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federalism against a “paper aristocracy” of financial elites.<sup>59</sup> Democrats in the state legislature, for instance, voted on corporate charters and banking issues in ways consistently different from, and much more hostile than, Whigs.<sup>60</sup> Likewise, voters further from metropolitan centers where finance capital was concentrated seemed especially amenable to the Jacksonian message.<sup>61</sup>

By vetoing the re-chartering of the Second Bank of the United States, Jackson fundamentally re-directed the platform of the Democratic Party to focus on the evils of federal aid to private corporations. Central to this platform was what I call the “anti-banker non-delegation doctrine.” Jackson’s essential position was that congressional delegations of power, revenue, and immunities to private corporations like the Second Bank of the United States (“the Bank”) should be subjected to what we would call in modern constitutional parlance “strict scrutiny”: Unless absolutely necessary, such privileges should be deemed to fall outside Congress’ Article I implied power to adopt means necessary and proper for execution of express powers. According to Jackson’s veto message, the federal charter’s various grants of exclusive privileges to the Bank were improper, because they were not strictly “necessary” for any legitimate federal policy beyond enriching the bank’s investors.<sup>62</sup> In particular, Jackson objected to the Congress’ granting the bank exclusive banking privileges in Washington, D.C.,<sup>63</sup> an exclusive role as the federal government’s fiscal agent, and a special tax exemption not enjoyed by state-chartered banks. “It cannot be ‘necessary’ or ‘proper,’” President Jackson complained in his veto message, “for Congress to barter away or divest themselves of any of the powers -- vested in them by the Constitution to be exercised for the public good.... This restriction on themselves and grant of a monopoly to the bank is therefore unconstitutional.”<sup>64</sup>

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<sup>59</sup> Joel H. Silbey, *The American Political Nation, 1838-1893*, at 81-86 (1991); Gerry Leonard, *The Invention of Party Politics: Federalism, Popular Sovereignty, and Constitutional development in Jacksonian Illinois* (2002). Democrats in the state legislature, for instance, voted on corporate charters and banking issues in ways consistently different from, and much more hostile than, Whigs,<sup>51</sup> and voters further from metropolitan centers seemed especially amenable to the Jacksonian message.<sup>52</sup>

<sup>60</sup> Herbert Ershkowitz & William G. Shade, *Consensus or Conflict?: Political Behavior in the State Legislatures during the Jacksonian Era*, 58 *J. Am. Hist.* 598-621 (1971).

<sup>61</sup> James Rogers Sharp, *The Jacksonians versus the Banks: Politics in the States after the Panic of 1837*.

<sup>62</sup> In Jackson’s words, “many of the powers and privileges conferred on it cannot be supposed necessary for the purpose for which it is proposed to be created, and are not, therefore, means necessary to attain the end in view, and consequently not justified by the Constitution.” President Jackson’s Veto Message Regarding the Bank of the United States, July 10, 1832, in *A Compilation of the Messages and Papers of the Presidents Prepared under the direction of the Joint Committee on printing, of the House and Senate Pursuant to an Act of the Fifty-Second Congress of the United States* \_\_\_, \_\_\_ (New York: Bureau of National Literature, Inc., 1897)

<sup>63</sup> Jackson’s message devotes special hostility to the provisions “declar[ing] that Congress shall not increase the capital of existing banks, nor create other banks with capitals exceeding in the whole \$6,000,000” for a term of fifteen years. “The Constitution declares that Congress shall have power to exercise exclusive legislation over this District ‘in all cases whatsoever,’ and this act declares they shall not,” Jackson complained: “Which is the supreme law of the land? This provision cannot be ‘necessary’ or ‘proper’ or constitutional unless the absurdity be admitted that whenever it be “necessary and proper ” in the opinion of Congress they have a right to barter away one portion of the powers vested in them by the Constitution as a means of executing the rest.” *Id.* at \_\_\_

<sup>64</sup> *Id.* at \_\_\_

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Unlike the Southern opposition to the Bank, which was largely rooted in a desire to prevent federal state-building,<sup>65</sup> Jackson's objection was not so much that the Congress was exercising *too much* power over banking as that the Congress was not exercising *enough* power: By delegating exclusive privileges for a 15-year period to a single private corporation, Congress was abdicating its responsibility to exercise oversight over self-interested private actors. Jackson's theory, in other words, was not a decentralization theory but rather a non-delegation theory. As a continuation of the Country Party tradition of suspicion towards financial elites, such a non-delegation theory was fundamentally similar to Findley's 1786 opposition to the Bank of North America.<sup>66</sup>

Such an anti-delegation theory required the federal government either actively to supervise the banks or step out of the way to allow state governments to do so. Such a theory could lead the Jacksonians to *enlarge* the federal government's regulatory capacity to insure that unsupervised power was not delegated away to private bankers. For instance, the "pet bank" policy adopted by Levi Woodbury, Taney's successor at the Department of the Treasury, forced the national government's "hard money" agenda on private banks by (for instance) making eligibility to receive federal deposits conditional on the banks' not issuing of bank notes in small denominations.<sup>67</sup> Replacing "pet banks" with the "independent Treasury system," President Van Buren also strengthened federal control of federal revenue by delegating to six federal agencies the duty of holding federal revenue without the power either to lend it themselves or to deposit it in state-chartered banks for private lending.<sup>68</sup>

Giving state governments control over the banking business was simply an alternative mechanism by which to insure that bankers were subjected to some government not beholden to bankers themselves. State-chartered banks, as bad as they were, were at least outside the power of the "great capitalists" like Nicholas Biddle<sup>69</sup> (believed by Jacksonians to have special influence over federal legislators like Henry Clay and Daniel Webster) and that "[t]he States in which these institutions are situated would control them and would effectually interpose to prevent such abuses of power."<sup>70</sup> That democratic processes available through state institutions –

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<sup>65</sup> On Southerners' general desire to suppress state-building in favor of private and plantation ordering, see Robin Einhorn, *Slavery and Taxation*; Daniel M. Mulcare, *Restricted Authority: Slavery Politics, Internal Improvements, and the Limitation of National Administrative Capacity*, 61 Pol. Research Q. 671 (2008).

<sup>66</sup> See, e.g., *Debates and Proceedings of the General Assembly of Pennsylvania* .... (Mathew Carey ed. 1786) at 14 ("A law whereby the corporation had an unlimited succession is unjust")(remarks by Representative Lollar).

<sup>67</sup> McFaul, *The Politics of Jacksonian Finance* at 78-79.

<sup>68</sup> The six agencies were the Treasury Department, the New Orleans branch mint, the Boston and New York customhouses, and two depositories in Charleston and St. Louis respectively. See Act of July 4, 1840, sections 2-4, 5 Stat. at 386.

<sup>69</sup> In justifying the removal of federal monies from the Bank of the United States to various state banks, Roger Taney, Jackson's Secretary of the Treasury, argued that the state banks would prevent the banking business from "being monopolized by the great capitalists." Roger Taney, Report on the Condition of the Bank of the United States in Relation to the Situation of the Different Chartered Banks in the Different States at 160, Appendix to Gale & Seaton's Register of Debates, 23<sup>rd</sup> Cong., 1<sup>st</sup> sess, April 15<sup>th</sup>, 1834.

<sup>70</sup> See Letter of the Government Directors to the House of Representatives, 23<sup>rd</sup> Cong., 1<sup>st</sup> sess, at 83-85 January 14<sup>th</sup>, 1834 (accusing the private directors of the Bank of the United States of "systematically nullifying the

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state constitutional conventions, state plebiscites, small electoral districts, numerous elections -- could legitimize enterprises that would otherwise exercise questionable powers was a familiar idea among Democrats.<sup>71</sup> Under this anti-banker non-delegation theory, *McCulloch*'s doctrine of bank immunity was especially objectionable because, while it preempted state control of nationally chartered banks, it did not insure federal control. Instead, the Bank became a law unto itself, immune from state taxation and regulation but also secured against congressional control by the guarantee in its federal charter that it would serve as the federal government's exclusive fiscal agent for fifteen years.

Jackson's veto message eventually became a basic text supplying the economic ideology of the antebellum Democratic Party. Dominating the entire federal government, the Democratic Party was in a position to bury *McCulloch* – which it did: After Roger Taney's appointment to the chief justiceship, *McCulloch* was not cited by the U.S. Supreme Court for another thirty years. The idea that a private corporation could be a federal agency immune from state control yet also not closely supervised by Congress or the President was anathema to “the Democracy” (as the Democratic Party was known): When the Second Bank's charter expired in 1836, there were no new federal corporate charters approved by the Democratic Congress, such that *McCulloch*'s broad theory of corporate immunity could not be put to any judicial test under the Taney Court.

### III. Judicial Exhumation and Reburial of *McCulloch*

The National Banking Act of 1864 represented the resurrection not only of *McCulloch* but more generally a repudiation of the Democratic Party's distrust for the federal empowerment of corporations and a triumph of the nationalistic protections for investment capital that had been the core of the Federalist and Whig Parties' platforms as well as the Marshall Court's jurisprudence. As initially incorporated into the National Bank Act by the U.S. Supreme Court between 1869 and 1923, *McCulloch*'s theory of immunity barred states from imposing regulations on nationally chartered banks that were specifically targeted at banking activities like deposit-taking or lending. This theory did not strip states of power over banks: The Court's reading of *McCulloch* permitted states to impose “general” laws on nationally chartered banks such as common-law rules of contract, property, and corporations. Nevertheless, the National Bank Act, so construed, prevented states from specifically regulating banking practices on the ground that nationally chartered banks were the moral equivalents of federal agencies.

Like *McCulloch*'s similar assumption, however, the notion that private bankers were somehow equivalent to federal officials proved too politically controversial to sustain. The antebellum demise of *McCulloch* repeated itself in the postbellum career of *McCulloch*'s theory

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representatives of the Government and people” by behaving in a secretive manner and acting like a “commercial bank” rather than a public agency).

<sup>71</sup> On the strategy of legitimating banking democratically, see L. Ray Gunn, *The Decline of Authority* chapter 6 (1988)(on 1846 state constitutional process in New York).

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of preemption under the National Bank Act. Just as the authority of the Second Bank of the United States was shaken by the Panic of 1819, so too, the credibility of bankers was undermined by the Panic of 1907. Likewise, opposition to the powers and immunities of bankers became a central plank in the platform of the Democratic Party between 1910 and 1914, just as they had in the 1830s. In particular Louis Brandeis rallied the Democratic Party around the agenda of curbing the power of the House of Morgan and the “Money Trust” using much the same rhetoric that Andrew Jackson had deployed in 1832 against Nicholas Biddle and his “monster bank.” Like Jackson before him, Brandeis not only successfully pressed for federal supervision of private bankers (in Brandeis’ case, through the creation of a presidentially appointed Federal Reserve Board) but also in moving the U.S. Supreme Court’s doctrine away from *McCulloch*’s theory of immunity for federal instrumentalities.

In short, once more, the American aversion to treating private bankers as the equivalent of a public government led to the demise of *McCulloch*’s theory of immunity despite an initial attempt by the Court to press the idea in the name of the supremacy of national law.

### A. *Applying McCulloch to State Regulation of Banks: Banking-specific rules as a suspect classification under the National Bank Act.*

The Republican ascendancy that permitted the enactment of the National Bank Act and the reinstatement of *McCulloch* as the reigning theory of bank immunity was hardly unshakably secure in 1864. It depended critically on the exclusion of Southern Democrats from the 38<sup>th</sup> Congress. Moreover, the Republicans were divided among themselves: The Party depended heavily on support from westerners – in particular, former Midwestern “anti-Kansas-and Nebraska” Democrats, who were deeply suspicious of eastern capital. Abraham Lincoln had worked assiduously to keep economic issues like the tariff and the powers of federal corporations off of the Republican Party’s agenda in order to woo western support and maintain Republican unity on opposition to slavery and secession in the 1860 and 1864 elections.

There was not, therefore, a new and permanent national popular consensus in favor of conferring broad immunity from state power on national financial institutions. Indeed, it would be odd to think that the anti-banking non-delegation theory – an ideology with roots reaching back before the Constitution and firmly entrenched in newly dominant Midwestern regions of the North -- could be brushed aside by a Civil War having nothing whatsoever to do with banking. Unsurprisingly, neither Congress nor the United States Supreme Court offered any general theory of banking and federalism with which to construe the National Bank Act. Instead, both Court and Congress both fell back on the middle ground suggested by *McCulloch* -- the distinction between resources within the states’ “original” possession and resources generated by the Union as a whole.

This distinction was easiest to apply in the familiar context of taxation. The National Bank Act expressly incorporated adopted *McCulloch*’s dicta on permissible taxes, banning taxes on national banks’ deposits but statutorily authorizing taxes on the value of private shareholder’s

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stock in national banks as well as the banks' real property, so long as these taxes were imposed in a nondiscriminatory fashion.<sup>72</sup> The practical emptiness of this distinction was illustrated nicely by *Van Allen v. Assessors*,<sup>73</sup> which upheld a state tax on private shareholders' stock on the theory that such a tax was no different than any other tax on personal property. As Chief Justice Chase noted in dissent, such a tax was, in practical effect, a tax on the federal bonds in the banks' vaults, because these bonds constituted the major source of the banks' value.<sup>74</sup> Although Chase denounced what he took to be the majority's departure from *McCulloch* and *Osborn* ("the judgments of great men and great judges" that "have acquired almost the force of constitutional sanction"), *Van Allen* was faithful to the central formalism of *McCulloch* – viz., the distinction between prohibited state taxes on banking "operations" such as bank deposits, on one hand, and permitted state taxes on activities falling within the states' "original" powers such as the owning of real estate or corporate shares.

Why rely on such a practically meaningless distinction? Like *McCulloch* itself, the Congress and the U.S. Supreme Court were trying to divide resources between the states and the federal government by those resources' proximity to the business of banking. Taxes on real estate or private citizens' "moneyed capital" were taxes on the resources ordinarily available to states. Taxes on deposits, by contrast, taxed a banking activity specifically authorized by a federal charter and, therefore, were an attack on federal resources. That the practical effect of the two sorts of taxes was identical did not detract from the value of the distinction as a plain and simple dividing line between state and federal spheres. Good (formalistic) fences, on this theory, made good neighbors.

This dividing line did not imply any overall "centralization default": It could, indeed, imply a presumption against preemption of state laws sufficiently remote from banking business. In extending *Van Allen* to permit state laws requiring nationally chartered banks to collect the tax on non-resident shareholders' bank stock, the U.S. Supreme Court emphasized that nationally chartered banks were "governed in their daily course of business far more by the laws of the State than of the nation" and that "[i]t is only when the State law incapacitates the banks from discharging their duties to the government that it becomes unconstitutional."<sup>75</sup> Even when state taxes imposed administrative duties identical to those imposed by the National Bank Act, the

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<sup>72</sup>Act of June 3, 1864, ch. 106, 13 Stat. 99, at § 41 ("[N]othing in this act shall be construed to prevent all the shares in any of said associations, held by any person or body corporate, from being included in the valuation of the personal property of such person or corporation in the assessment of taxes imposed by or under state authority at the place where such bank is located, and not elsewhere, but not at a greater rate than is assessed upon other moneyed capital in the hands of individual citizens of such state:.... [N]othing in this act shall exempt the real estate of associations from either state, county, or municipal taxes to the same extent, according to its value, as other real estate is taxed").

<sup>73</sup>70 U.S. 573 (1865).

<sup>74</sup>*Id.* at 589.

<sup>75</sup>*Nat'l Bank v Commonwealth of Kentucky*, 76 U.S. (9 Wall.) 353, 362 (1869).

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Court would tolerate the state law if the tax did not touch the banks' deposits but instead was legally incident on types of property not unique to banking.<sup>76</sup>

Using *McCulloch* to define banks' tax liability under state law was a familiar enterprise. But how would *McCulloch* apply to state regulation of nationally chartered banks? The U.S. Supreme Court relied on a distinction analogous to the line between nonbanking property (e.g., real estate and private stock shares) and bank deposits. State laws that specifically targeted banking practices like the charging of interest or the taking of deposits were subjected to a strict rule of field preemption: If any provision of federal law remotely addressed the topic covered by state law, then the latter was preempted. In *Farmers' & Mechanics' Nat'l Bank v. Dearing*,<sup>77</sup> for instance, the Court refused to use state usury laws to clarify ambiguous terms in the National Banking Act's statutory limits on interest,<sup>78</sup> justifying this result with "[t]he reasoning of Secretary Hamilton and of this court in *McCulloch v. Maryland* ... and in *Osborne v. Bank of the United States*." "Being such means [for executing federal policy], brought into existence for this purpose, and intended to be so employed," *Dearing* stated, "the States can exercise no control over them, nor in any wise affect their operation, except in so far as Congress may see proper to permit." To allow states to set the penalty as well as interest rate would insure that a nationally chartered bank "would be liable, in the discharge of its most important trusts, to be annoyed and thwarted by the will or caprice of every State in the Union."<sup>79</sup>

The Court was equally hostile to state regulation specifically directed at deposit-taking when such laws were applied to nationally chartered banks. In *Easton v. State of Iowa*,<sup>80</sup> for instance, the Court held that the National Bank Act preempted Iowa's law imposing criminal liability on bank officers for committing fraud if they accepted deposits after knowing that their bank had become insolvent. As in *Dearing*, the Court invoked *McCulloch* and *Osborn*, noting that, despite being private institutions, national banks were also federal instrumentalities that could not be subject even to state laws that did not directly conflict with any federal rule,<sup>81</sup>

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<sup>76</sup> In *Waite v. Dowley* 94 U.S. 527 (1876), for instance, the Court specifically rejected the notion that, because federal law also required shareholder lists, federal law "cover[ed] the same ground as that covered by the Vermont statute" and should, therefore, be preempted. The Vermont statute served a different purpose than the similar federal law, according to *Waite*, and, therefore, "was not in conflict with any provision of the act of Congress." *Id.* at 533-34.

<sup>77</sup> 91 U.S. 29 (1875)

<sup>78</sup> The National Bank Act incorporated as a ceiling on interest either "interest at the rate allowed by the laws of the State or Territory where the bank is located, and no more" or, "when no rate is fixed by the laws of the State or Territory ... a rate not exceeding seven per centum." The statute's definition of the penalty for violating this ceiling, however, suffered from an ambiguous modifier, applying only to banks that "knowingly taking, receiving, reserving, or charging a rate of interest greater than aforesaid." To what did "aforesaid" refer – to the 7% interest ceiling set by federal law, or to the violation of state-defined interest rates as well? Under the latter interpretation, federal penalties would apply in every state; under the former construction, states could set their own penalties for violations of their interest ceilings.

<sup>79</sup> *Id.* at 35.

<sup>80</sup> 188 U.S. 220 (1903).

<sup>81</sup> As *Easton* acknowledged, "there is no express prohibition contained in the Federal statutes [duplicating or contradicting Iowa's rule], but there are apt provisions, sanctioned by severe penalties, which are intended to protect the depositors and other creditors of national banks from fraudulent banking." *Id.* at 231.

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because “confusion would necessarily result from control possessed and exercised by two independent authorities.”<sup>82</sup> Iowa’s law could not stand not because some provision of the National Bank Act specifically prohibited it or even duplicated it, but rather because the existing rules contained within the National Bank Act were presumed to be exclusive: “It thus appears that Congress has provided a symmetrical and complete scheme for the banks to be organized under the provisions of the statute.”<sup>83</sup>

Likewise, the Court held in *First Nat’l Bank v. State of California*<sup>84</sup> that the National Bank Act preempted California’s law providing for the escheat to the state of bank accounts that were unclaimed for more than twenty years, to the extent that the state law applied to nationally chartered banks. As with Iowa’s law in *Easton*, there was no specific provision of the National Bank Act addressing the abandonment of bank accounts with which California’s law implicitly conflicted. Instead, the Court emphasized that the National Bank Act generally authorized national banks power to receive deposits, a power that reasonably implied the right to repay the deposit on the demand of the rightful accountholder despite the passage of time. This general federal authorization to repay accounts did not express any specific policy about abandoned accounts: California was manifestly dealing with an issue that Congress simply had overlooked. Nevertheless, the Court presumed that Congress’ silence indicated an intention to exclude any state law specifically directed to the management of bank accounts. The basis for this presumption of field preemption was less a judicial inquiry into the likely beliefs of Congress, however, than *McCulloch*’s idea that national banks were federal instrumentalities “designed to be used to aid the government in the administration of an important branch of the public service.”<sup>85</sup> According to *First Nat’l Bank*, “the states can exercise no control over them, nor in any wise affect their operation, except in so far as Congress may see proper to permit,” and the Court was not willing to infer any such permission from Congress’ silence on the topic of abandoned accounts.

In sum, the Court invoked *McCulloch* to bar states from filling the gaps in the National Bank Act with state laws if those state laws specifically targeted activities integral to the business of banking – for instance, the charging of interest (*Dearing*), the acceptance of deposits (*Easton*), and the maintaining of accounts (*First Nat’l Bank*). For such state laws that singled out banking practices, the Court construed *McCulloch* to require a presumption of field preemption: In Professor Tom Merrill’s phrase, federal law was presumed to act “like an eraser that rubs out state law in a given area, leaving only federal law standing,”<sup>86</sup> even when there was nothing in the federal specifically addressing the issue covered by the state law. Insofar as states regulated

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<sup>82</sup>“Such being the nature of these national institutions, it must be obvious that their operations cannot be limited or controlled by state legislation,” *Easton* stated. *id.* at 229, further noting that “we are unable to perceive that Congress intended to leave the field open for the states to attempt to promote the welfare and stability of national banks by direct legislation.” *Id.* at 231-32.

<sup>83</sup> *Id.*

<sup>84</sup> 262 U.S. 366 (1923).

<sup>85</sup> *Id.* at 369.

<sup>86</sup> Thomas Merrill, 102 Nw. L. Rev. 727, 731 (2008).

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banking-specific activities (deposit-taking, lending money at interest), the National Bank Act was presumed to be (in *Easton*'s words) "a symmetrical and complete scheme for the banks" that implicitly excluded any state gap-filling on topics not covered by the Act. In effect, state laws specifically addressing banking practices fell into a statutory "suspect classification" under which the Court would presume preemption absent very specific statutory authorization.

The Court completely abandoned this presumption of preemption, however, when states imposed laws on nationally chartered banks that were less closely tied to the business of banking. As *First Nat'l Bank* stated, nationally chartered banks' "contracts and dealings are subject to the operation of general and undiscriminating state laws," because these laws "do not conflict with the letter or the general object and purposes of congressional legislation."<sup>87</sup> Likewise, *Easton* gave its blessing to state criminal laws, noting that "[u]ndoubtedly a state has the legitimate power to define and punish crimes by general laws applicable to all persons within its jurisdiction."<sup>88</sup> This did not mean that such general state laws were never preempted by the National Bank Act. If there were some provision of the Act (say, the NBA's anti-preference policy regarding distributions to creditors) that contradicted the state's common-law rule, then the state's rule would have to give way.<sup>89</sup> Such a specific conflict between state and federal law, however, would not be presumed. Instead, the Court relied on an opposite presumption assuming, absent some specific congressional intention to the contrary, that nationally chartered banks were "governed in their daily course of business far more by the laws of the State than of the nation."<sup>90</sup>

This toleration for "general laws" insured that state common law of contract, property, and corporations would generally escape preemption unless there was a specific conflict between the common-law rule and some policy contained within the National Bank Act. In *McClellan v. Chipman Traders' Nat'l Bank*,<sup>91</sup> for instance, the Court allowed Massachusetts to enforce its prohibition on preferential transfers to creditors against a nationally chartered bank, even though such a rule prohibited a particular exercise of a power expressly conferred by the National Bank Act to receive real estate in satisfaction of debts. The state's prohibition of the national bank's power to receive real estate in a preferential transfer was not "significant," because the state law barred the exercise of the national bank's powers only "under particular and exceptional circumstances": "No function of such banks is destroyed or hampered by allowing the banks to exercise the power to take real estate, provided only they do so under the same conditions and restrictions to which all the other citizens of the state are subjected."<sup>92</sup> Subjecting the bank to the

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<sup>87</sup> *First Nat'l Bank*, at 368-69.

<sup>88</sup> *Easton*, at 239.

<sup>89</sup> In *Davis v. Elmira Savings Bank*, 161 U.S. 275 (1896), for instance, the Court held that New York could not give a preference to savings banks who were creditors of a nationally chartered bank in the event of the latter's insolvency, because "one of the objects of the national bank system was to secure, in the event of insolvency, a just and equal distribution of the assets of national banks among all unsecured creditors, and to prevent such banks from creating preferences in contemplation of insolvency." *Id.* at 284.

<sup>90</sup> *Nat'l Bank v Commonwealth of Kentucky*, 76 U.S. (9 Wall.) 353, 362 (1869).

<sup>91</sup> 164 U.S. 347 (1896).

<sup>92</sup> *Id.* at 358.

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general background provisions of state contract law was not a “significant burden” on the exercise of federally conferred powers even when that law completely foreclosed one such exercise (receiving preferential transfers), because the NBA presupposed that nationally chartered banks would engage in business, “as to their contracts in general, under the operation of the state law.”<sup>93</sup>

In contrast to its decisions dealing with state laws specifically addressing banking practices, the Court upheld “general” state laws even when they overlapped with specific provisions of the National Bank Act. The private right of shareholders to inspect a nationally chartered bank’s books under state law, for instance, served some of the same functions as the powers of the federal Comptroller of the Currency to inspect a bank’s accounts. The state law was nonetheless held not to be preempted in *Guthrie v. Harkness*,<sup>94</sup> because the Court was “unable to find any definition of ‘visitorial powers’ which can be held to include the common-law right of the shareholder to inspect the books of the corporation.”<sup>95</sup>

What made the states’ general rules of common law less subject to preemption than their rules specifically addressing banking practices? There were practical reasons why the Court would want to preserve states’ common-law rules. In 1882, Congress enacted a statute<sup>96</sup> eliminating nationally chartered banks’ power to remove cases to federal court that had previously existed since 1863,<sup>97</sup> thereby reducing the capacity of the federal courts to fashion general federal common law to govern the banks’ transactions pursuant to *Swift v. Tyson*.<sup>98</sup> The alternative to subjecting banks to state law was, therefore, frequently anarchy.

This practical explanation, however, cannot explain why the Court did not simply allow state law to apply in any case where the federal statute did not address the mischief that was the topic of that state law. Why not simply use conflict preemption to define the scope of state power over national banks, allowing state statutes -- even statutes specifically regulating deposit-taking, lending, or other banking-specific activities -- to fill gaps in the National Bank Act where the latter was silent or unclear? The answer cannot be that “general” laws intrude less

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<sup>93</sup> *Id.* at 359.

<sup>94</sup> 199 U.S. 148 (1905). *Guthrie* acknowledged that national banks still fit within McCulloch’s idea of a federal instrumentality – “a public institution, notwithstanding it is the subject of private ownership” that “may issue bills, which circulate as part of the currency of the country” and that “is subject to examination, and, in a large measure, to the supervision, of the Comptroller of the Currency.” *Id.* at 157.

<sup>95</sup> *Id.*

<sup>96</sup> Law of July 12, 1882, ch. 290, § 4, 22 Stat. 162, 163, repealed by ch. 346, § 39, 62 Stat. 992 (1948) (current version at 28 U.S.C. § 1348 (2000)).

<sup>97</sup> Prior to 1882, under the National Currency Act of 1863, ch. 58, § 59, 12 Stat. 665, 681 (1863) (current version at 28 U.S.C. § 1348 (2000 & Supp. 2004)), nationally chartered banks could remove their contractual disputes to federal courts.

<sup>98</sup> Under *Swift v. Tyson*, federal courts had fashioned rules of general federal common law to govern nationally chartered banks’ transactions whenever disputes arising out of those transactions ended up in federal court. For examples of federal courts applying federal common law to questions of nationally chartered banks’ corporate powers and governance, see *Briggs v. Spaulding*, 141 U.S. 132 (1891) (Degree of care required of directors of corporations depends upon the subject to which it is to be applied, determined in view of all circumstances); *Martin v. Webb*, 110 U.S. 7 (1884) (cashier can be given power to bind bank as its agent, where agency is shown by parol evidence).

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into the business of banking than banking-specific state laws. Massachusetts' law at issue in *McClellan* prohibiting debtors from preferentially transferring real estate to banks practically impedes a bank's business just as much as Iowa's law in *Easton* prohibiting bank officers from accepting deposits. The difference between the two, therefore, cannot be explained by any desire to protect a national market with uniform rules suitable for interstate banking.

The distinction between general and banking-oriented state laws, therefore, was driven less by bankers' needs for regulatory uniformity in a national market and more by judges' needs for doctrinal simplicity. *McCulloch* provided a relatively crisp way to divide federal from state jurisdictions, so the federal courts adapted *McCulloch*'s rules for state taxation to state regulation. Like those state taxes on real property or corporate stock blessed by *McCulloch*, state common-law rules seemed to fall within the states' "original" powers rather than to exploit federally created resources. By contrast, state rules targeting banking, like state taxes imposed on banks' deposits, seem to attack a subject (nationally chartered banking) that was purely a product of federal law. Treating banking-specific activity as a suspect classification that state laws could not address without triggering preemption was just an easy way to translate *McCulloch*'s tax-based lines into the context of regulation.

### B. The Second Demise of *McCulloch*'s Field Preemption

Whatever its advantages in terms of doctrinal clarity, *McCulloch*'s distinction between suspect banking-specific laws and general laws had one striking disadvantage: The distinction prohibited states from addressing issues that neither Congress nor any federal agency had actually considered. The reason was simply that the presence or absence of a federal law addressing some topic was orthogonal to *McCulloch*'s test. States could not, therefore, fill gaps in federal regulations of banks with their own banking-specific rules. In effect, *McCulloch* delegated the duty of filling gaps in federal regulatory schemes away from states to the officers of a private banking corporation. Such preemption might make sense if one viewed national banks' officers as (in Justice Van Devanter's words) "upon much the same plane as are officers of the United States."<sup>99</sup> If one lacked such confidence in private bankers' high-minded disinterestedness, however, then exempting banks from state oversight even when federal law is silent about the merit of the bankers' activities is tantamount to declaring bankers be a law unto themselves – a sort of private government of financiers subject to no democratic oversight whatsoever.

By the early twentieth century, the notion that privately owned banks were the equivalent of disinterested federal officials had become completely untenable. Between 1907 and 1914, the Democratic Party made opposition to legal privileges for private bankers the centerpiece of their political platform, culminating in Woodrow Wilson's and Louis Brandeis' "New Freedom" campaign of 1912. Like Andrew Jackson's veto message of 1832, this campaign created a

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<sup>99</sup> *First National Bank of Bay City v. Fellows*, 244 U.S. 416, 430 (1917)(Van Devanter, J., dissenting).

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political climate in which *McCulloch*'s theory of banking immunity from state law was politically – and, eventually, judicially – doomed.

### *1. The Panic of 1907 and Brandeis' Revival of the Anti-Banker Non-Delegation Principle*

The end of *McCulloch*'s privileging of private bankers as federal officials was a long time coming. Greenbackers, Anti-Monopoly Party members, and Populists had railed against the power of financial elites since the end of the Civil War,<sup>100</sup> but these attacks had little political traction in a two-party system where neither major party would espouse the anti-banking cause.<sup>101</sup> Although William Jennings Bryan made hostility to banks a major part of the Democratic Party's platform in 1896, he had been so thoroughly trounced that embrace of an anti-banking agenda seemed like political suicide. The Panic of 1907, however, changed everything. Brought on by a coincidence of events – the San Francisco earthquake and the resulting loss of capital reserves, an unsuccessful but highly leveraged effort to corner the copper market and a resulting fear that the lenders would be illiquid – the Panic exposed the fragility of a financial system rooted in essentially the self-governance of decentralized bankers.<sup>102</sup> J.P. Morgan almost single-handedly staved off a full-blown depression by pledging his own resources and strong-arming bankers to do likewise, thereby guaranteeing the deposits of illiquid but solvent banks. Despite the arguably heroic quality of his intervention, Morgan's determining the nation's fate by negotiating with other Wall Street elites in his private library rubbed against democratic sensibilities. Farmers, workers, and middle-class professionals all rebelled against this notion of being governed thus by the House of Morgan.

The historical moment was ripe for reevaluation of the idea of national banks' privileges and immunities. The first sign of trouble for the idea of self-governing banks was the newly elected Democratic Congress' rejection of the "Aldrich Plan" in 1912. A proposal of the National Monetary Commission and named for stalwart conservative Republican Senator Nelson Aldrich, the Aldrich Plan would have authorized a self-governing association of national banks stave off future runs and panics by pooling their deposits free from meddling politicians,<sup>103</sup> effectively codifying the power that J.P. Morgan had informally wielded in 1907. The Democratic Congress, newly elected between 1910 and 1912, hooted the plan down, setting the stage for a showdown in 1912 over the legal status of banks in the 1912 Presidential election.

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<sup>100</sup> See Irwin on Greenbackers.

<sup>101</sup> The Democratic Party was the most obvious home for such anti-banking sentiment, as it was dominant in the under-capitalized South. The Democrats, however, depended on support from New York to win the Presidency, requiring them to adopt a more neutral attitude towards banking. See Scott C. James.

<sup>102</sup> On the causes of the Panic of 1907, see Robert F. Bruner & Sean D. Carr, *The Panic of 1907: Lessons Learned from the Market's Perfect Storm* 13-47 (2007).

<sup>103</sup> The National Monetary Commission was an entity created by the Aldrich-Vreeland Act in the wake of the Panic of 1907. For a summary of the Aldrich Plan, see Elmus Wicker, *The Great Debate on Banking Reform: Nelson Aldrich and the Origins of the Fed* (Ohio University Press 2005). For the Commission's report, see *Report of the National Monetary Commission, Letter from the Secretary of the Commission and a draft bill to incorporate the National Reserve Association of the United States, and for other purposes*, Sen. Doc. No. 243. 62d Congress (U.S. Government Printing Office, January 9, 1912).

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Like Jackson's 1832 veto message, Woodrow Wilson's "New Freedom" campaign platform focused on the illegitimacy of bankers' exercising governmental power without democratic oversight. Inspired by Louis Brandeis' denunciation of "the Money Trust," the New Freedom platform maintained that investment bankers fostered inefficient and undemocratic monopolies in utilities, railroads, and manufacturing by sitting on "interlocking directorates" of corporate boards. The campaign was fueled by the Pujo Committee's investigation during the summer of 1912 into the influence of bankers over industry, in which an aged J.P. Morgan was called to testify about the appointment of directors from the House of Morgan and related financial firms to dozens of corporate boards. The Committee's report concluded that a system of interlocking directorates allowed a handful of bankers to govern the nation. Louis Brandeis' essays in Harper's Weekly, published between August and December of 1912 (and later collected as the 1914 tract *Other People's Money*), publicized the Pujo Committee's findings and reinforced the idea the bankers formed a "financial oligarchy" resulting in "the suppression of industrial liberty, indeed of manhood itself."<sup>104</sup> Brandeis called for a variety of reforms to curb bankers' power, including more disclosures of bankers' fees and influence to investors and stricter prohibitions on bankers' conflicts of interest in sitting on multiple boards.<sup>105</sup> , and Influenced by Brandeis, Congress adopted the 1913 Federal Reserve Act with its key Brandeisian principle that banks in the federal reserve system must be subject to the supervision of a Federal Reserve Board appointed by the President.

Beyond the precise mechanism for supervising banks, however, lay a single common assumption that Andrew Jackson would readily have embraced: Private bankers were not trustworthy federal officials entitled to determine the nation's financial policies without some form of democratic oversight. The implication of this anti-banker non-delegation doctrine was that federal law should not preempt state banking rules unless federal officials had actually evaluated the particular risk addressed by state law. In short, Brandeis' assault on "government by bankers" was also an assault on *McCulloch's* theory of field preemption.

### 2. Judicial Retreat from *McCulloch's* field preemption, 1924-1948.

In short, the early twentieth century saw a revival of the anti-banker non-delegation doctrine remarkably similar to the Jacksonian principles leading to the first downfall of *McCulloch*. By the 1920s, the Court itself beat a steady retreat from its earlier confident assertions about nationally chartered banks' being federal instruments beyond state control. Instead, the Court repeatedly upheld state laws specifically targeting banking practices using ordinary principles of conflict preemption to find no conflict with the National Bank Act.

There were signs of trouble for *McCulloch* even before the 1920s. *First National Bank of Bay City v. Fellows*<sup>106</sup> was ostensibly a nationalistic decision in which the Court upheld the Federal Reserve Act of 1913, finding that Congress had the power to confer on national banks

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<sup>104</sup> Louis Brandeis, *Other People's Money and How the Bankers Use It* 48 (McClures 1914).

<sup>105</sup> *Id.* at 56-64, 72-82,

<sup>106</sup> 244 U.S. 416 (1917).

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the power to hold securities as a trustee in a probate proceeding and summarily slapping aside the notion that delegating broad supervisory powers to the Federal Reserve Board violated the non-delegation doctrine. But buried in *Bank of Bay City* was a sign of judicial impatience with *McCulloch*: The Court upheld the power of the state courts to enforce state limits on banks' powers against a national bank. Setting aside 19<sup>th</sup> century decisions holding that state courts could not issue writs of habeas corpus against federal officers, the Court upheld the state courts' power to supervise national banks by noting the urgent need for state probate courts to secure a determination of the powers of trustees. As Justice Van Devanter noted in dissent, the idea of allowing state courts to enforce state law against a federal instrumentality was flatly inconsistent with the spirit of *McCulloch*.<sup>107</sup> But 1917, however, *McCulloch*'s equation of private banks with federal officials had apparently worn a bit thin.

*First Nat'l Bank of St. Louis v. Missouri*,<sup>108</sup> however, was the first decision overthrowing *McCulloch*'s analysis to uphold a state law. In *First Nat'l Bank*, the Court upheld Missouri's law barring banks from opening branch offices within the state, ignoring *McCulloch*'s principle of field preemption and instead applying only those precedents like *McClellan* allowing state laws to be enforced where they did not conflict with any specific provision of the National Bank Act. Noting that the National Bank Act "by fair construction of the statutes" denied nationally chartered banks any power to form branches unless they had such a power under a previous state charter,<sup>109</sup> the majority stated that it was "self-evident" that the state statute could not frustrate the purpose of the federal statute by prohibiting precisely what the federal statute also prohibited.<sup>110</sup> Given that the state statute did not conflict with the National Bank Act, the majority concluded that "the way is open for the enforcement of the state statute."<sup>111</sup> In other words, without expressly overruling *McCulloch*'s theory of field preemption, the Court ignored it, instead applying ordinary conflict preemption. In his dissent, Justice Van Devanter (joined by Chief Justice Taft and Justice Pierce Butler) correctly asserted that principles "settled a century ago in the days of the Bank of the United States" dictated that Missouri's banking-specific statute should be preempted insofar as the banking-specific state rule applied to "corporate instrumentalities of the United States."<sup>112</sup> Unsurprisingly, Taft joined his own appointee's dissent, for Taft had been a backer of the Aldrich Plan as President.

The destruction of *McCulloch*'s immunity for national banks was completed in the New Deal Courts of Chief Justices Hughes, Stone, and Vinson. From 1934 until 1948, the Court repeatedly upheld the application of states' banking-specific laws to nationally chartered banks, applying ordinary conflict preemption and ignoring the idea that banks should be free from state oversight even when federal law did not endorse banks' policy choices. *Lewis v. Fidelity &*

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<sup>107</sup> 244 U.S. at 430 (Van Devanter, J., dissenting).

<sup>108</sup> 263 U.S. 640 (1924).

<sup>109</sup> *Id.* at 657-58.

<sup>110</sup> *Id.* at 659.

<sup>111</sup> *Id.* at 660.

<sup>112</sup> *First Nat'l Bank*, 263 U.S. at 662 (Van Devanter, J., dissenting)

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*Deposit Co.*<sup>113</sup> held that states could prohibit banks from being appointed depositories of state or local governments' revenues unless the bank provided a bond creating a lien on all of the bank's assets to insure faithful performance of the contract. The Court began and ended its analysis with the question of whether the National Bank Act's prohibition on preferences for creditors implicitly prohibited such a bonding requirement. Finding no conflict, the Court upheld the Georgia statute without any reference to *McCulloch*. Likewise, *Wichita Royalty Co. v. City Nat'l Bank of Wichita Falls*<sup>114</sup> followed *Erie v. Tompkins* in applying Texas's law to the question of whether the bank was responsible for a depositor's trustee's misappropriation of a deposit for personal use. Again, there was no mention of *McCulloch*'s prohibition on subjecting national banks to states' banking-specific laws.

Finally, *Anderson Nat'l Bank v. Lockett*<sup>115</sup> virtually overruled the Court's 1923 opinion in *First Nat'l Bank v. California*, holding that Kentucky could deem that certain bank accounts were abandoned and, therefore, escheat to the state after giving notice to accountholders and waiting for a defined interval of time. The Court attempted to distinguish *First Nat'l Bank* by characterizing Kentucky's statute as less "unusual and harsh" than California's and, therefore, less of a deterrent to depositors' entrusting their funds to a national bank.<sup>116</sup> But the Court's re-characterization of *McCulloch* represented the complete repudiation of *McCulloch*'s theory of field preemption. According to *Lockett*, the Kentucky statute was consistent with *McCulloch*, because it "does not discriminate against national banks, *cf. McCulloch v. State of Maryland*, 4 Wheat. 316, ... by directing payment to the state by state and national banks alike, of presumptively abandoned accounts." Such a statement flew in the face of the Marshall Court's understanding of *McCulloch*: As noted in Part II, *Weston* specifically rejected this idea that non-discrimination against the federal government sufficed to satisfy *McCulloch*'s principle of supremacy. *Lockett* also noted that there was not "any word in the national banking laws which expressly or by implication conflicts with the provisions of the Kentucky statutes"<sup>117</sup> – a true observation but an irrelevant one under *Easton* and *Dearing*, under which such a conflict was presumed absent clear federal authorization for state regulation of federal instrumentalities.

*Lockett*, in short, implicitly and *sub silencio* adopted a new and narrower reading of banks' immunity that permitted states to impose regulations of lending and deposit-taking just so long as the states did not thereby discriminate against, or contradict any policy of, the federal government. This did not mean that banks never received the benefits of preemption. If a federal statute contained a specific provision preempting a state law, then, of course, that state law could have no effect.<sup>118</sup> Moreover, the preemptive provision of the federal statute could be

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<sup>113</sup> 292 U.S. 559 (1934).

<sup>114</sup> 306 U.S. 103 (1939).

<sup>115</sup> 321 U.S. 233 (1948).

<sup>116</sup> *Anderson*, 321 U.S. at 250.

<sup>117</sup> *Id.* at 247-48

<sup>118</sup> See, e.g., *Federal Land Bank of St. Paul v. Bismarck Lumber Co.*, 314 U.S. 95 (1941)(holding that tax exemption for federal land banks expressly conferred by Federal Farm Loan Act of 1916 applied to sales tax paid on lumber for fences and buildings).

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implied rather than explicit: If some state law contradicted the spirit or purpose of federal banking law, then the former would be set aside in favor of the latter.<sup>119</sup> The New Deal Court embraced a robust judicial purposivism in statutory interpretation during the 1940s,<sup>120</sup> and federal courts could exercise a lot of creativity in inferring such implied federal purposes from federal statutes – an effort that could be the occasion of much judicial hand-wringing about the degree to which federal banking law permitted judges to invent principles of federal common law to govern national banks.<sup>121</sup>

### **3. *McCulloch* and modern conflict preemption**

After *Lockett*, the fundamental question defining banking preemption had changed, as lower courts recognized.<sup>122</sup> The U.S. Supreme Court no longer asserted that states could never regulate national banks' operations. The Court instead emphasized that states could not deny or impair a banking power that Congress explicitly conferred.

*Barnett Bank v. Nelson*<sup>123</sup> illustrates this post-New Deal focus on conflict preemption. The Florida law at issue in *Barnett* – a prohibition on banks' selling insurance if they were affiliated with any holding company -- was a banking-specific law that, under the old reading of the National Bank Act of *Dearing* and *Easton*, should have been automatically preempted as a forbidden regulation of banks' deposit-taking operations. *Barnett*, however, ignored the banking-specific character of the Florida law. Instead, *Barnett* focused on the conflict between the Florida statute and a 1916 federal law authorizing national banks to sell insurance. Relying on what it called "ordinary legal principles of pre-emption,"<sup>124</sup> *Barnett* stated that a federal grant of banking power "ordinarily preempts *contrary* state law" such that "normally Congress would not want States to forbid, or to *impair significantly*, the exercise of a power that Congress *explicitly* granted."<sup>125</sup> Because the Florida law barred Barnett Bank from any exercise of a

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<sup>119</sup> *Deitrick v. Greaney*, 309 U.S. 190 (1940)(holding that federal courts could disregard state law that would circumvent federal prohibition on national bank's purchasing its own stock).

<sup>120</sup> *United States v. Am. Trucking Ass'n*, 310 U.S. 534, 542 (1940) ("In the interpretation of statutes, the function of the courts is easily stated. It is to construe the language so as to give effect to the intent of Congress").

<sup>121</sup> *Compare D'Oench, Duhme & Co. v. Federal Deposit Ins. Corp.*, 315 U.S. 447, 456-58 (1942)(Douglas, J., defending principle of federal common law, inferred from spirit of statute, that certain state-law defenses against promissory note were inapplicable against FDIC as receiver of national bank) *with Id.* at 469-70 (Frankfurter, J., concurring in judgment) (decrying reliance on federal common law absent statutory text and using state law to resolve question of note's validity).

<sup>122</sup> *See, e.g., People of State of Cal. v. Coast Federal Sav. & Loan Ass'n*, 98 F.Supp. 311, 319 (D.C.Cal. 1951) (distinguishing *Lockett* because it addressed the powers of nationally chartered banks rather than nationally chartered savings & loans and noting, with respect to the former that Congress left more space for states to regulate). Although *Coast Federal Sav. & Loan Ass'n* is a mere district court decision, it was one of the first decisions to recognize that federally chartered savings and loans were governed by a more aggressive standard of federal preemption than nationally chartered banks, a distinction the *Coast* correctly attributed to New Deal decisions like *Lockett*.

<sup>123</sup> 517 U. S. 25 (1996).

<sup>124</sup> *Barnett*, 517 U.S. at 37.

<sup>125</sup> *Barnett*, 517 U. S. 25, 32, 33 (1996)(emphasis added).

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federally conferred power, the Court held that it constituted a “significant” impairment of that power – hardly a surprising conclusion, given the breadth of the state law restriction. In so holding, *Barnett Bank* cited *Luckett* for the proposition that *Barnett*’s holding would not “deprive States of the power to regulate national banks, where (unlike here) doing so does not prevent or significantly interfere with the national bank’s exercise of its powers.”<sup>126</sup> The citation was significant as a re-affirmation of *Luckett*’s holding that federal banking law did not automatically preempt a state regulation that was targeted specifically at a banking activity (in the case of *Luckett*, the banking activity of maintaining abandoned or dormant accounts).

It would be an exaggeration to state that the Court abandoned entirely the earlier 19<sup>th</sup> century tradition under which states were barred from regulating banks with laws specifically targeting banking activities. The old precedents continued to be cited and language, quoted. In *Watters v. Wachovia Bank*,<sup>127</sup> for instance, the Court approvingly quoted *Dearing*’s sweeping statement that “the States can exercise no control over [national banks], nor in any wise affect their operation, except in so far as Congress may see proper to permit...”<sup>128</sup> While *Watters* acknowledged that “[f]ederally chartered banks are subject to state laws of general application in their daily business to the extent such laws do not conflict with the letter or the general purposes of the NBA,”<sup>129</sup> the use of the phrase “state laws of general application” suggested by negative implication that state laws *not* of general application would be preempted. This suggestion of some sort of field preemption for all state laws targeting national banks’ lending or deposit-taking activities was reinforced by *Watters*’ statement that “[d]iverse and duplicative superintendence of national banks’ engagement in the business of banking, we observed over a century ago, is precisely what the NBA was designed to prevent.”<sup>130</sup> To support this last statement, the Court quoted with approval *Easton*’s statement that federal banking law created a banking system that was “independent, so far as powers conferred are concerned, of state legislation which, if permitted to be applicable, might impose limitations and restrictions as various and as numerous as the States.”<sup>131</sup>

*Watters*, however, never embraced wholesale field preemption of all state laws specifically targeted banking business. Instead, the Court rested its holding on reasoning more specific than a general ban on states’ enforcing their banking-specific rules against national banks or those banks’ subsidiaries. In analyzing why Michigan could not require such subsidiaries to register with and be subject to the general oversight of Michigan’s banking authorities, *Watters* relied on the National Bank Act’s specific provision barring states from exercising visitorial powers over national banks.<sup>132</sup> Moreover, *Watters* offered an argument

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<sup>126</sup> *Barnett*, 517 U.S. at 33.

<sup>127</sup> 550 U.S. 1 (2007).

<sup>128</sup> 550 U.S. at 11.

<sup>129</sup> *Id.* (emphasis added).

<sup>130</sup> 550 U.S. at 13-14.

<sup>131</sup> 550 U.S. at 14 (quoting *Easton v. Iowa*, 188 U.S. 220, 229 (1903)).

<sup>132</sup> “No national bank shall be subject to any visitorial powers except as authorized by Federal law ....” 12 U.S.C. § 484(a).

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specific to the “duplicative” character of the general supervisory power asserted by Michigan, noting that the OCC already exercised precisely the same power in the form of the OCC’s visitorial power.<sup>133</sup>

The Court has most clearly rejected *McCulloch*’s theory of preemption in *Cuomo v. Clearing House Ass’n*,<sup>134</sup> when the Court held that the OCC’s exclusive visitorial power did not preempt the New York Attorney General’s power to enforce the state’s fair lending laws in state or federal court. In defense of its theory that the lawsuit was preempted because it was an exercise of visitorial powers exclusively vested in the OCC, the OCC argued that the National Bank Act barred, at the very least, public officials’ lawsuits to enforce “state banking laws” even if that grant did not preempt such officials’ enforcement of other more general laws – for instance, general rules of contract and property -- that supply the legal “infrastructure” for banking. In rejecting this “distinction between ‘implementation’ of ‘infrastructure’ and judicial enforcement of other laws,” *Clearing House Ass’n* (written by the Court’s most outspoken textualist, Justice Scalia) invoked the text of the statute: The distinction “[o]f course ... can be found nowhere within the text of the statute” and, therefore, “attempts to do what Congress declined to do: exempt national banks from all state banking laws, or at least state enforcement of those laws.”<sup>135</sup> Thus, *Clearing House Ass’n* expressly rejected the idea that there was implicit in the spirit of the National Bank Act a general prohibition on state laws specifically tailored for the regulation of lending – precisely the position that the Court had defended since *McCulloch*. Indeed, even the OCC seemed to concede that the state’s fair lending law might not be preempted “because its substantive requirements are not meaningfully different from those imposed by federal law.”<sup>136</sup>

In sum, since the New Deal, the Court has gradually edged away from the idea, derived from *McCulloch*, that national banks are immune from state laws specifically targeting the business of banking. The law remains ambiguous: No decision ever acknowledged that the Court was overruling its earlier doctrine (although some dissenting opinions did). Nevertheless, the decisions became more tolerant of the idea that national banks could be subjected to even banking-specific state laws, just so long as the actions governed by those state laws (for instance, abandoned or dormant accounts, bonds for state or local governments’ deposits, the opening of branch offices) were not inconsistent with the letter or the spirit of the federal banking laws.

The New Deal Court never explained why it retreated from *McCulloch*’s definition of nationally chartered banks’ immunities as barring all state regulation of national banks that singled out banking activities. One can, however, identify two trends in the policies and jurisprudence of the early Twentieth century sufficient to explain the outcomes of these decisions – decreasing trust of private bankers and increasing trust for state governments.

First, the idea that federally chartered banks were somehow carrying out the policies of the federal government simply seemed absurd in light of the distrust of bankers expressed in the

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<sup>133</sup> 550 U.S. at 13-14.

<sup>134</sup> 557 U.S. 519 (2009).

<sup>135</sup> 557 U.S. at 531.

<sup>136</sup> Federal Respondent OCC’s Brief, *Cuomo v. Clearing House Ass’n*, No. 08-453, at 42 (March 25, 2009).

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Progressive and Populist politics leading up to the Wilson Administration. The Second Bank of the United States (“BUS”) might plausibly have been regarded as a federal agent akin to, say, a member of the federal reserve today: The federal government owned 20% of the BUS’s stock and appointed several of its directors, and the BUS enjoyed the unique position in holding and disbursing federal deposits in return for a sizable “bonus” paid over to the federal government. One might, therefore, regard the BUS as a sort of quasi-governmental entity like Amtrak – an entity that, while formally private, nevertheless enjoys a unique status as an agent of federal financial policy.<sup>137</sup> Nationally chartered banks, however, do not have any relationship with the federal government remotely resembling that of the Second BUS. The federal government does not appoint their directors, own their stock, or even review their federal charter according to any predictable standards.<sup>138</sup> That such banks make various marketing, lending, or deposit-taking decisions hardly means that the federal government has implicitly endorsed these decisions. To the contrary, as Louis Brandeis urged before his appointment to the U.S. Supreme Court, those decisions might be made by an “inner group of the money trust,” “builders of imperial power,” a “financial oligarchy,” without any imprimatur whatsoever from any democratically accountable federal official.<sup>139</sup>

Indeed, the very legal tradition of private implementation of public policy on which *McCulloch* rested has been swept away by late 19<sup>th</sup> century state-building. It was the norm in the early 19<sup>th</sup> century to delegate regulatory matters to essentially private actors operating for their own profit. Navy ship captains were paid through prize money from their captures, U.S. attorneys, with bounties from their victorious litigation, and so forth.<sup>140</sup> This regime of privatized government, however, was swept away by the gradual development of a professional, full-time American bureaucracy between the end of the Civil War and the New Deal. The doctrinal culmination of the disparagement of delegations of “governmental” power to private enterprises are the non-delegation decisions striking down the NIRA’s authorization for private trade associations of industry to fix prices, wages, and working conditions in fair codes of competition.<sup>141</sup> This doctrinal rejection of private delegations not tightly supervised by full-time bureaucrats is a special application of the more general idea that private entities cannot have the last word on their own regulation. This principle is so deeply rooted in American political culture that efforts to immunize federally chartered banks from state control through broad field preemption have twice collapsed.

Second, and quite apart from hostility towards bankers, the foundations of *McCulloch* were being sapped by increased judicial trust of states. Chief Justice Marshall called for a

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<sup>137</sup> *Lebron v. Nat’l Passenger Corp.*, 513 U.S. 374 (1995)(Amtrak is federal agent for purposes of First Amendment in assessing legality of restrictions on advertisements)

<sup>138</sup> Jonathan Macey & Henry Butler, *The Myth of Competition in the Dual Banking System*, 73 Cornell L. Rev. 678, 685 (1987-88)(the process of obtaining a national bank charter is untethered by any predictable standards).

<sup>139</sup> Louis Brandeis, *Other People’s Money* at 1, 35-36, 44.

<sup>140</sup> See Nicholas Parillo, *Against the Profit Motive: The Transformation of American Government, 1780-1940* (book in progress, forthcoming with Yale University Press).

<sup>141</sup> *Carter Coal; Schechter Poultry*.

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simple, formal, bright line separating federal and state jurisdiction, because he wanted the Court to be “relieved from clashing sovereignty; from interfering powers; from a repugnancy between a right in one Government to pull down what there is an acknowledged right in another to build up; from the incompatibility of a right in one Government to destroy what there is a right in another to preserve.”<sup>142</sup> Marshall’s implicit assumption – accurate in the antebellum period – was that states were itching to undermine federal policy and, therefore, needed to be restrained by clear lines rather than any “perplexing inquiry” into judgments of degrees of interference with federal ends.

By the 1920s, however, this worry about states’ making war on the federal government was obsolete, and its obsolescence led the Court to abandon antebellum notions of federal immunity from state taxes. Justice Holmes led the way in 1928 with his famous aphorism that “[t]he power to tax is not the power to destroy while this Court sits.”<sup>143</sup> Although Holmes’ phrase occurred in his dissent from an opinion barring state taxation of gasoline sold to the federal government by a private firm, Holmes’ view became the law within a decade: Rather than stop states’ usurpations with simple, bright-line rules that over-protect federal turf, the Court switched to case-by-case adjudication of mushy standards, weighing each state law against the specific federal interest that it was said to transgress. In *Graves v. People of the State of New York ex rel. O’Keefe*,<sup>144</sup> the Court finally overruled *Dobbins v. Erie County*, allowing states to tax the incomes of federal employees. In approving what he took to be the majority’s “important shift in constitutional doctrine,” Justice Frankfurter noted that the expansive scope of federal immunity from state taxes was the result of “an unfortunate remark in the opinion in *McCulloch v. Maryland* “that was “[p]artly as a flourish of rhetoric and partly ... the intellectual fashion of the times” that “indulged a free use of absolutes.”<sup>145</sup> But this penchant for “absolutes” was driven not only by “intellectual fashion” but also antebellum political realities – in particular, states’ seeking to shut down federal policy and even make war against the federal government -- that had since vanished.

The obsolescence of extreme distrust towards state governments similarly justified the Court’s shift away from field preemption of state laws regulating federally chartered banks’ banking activities. As the U.S. Supreme Court noted in *Atherton v. FDIC*,<sup>146</sup> the notion that federally chartered banks required the protection of federal common law “might have seemed a strong one during most of the first century of our Nation’s history, for then state-chartered banks were the norm and federally chartered banks an exception -- and federal banks often encountered hostility and deleterious state laws.”<sup>147</sup> That fear of state hostility to federal policy being obsolete, the capacious immunity designed to counteract it also lapsed into desuetude. *Atherton* concluded that “[t]o point to a federal charter by itself shows no conflict, threat, or need for

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<sup>142</sup> *McCulloch*, 17 U.S. at 430.

<sup>143</sup> *Panhandle Oil Company v. State of Mississippi ex rel. Knox*, 277 U.S. 218, 223 (1928)(Holmes, J., dissenting).

<sup>144</sup> 306 U.S. 466 (1939).

<sup>145</sup> *Graves*, 306 U.S. at 488 (Frankfurter, J., concurring).

<sup>146</sup> 519 U.S. 213 (1997)

<sup>147</sup> 519 U.S. at 221.

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‘federal common law.’”<sup>148</sup> For identical reasons, the mere existence of a federal charter also indicates no special need for field preemption whenever the powers associated with that charter are limited.

### IV. *McCulloch’s* Third Resurrection? The Case Against the OCC’s 2004 and 2011 Rules on Preemption

Having died two deaths already, one might think that *McCulloch’s* theory of field preemption would be well and truly buried by now. In 2004, however, the OCC revived the theory once more by issuing rules calling for the preemption of virtually any state law focused on the business of banking to the extent that such laws are enforced against nationally chartered banks. In essence, the rules reinstated the 19<sup>th</sup> century theory derived from *McCulloch* that banking-specific laws constitute a “suspect classification” for purposes of preemption under the National Bank Act.

As with *McCulloch’s* two earlier incarnations, an economic crisis has inspired a political backlash against the OCC’s 2004 attempt to insulate banks from state law. Following the collapse of real estate prices between 2007 and 2008 and the resulting wave of bank failures and bailouts, Congress enacted §1044(a) of the Dodd-Frank Act in 2010, a provision containing specific language apparently constraining the preemption of states’ “consumer financial protection laws.” In 2011, however, the OCC doubled down on its 2004 approach to preemption, re-issuing its 2004 rules in barely altered form.

As in 1832 and 1912, the stage is once more set for another legal and political showdown over federal officials’ efforts to protect national banks from state control. As I argue below, there a couple of plausible legal arguments that the OCC should lose this third round. First, as a matter of pure administrative rationality, the OCC’s 2004 and 2011 preemption rules are only tenuously related to the goal of market harmonization that the OCC proffers as their justification. Those rules are more closely geared towards protecting private bankers’ autonomy than national regulatory uniformity – an apparent purpose that should not be a surprise, given that the OCC’s rules are derived from *McCulloch’s* theory of federal instrumentalities. This mismatch between rule and justification suggests that those rules are arguably arbitrary and capricious under §706(2)(A) of the Administrative Procedure Act.

Second, §1044(a) of the Dodd-Frank Act seems to adopt an anti-banker non-delegation doctrine that, like Andrew Jackson’s 1832 campaign against Nicholas Biddle and Brandeis’ “New Freedom” campaign against the House of Morgan, rejects the idea of preempting state law without substituting equivalent federal regulation. In particular, section 1044(a)’s specific call for “case by case” evaluation of “the impact of a particular State consumer financial law on any

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<sup>148</sup> *Id.* at 223.

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national bank” is hard to explain except as a third major instantiation of the anti-banker non-delegation doctrine, requiring that, before national regulators preempt state law, they analyze the specific risks addressed by that law to insure that bankers can be trusted to self-regulate those risks. Despite their assurances to the contrary, the OCC has no such procedure in place for such analysis.

### A. The OCC’s 2004 Rules on Preemption: Reviving the Ban on Banking-Specific State Law

Provoked, in part, by states’ efforts to control so-called predator lending,<sup>149</sup> the OCC issued rules in 2004 that broadly construed the preemptive effects of federal banking laws. Regarding its visitorial powers under the National Bank Act,<sup>150</sup> the OCC took an outspoken stance against any enforcement by state officials of banking-specific laws pertaining to lending or deposit-taking.<sup>151</sup> The OCC also aggressively asserted that nationally chartered banks were free to disregard state laws dealing with dozens of categories activities specifically related to the lending of money secured by real estate, on the theory that such state laws “obstruct, impair, or condition a national bank's ability to fully exercise its Federally authorized real estate lending powers.”<sup>152</sup> The OCC emphasized that its list of preempted state limits was non-exhaustive and that other state laws could be preempted if the OCC found that they obstructed, impaired, or conditioned banks’ power to make loans secured by real estate.<sup>153</sup> The OCC qualified this apparently sweeping criterion for preemption by also listing several categories of laws such as contracts, torts, criminal law, rights to acquire and transfer real property, and rights to collect debts that were presumptively not preempted “to the extent that they only incidentally affect the exercise of national banks' real estate lending powers.”<sup>154</sup> Again, the list was non-exhaustive:

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<sup>149</sup> For an overview of “predatory lending” and state responses in the late 1990s and early 2000s, see Nicholas Bagley, *The Unwarranted Regulatory Preemption of Predatory Lending Laws*, 79 NYU L. Rev. 2274, 2277-2278 (2004). Predatory loans are loans with high fees or interest rates made to borrowers at high risk of defaulting, with the expectation that

<sup>150</sup> 12 U.S.C. §484(a).

<sup>151</sup> “Federal law commits the supervision of national banks' Federally-authorized banking business exclusively to the OCC, (except where Federal law provides otherwise), and does not apportion that responsibility among the OCC and the states.” Bank Activities & Operations, 69 Fed. Reg. 1895-01, 2004 WL 50762 at 2 (Tuesday, January 13<sup>th</sup>, 2004)

<sup>152</sup> 12 C.F.R. § 34.4(a)(real estate loans); 4007(d)(deposit-taking); 4008(d)(non-real estate loans). Each rule followed the same format, listing a dozen or types banking activities ranging from loan-to-value ratios to the use of credit ratings) the limitation of which by state law was preempted, and then listing eight or so presumptively non-preempted types of state laws that did not specifically target banking.

<sup>153</sup> “[t]he list of the types of preempted state laws is not intended to be exhaustive, and we retain the ability to address other types of state laws by order on a case-by-case basis, as appropriate, to make determinations whether they are preempted under the applicable standards.”

<sup>154</sup> 12 C.F.R. §34.4(b)(1)-(8).

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*Any* state law could escape preemption so long as “the OCC determines [the state law] to be incidental to the real estate lending operations of national banks.”<sup>155</sup>

What explains the OCC’s division of state laws into these presumptively preempted and non-preempted categories? The OCC repeatedly invoked the idea of national uniformity to facilitate an interstate market in financial services. Technological change (*e.g.*, internet banking), legal change (*e.g.*, the authorization of interstate bank branching), and increased mobility of consumers caused “[m]arkets for credit (both consumer and commercial), deposits, and many other financial products and services” to be “national, if not international, in scope.”<sup>156</sup> Such national markets required “consistent, national standards, regardless of the location of a customer when he or she first becomes a bank customer or the location to which the customer may move after becoming a bank customer.”<sup>157</sup> “[D]iverse and potentially conflicting state and local laws” impede the ability of banks to do business in multiple jurisdictions, because “the variety of state and local laws that have been enacted in recent years—including laws regulating fees, disclosures, conditions on lending, and licensing—have created higher costs and increased operational challenges” such as the customized re-programming of computer systems or customized warnings on credit card customers within a state with idiosyncratic banking requirements.<sup>158</sup> “As a result,” OCC concluded, “national banks must either absorb the costs, pass the costs on to consumers, or eliminate various products from jurisdictions where the costs are prohibitive.”<sup>159</sup>

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<sup>155</sup> 12 C.F.R. §34.4(b)(9).

<sup>156</sup> 69 FR 1904-01, at 1907-1908.

<sup>157</sup> *Id.* at 1908.

<sup>158</sup> *Id.*

<sup>159</sup> *Id.*

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This argument for a single set of rules to control a single market is essentially an argument for field preemption to realize scale economies in regulation. Using the term familiar from the jurisprudence of the European Court of Justice, one can conveniently dub such a rationale for preemption the argument from “market harmonization.”<sup>160</sup> Because one set of rules perform as well as fifty, the only effects of multiple rules are “costly and burdensome” compliance efforts that lead to “uncertain liabilities and potential exposure.”<sup>161</sup> Uniformity, on this account generates benefits regardless of the content of the uniform rules, because it is cheaper to learn and comply with one set of rules than fifty. Such a rationale implies across-the-board preemption of disuniform laws, without any case-by-case particularized inquiry into the effects of each specific rule, because the problem caused by regulatory diversity is unconnected to the rules’ content: The fact of regulatory diversity alone leads to unjustified regulatory costs. Professor Tom Merrill terms such preemption the “displacement” of state law that “radically simplifies the regulatory structure in any given area, replacing a *mélange* of federal, state, and local requirements with a single set of federal rules.”<sup>162</sup> As Merrill notes, such a decision rests on a general judgment “about the benefits and costs of legal uniformity,” not any individualized determination that some particular state rule interferes with any specific federal rule.<sup>163</sup>

In short, despite the OCC’s disclaimers to the contrary,<sup>164</sup> the OCC’s rationale for its 2004 rules, with its emphasis on the overall benefits of regulatory uniformity regardless of the content of any specific state banking rule, appears to have adopted a regime of field preemption. As I shall suggest below, there are both legal reasons and policy reasons deeply rooted more in American political culture to believe that this field preemption regime is illegal and ill-advised.

### B. [Are OCC’s preemption rules rationally related to the goal of market harmonization?](#)

How well does market harmonization explain or justify the OCC’s preemption rules? The rationale seems remote from the OCC’s revival of *McCulloch*’s distinction between general and banking-specific laws, because that distinction was designed for an entirely different purpose – the protection of nationally chartered banks from hostile state legislation. By leaving states’ general common-law doctrines largely intact, the OCC has pursued the goal of national uniformity with extraordinary under-inclusiveness. Given this under-inclusiveness, OCC’s rules seem only tenuously related to the goal of creating a nationally uniform system of rules for banks. The irrationality of the OCC’s rules are only exacerbated by the OCC’s inability to provide any coherent account of what it means for general state law to constitute permissible

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<sup>160</sup> Paul Craig & Grainne De Burca, *EU Law: Text, Cases, and Materials* 613-677 (3d ed. 2003).

<sup>161</sup> *Id.*

<sup>162</sup> Merrill, 102 Nw. L. Rev. at 732.

<sup>163</sup> *Id.* at 733.

<sup>164</sup> 76 FR 43549-01, at 43556 (“[T]hese rules are not based on a field preemption standard.[FN44] They were based on the OCC’s conclusion that the listed types and terms of state laws would be preempted by application of the conflict preemption standard of the *Barnett* decision”).

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“legal infrastructure” for banking, as opposed to impermissible impediments to national banks’ powers.

That common-law claims can have the same regulatory purpose and effects as rules enforced by administrative agencies is hardly a novelty. As the U.S. Supreme Court now regularly announces, “a liability award ‘can be, indeed is designed to be, a potent method of governing conduct and controlling policy.’”<sup>165</sup> Moreover, that regulatory purpose and effect is not mitigated by the generality of the underlying common-law standard. If a bank is held liable for abusive debt collection practices because (for instance) it made use of harassing or deceptive telephone calls to dun a debtor, the fact that the underlying common-law or statutory cause of action does not turn on the defendant’s identity as a bank will not affect the incentives created by such liability: Regardless of the underlying state rule’s general phrasing, the bank will still have to change its behavior with respect to borrowers or face a (using the OCC’s phrase) “uncertain liabilities and potential exposure.”<sup>166</sup> As the U.S. Supreme Court has noted, “there is little reason why state impairment of the federal scheme should be deemed acceptable so long as it is effected by the particularized application of a general statute.”<sup>167</sup> In short, OCC’s ban on state laws’ “singling out” banking practices is completely orthogonal to their rational of harmonizing markets.

Aware that even general state laws can effectively regulate banking activities in precisely the same ways as banking-specific state laws, OCC does not automatically give blanket approval to any state law that is general in form.<sup>168</sup> Instead, OCC’s rules provide that general state laws escape preemption only if they are “not inconsistent with the real estate lending powers of national banks” and “only incidentally affect the exercise of national banks’ real estate lending powers.”<sup>169</sup>

But what does it mean for a state law to affect banking “incidentally”? OCC has invoked the metaphor of “legal infrastructure” to explain “incidental” effects, stating that the critical question is whether or not the state laws “form the legal infrastructure that makes it practicable to exercise a permissible Federal power.”<sup>170</sup> General laws that constitute such “legal infrastructure” are not preempted, because their effects on banking are “incidental.” By contrast, state laws that “attempt to regulate the manner or content of national banks’ real estate lending” are preempted even if those laws are general in form.

The term “legal infrastructure,” however, is a metaphor vainly searching for some unambiguous definition. OCC is surely correct that, at least since *Erie* and arguably since 1882 (when national banks lost their automatic capacity to remove litigation to federal courts), national banks depend on state law to avoid anarchy, because there has been no general federal

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<sup>165</sup> See *Kurns v. Railroad Friction Products Corp.*, 132 S. Ct. 1261, 1270 (2012).

<sup>166</sup> 69 FR 1904-01, at 1907-1908.

<sup>167</sup> *Morales v. Trans World Airlines*, 504 U.S. 374, 388-89 (1992).

<sup>168</sup> “The label a state attaches to its laws will not affect the analysis of whether that law is preempted.” 69 FR 1904-01, at 1912

<sup>169</sup> 12 C.F.R. §34.4(b).

<sup>170</sup> *Id.*

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common law to define banks' powers to engage in banking business.<sup>171</sup> Without state law, national banks would not be liberated from legal burdens but rather be relegated to legal anarchy. One cannot, after all, lend money without contract law or hold title to real property without property law, and neither OCC nor the federal courts are willing to supply such rules.

The difficulty, however, is that even the most traditional common-law rules of contract, property, debt collection, and so forth all contain limits on the powers that they confer, and these limits address evils like consumer ignorance, unequal bargaining power, deceptive trade practices, problems in proving consent arising from forgery, duress, and the like – all of which are precisely the mischiefs against which banking-specific state laws are also directed. If a state's common law of contracts limits the power of a bank to enforce a bargain, is this limit part of the “legal infrastructure” necessary for banking business? Or is it an impediment to a banking power that should be preempted as outside such “infrastructure”?

The metaphor of “infrastructure” by itself obviously will not answer this question. One gets the sense that OCC regards legitimate common-law rules as defining a road over which banking bargains can be driven, while preempted rules constitute mere road blocks and impediments to commerce. But the distinction implied by the metaphor turns out to be malleable and confusing: Roads, after all, need rules, traffic signs, and signals if traffic is to move smoothly, and such rules will slow traffic down and re-direct it to safe routes as well as speed traffic up. How, then, can one distinguish between those commerce-guiding rules that facilitate banking business rather than impermissibly impede it?

The OCC has nothing to say on the definition of “legal infrastructure” that is neither an empty tautology nor patently incorrect. Take, for instance, the following passage from the OCC's rule on visitorial powers, in which the OCC explains that “legal infrastructure”

typically does not affect the content or extent of the Federally-authorized business of banking conducted by national banks, but rather establishes the legal infrastructure that surrounds and supports the ability of national banks—and others—to do business. In other words, these state laws provide a framework for a national bank's ability to exercise powers granted under Federal law; they do not obstruct or condition a national bank's exercise of those powers.<sup>172</sup>

This statement, taken literally, is absurd. How can it be that a common-law rule of contract law “typically does not affect the content or extent ... of the ... business of banking”? Common-law rules provide contractual procedures that are designed to reduce fraud and deception, increase parties' information, and otherwise insure that bargains reflect preferences. By definition, such rules change the content of bargains by eliminating the fraudulent bargains and promoting the

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<sup>171</sup> *O'Melveny & Myers v. F.D.I.C.*, 512 U.S. 79, 88 (1994) (“[u]niformity of law might facilitate the [federal agencies'] nationwide litigation of these suits, eliminating state-by-state research and reducing uncertainty -- but if the avoidance of those ordinary consequences qualified as an identifiable federal interest, we would be awash in 'federal common-law' rules”).

<sup>172</sup> 69 FR 1895-01, at 1896.

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honest ones. Likewise, contract law regularly reduces the “extent” of bargains by rendering some contracts illegal that might otherwise be enforced. As *McClellan* – a case approved by OCC -- noted, “[o]f course, in the broadest sense, any limitation by a state on the making of contracts is a restraint upon the power of a national bank within the state to make such contracts” -- *i.e.*, contracts for “the taking of real estate as a security for an antecedent debt.”<sup>173</sup> If a state bars a sixteen year old from making a credit card contract, then the extent of credit card contracts will be diminished, but OCC would surely not regard this law as impermissibly impeding national banks’ powers to make loans or take deposits.

The confusion inherent in OCC’s concept of “legal infrastructure” is well-illustrated by *Monroe Retail, Inc. v. RBS Citizens, N.A.*<sup>174</sup> The issue in *Monroe Retail* was whether national banks violated Ohio’s anti-conversion law by charging between \$25 and \$80 to garnish debtors’ bank accounts on behalf of creditor-retailers. The retailers argued that, because Ohio law allowed banks to charge only one dollar to cover the administrative costs of garnishing debtors’ bank accounts, the extra fees charged by the banks (which frequently left no money to satisfy the garnishor-creditors’ claims) constituted illegal conversion under Ohio law. In response, the banks argued that Ohio’s conversion laws were preempted, because OCC’s rules barred state laws limiting an “activity incidental to receiving deposits” such as charging a fee.<sup>175</sup> According to the banks, the OCC rules’ protection for “rights to collect debts”<sup>176</sup> applied only to *the banks’* rights to collect debts: The very same state law could be preempted or not preempted, depending on whether a bank was seeking the benefit of the law.

Not surprisingly, the Sixth Circuit rejected this one-sided view of banking preemption, simply because it “defies common sense.”<sup>177</sup> That view, however, even if absurd, was consistent with the literal meaning of the OCC’s definition of “legal infrastructure” stating that state law counts as part of the permissible “legal infrastructure” only if it does not “obstruct or condition a national bank’s exercise of [federally conferred] powers.”<sup>178</sup> If a national bank loses a case as a result of state law, then why have its powers not been obstructed or conditioned?

The OCC, in short, has adopted a definition of permissible “legal infrastructure” the literal terms of which are absurd and, therefore, untenable.<sup>179</sup> Yet it is not obvious how the absurdity can be cured short of simply enforcing every generally applicable state law that does not subject the business of banking to any special conditions. With a few exceptions, this is the course that lower courts have taken. Thus, courts have consistently sided with OCC’s efforts to preempt state regulations specifically directed towards banking practices, rejecting state efforts

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<sup>173</sup> *McClellan*, at 358.

<sup>174</sup> 589 F.3d 274 (6<sup>th</sup> Cir. 2009).

<sup>175</sup> The rule on which the banks relied is codified at 12 C.F.R. §7.4007(a) (“any activity incidental to receiving deposits”)

<sup>176</sup> 12 C.F.R. § 7.4007(c)(4)(“right to collect debts”).

<sup>177</sup> *Monroe Retail*, 589 F.3d at 282.

<sup>178</sup> 69 FR 1895-01, at 1896.

<sup>179</sup> On legal asymmetry of rights between parties as an indication of absurdity calling for rejection of the literal meaning of the text that produces the asymmetry, see *Green v. Bock Laundry*.

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to subject national banks to comprehensive licensing schemes,<sup>180</sup> mandated disclosures,<sup>181</sup> various forms of price regulation for ATM fees or check-cashing,<sup>182</sup> anti-usury limits on interest rates,<sup>183</sup> or (most controversially) bans on lending practices deemed to be “predatory.”<sup>184</sup> But courts have also allowed private claims rooted in more general state common law doctrines or general statutes defining anti-consumer fraud. These general state-law claims have taken a wide variety of forms, including allegations that either national banks or mortgage servicers claiming to act on their behalf should be held liable for deception in the sale of liens,<sup>185</sup> “unconscionably” skimming home equity with fraudulent appraisals or over-estimating a borrowers’ income in approving a loan,<sup>186</sup> involuntarily enrolling plaintiff in credit card program in violation of state false claims act,<sup>187</sup> “unconscionably” harassing debtors to collect payment in violation of state consumer protection statute,<sup>188</sup> illegally turning tax refund anticipation loan proceeds over to other banks to satisfy plaintiff’s pre-existing debts in violation of state debt collection rules,<sup>189</sup> “wrongfully” demanding excessive service charges in connection with mortgage foreclosures in

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<sup>180</sup> *Wells Fargo Bank N.A. v. Boutris*, 419 F.3d 949 (9th Cir. 2005)(holding that National Bank Act preempts California’s system for licensing real estate lending); *Wachovia Bank, N.A. v. Burke*, 414 F.3d 305 (2d Cir. 2005)(holding that National Banking Act and OCC rules prohibit Connecticut bank regulators from imposing state licensing requirements on mortgage subsidiary of a national bank).

<sup>181</sup> *Rose v. Chase Bank*, 513 F.3d 1032 (9<sup>th</sup> Cir. 2008)(barring California’s requirement of specific disclosures to accompany bank offers of credit cards as preempted by National Bank Act’s authorization to “loan money on personal security”).

<sup>182</sup> *National City Bank of Indiana v. Turnbaugh*, 463 F.3d 325 (4th Cir. 2006)(holding preempted Maryland law that restricts amount of prepayment fees a national bank or its mortgage lending subsidiary may impose upon borrowers); *Wells Fargo Bank of Tex., N.A. v. James*, 321 F.3d 488 (5th Cir. 2003) (holding that Texas law prohibiting banks from charging check-cashing fees was preempted by OCC regulation permitting national banks to charge “non-interest charges and fees”); *Bank of America v. City & County of San Francisco*, 309 F.3d 551 (9th Cir.2002)(striking down San Francisco’s ban on banks’ charging non-account holders for use of ATM machines).

<sup>183</sup> *Discover Bank v. Vaden*, 489 F.3d 594 (4<sup>th</sup> Cir. 2007).

<sup>184</sup> North Carolina was the first state to enact a statute banning banking practices targeting low-income and unsophisticated borrowers to induce them to borrow more than they can re-pay and thereby generate loan origination fees or strip borrowers of home equity. Act to Prohibit Predatory Lending, 1999 N.C. Sess. Laws 332 (codified at N.C. Gen. Stat. § 24-1.1A - 10.2 (2003)). Georgia followed with a statute of its own in 2004. Ga. Code Ann. § 7-6A (2004). OCC’s rules preempting state regulation of lending and deposit-taking was promulgated shortly after, and in response to, Georgia’s statute. See Bank Activities and Operations; Real Estate Lending and Appraisals, 69 Fed. Reg. 1904, 1917 (Jan. 13, 2004) (codified at 12 C.F.R. § 34.4(a) (2005)).

<sup>185</sup> *Gerber v. Wells Fargo Bank, N.A.*, Slip Copy, 2012 WL 413997 (D.Ariz 2012)(Consumer Fraud Claim based on deception in the sale of a lien that was junior but not so disclosed by Wells Fargo (the seller), not preempted).

<sup>186</sup> *In re Moore*, 2012 WL 872239 (Bkrtcy.S.D.W.Va. 2012); *Conrad v. Wells Fargo Bank, N.A.*, No. 08-0829, 2009 WL 36478, at \*2-3 (S.D. W. Va. Jan. 5, 2009) (no preemption of claims that bank engaged in pattern of home equity skimming and predatory lending practices to make unfair loans based on fraudulent appraisals).

<sup>187</sup> *Arevalo v. Bank of America*, 2011 WL 1195973 (N.D.Cal. 2012)(allowing claims against national bank under California’s Consumer Legal Remedies Act and False Advertising Law for involuntarily enrolling plaintiff in credit card program, rejecting bank’s preemption defense).

<sup>188</sup> *Smith v. BAC Home Loans Servicing, LP*, 769 F.Supp.2d 1033 (S.D.W.Va. 2011)(National Bank Act (NBA) and regulations promulgated thereunder by Office of Comptroller of Currency did not preempt borrower’s claims against mortgage servicer for misrepresentation and unconscionable and unfair debt collection practices, in violation of West Virginia Consumer Credit and Protection Act); *Cline v. Bank of America*, 2011 WL 4857934 (S.D.W.Va. 2011)(same).

<sup>189</sup> *Hood v. Santa Barbara Bank & Trust*, 143 Cal.App.4th 526, 49 Cal.Rptr.3d 369 (Cal.App. 2006)

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violation of state Unfair Trade Practices Law,<sup>190</sup> or “fraudulently” adjusting the order in which ATM fees were posted in order to maximize overdraft fees.<sup>191</sup>

It is easy to see that virtually any banking-specific prohibition can be re-framed as a general common-law or statutory theory under a law that makes no mention of banking in particular. Indeed, some courts have allowed general state-law claims of “unfair” trade practices, even when these claims incorporate statutory standards rules peculiar to lending as the standard for liability. In *Aguayo v. U.S. Bank*,<sup>192</sup> for instance, the Ninth Circuit characterized the California Rees–Levering Act's post-repossession notice requirements as pertaining to “rights to collect debts” (a non-preempted category under OCC’s rules) rather than a “state law concerning [d]isclosure and advertising” (a preempted category, according to the OCC). The notice requirements were not vague common-law injunctions to be “fair” or avoid “fraud” but rather bright-line regulatory mandates to provide detailed information to the borrower after the lender re-possesses a motor vehicle for non-payment of a loan. Because the plaintiff had advanced the bank’s non-compliance with the state’s bright-line rules in the form of a private claim brought under California’s Unfair Competition Law, the *Aguayo* court treated the state’s regulatory mandates as fitting in with other private-law claims that OCC seemed to preserve. Even when courts disallow general claims as effectively targeting banking practices, they do not offer any clear criteria for distinguishing permissible from preempted state rules. Thus, the power to invoke preemption of general state law hangs on arbitrary and unpredictable matters of legal characterization. In *Martinez v. Wells, Fargo Home Mortgage*,<sup>193</sup> for instance, the Ninth Circuit held that the plaintiff’s state-law claim alleging fraudulent failure to disclose closing costs was preempted by OCC’s rule authorizing non-interest charges and fees. The Court offered no reason why the state-law claim should be preempted as a regulation of fees and charges under OCC’s rule preempting states’ regulation of non-interest fees rather than permitted as a state contract or tort claim under OCC’s rule preserving state common law. *Martinez* and other decisions like it<sup>194</sup> seem to be based on nothing more than purely arbitrary characterization of a

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<sup>190</sup> *In re Ocwen Servicing, LLC*, 491 F.3d 638 (7th Cir. 2007)(Office of Thrift Supervision’s rules implementing Home Owners Loan Act do not “deprive persons harmed by the wrongful acts of savings and loan associations of their basic state common-law-type remedies”).

<sup>191</sup> *In re Check Account Overdraft Litigation*, No. 09-MD-02036-JLK, 2011 WL 4454913 at \*4 (S.D. Fla. Sept. 1, 2011)(holding that liability under state law for banks’ “largest to smallest” posting policy was not preempted by OCC’s 2011 rules authorizing non-interest fees and guidance allowing posting of withdrawals in any order), reversed in part by *In re Checking Account Overdraft Litigation*, Slip Copy, 2012 WL 660974 (11<sup>th</sup> Cir. 2012)(holding that waiver of trial by arbitration clause was not unconscionable); *White v. Wachovia Bank, N.A.*, 563 F.Supp.2d 1358 (N.D.Ga.2008) (same holding construing OCC’s 2004 rules)

<sup>192</sup> 653 F.3d 912 (9th Cir. 2011).

<sup>193</sup> 598 F.3d 549 (9th Cir. 2010) .

<sup>194</sup> See, e.g., *Wier v Countrywide Bank*, (E.D. Mich. 2011)(finding preemption of state-law claim of fraudulent inducement and misrepresentation); *Austin v. Provident Bank*, 2005 WL 1785285 (N.D.Miss. 2005)(finding preemption of common-law fraud claims that lenders entered into a deliberate, systematic plan of targeting to disadvantaged individuals in need of financing who were more vulnerable to the defendants' practices of selling over-priced loans at excessive interest rates).

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private claim as either contract, tort, or collection of debts (in which claim is not preempted) or as regulation of banks (in which case the claim is presumptively preempted).

OCC's rules, in short, invite unpredictable arguments about how to characterize a state law (as "infrastructure" that "incidentally" affects banking or as a "significant impairment" to banking). This is not the only sort of unpredictability promoted by the rules. They also encourage vague common-law standards enforced with *ex post* damages while preempting crisply defined *ex ante* rules. General common-law theories of fraud are rooted in fuzzy legal standards that are cashed out in a specific case only after a verdict is rendered. By contrast, state laws specifically directed towards banking can be crisply defined duties that banks can easily identify in advance of a dispute. If market harmonization is one's goals, why would one seek to prohibit the predictable legal duty, defined *ex ante* in a statute or regulation, but allow the vague and unpredictable legal duty, enforced *ex post* through damages?

The paradox is well-illustrated by the California supreme court's recent decision in *Parks v. MNBA, N.A.*,<sup>195</sup> striking down a California statute regulating so-called "convenience checks." The California supreme court held that this state law, which required that certain specific disclosures be printed on the front of preprinted checks sent to credit card holders, was preempted by the National Bank Act, because it limited the bank's powers to enter into agreements for the lending of personal credit. In reaching this conclusion, however, *Parks* distinguished *Perdue v. Crocker National Bank*,<sup>196</sup> a decision holding that banking laws did not preempt state-law theories that bank charges for overdrawn accounts were based on unconscionable contracts. Unlike theories of unconscionability, *Parks* reasoned,

[California's disclosure requirement] does not state a background legal principle against fraudulent, deceptive, or unconscionable practices. It prescribes specific and affirmative conduct that credit card issuers must undertake if they wish to lend money through convenience checks. Unlike the state law considered in *Perdue*, the disclosure requirements of [California's disclosure requirement] cannot be understood as part of the general legal backdrop to Congress' enactment of federal banking legislation.

The passage illustrates the paradox of the OCC's distinction: How does it advance the goal of reducing the costs of banks' compliance with multiple state laws to preempt requirements of "specific and affirmative conduct" in favor of amorphous "background legal principles" barring "unconscionable" conduct? Surely, the latter deters as much or more banking practices than the former, if only because the bank has to tailor its conduct to create a margin of safety to safeguard against liability under an unpredictable standard.

In sum, the OCC's preemption rule hardly seems well-suited for producing uniform and predictable national rules that advance the goal of market harmonization. Indeed, the distinction

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<sup>195</sup> 54 Cal.4th 376, 278 P.3d 1193 (June 21<sup>st</sup>. 2012)

<sup>196</sup>38 Cal.3d 913, 932-944 (1985)

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between general and banking-specific state laws is so unrelated to the proffered goal that one suspects that the latter is mere pretext for some other justification.

An obvious alternative candidate immediately suggests itself as the more likely justification of the OCC's preemption rule: The OCC is reviving the twice-buried theory of field preemption first set forth in *McCulloch* as a way to protect federal instrumentalities from state interference while simultaneously preserving some scope for state law.

Consider two reasons why such an explanation seems more plausible than OCC's proffered justification of market harmonization. First, the shoe fits: As argued above in Part III, the distinction between general state laws and banking-specific state laws is precisely the distinction adopted by 19<sup>th</sup> century courts trying to extend *McCulloch* from taxation to regulation. The intuitively obvious point of declaring banking-specific laws to be suspect classification is not to secure uniformity but rather to protect banks from hostile legislation. Such suspicion towards banking-specific laws still leaves in place a vast amount of regulatory diversity that is not targeted at banking.

Second, OCC devoted much of its justification for its rule to quotations from opinions invoking *McCulloch* and the idea of the immunity of federal instrumentalities from state law as the justification for preempting state law. At the same time, OCC ignored or minimized the importance of precedents that had earlier abandoned the idea of federal instrumentalities' immunity. Ignoring *First Nat'l Bank of Bay City v. Fellows*,<sup>197</sup> the OCC's reasons for its rule on visitorial powers quoted heavily from *Dearing* and *Easton*<sup>198</sup> while distinguishing *Nat'l Bank of St. Louis*<sup>199</sup> as resting on "a unique set of circumstances, now outdated."<sup>200</sup> The OCC made no mention of Justice Van Devanter's dissenting opinion – joined by Chief Justice Taft – that *St. Louis*, in fact, undercut the basic premise of *McCulloch*. The OCC underscored how closely they were following the old jurisprudence by basing the list of non-preempted areas closely on the U.S. Supreme Court's language in *National Bank v. Commonwealth* (1869)<sup>201</sup> to include "debt collection" among the categories of non-preempted laws,<sup>202</sup> because *Commonwealth* included debt collection.<sup>203</sup> The OCC's rule on deposit-taking grudgingly acknowledges that preemption of state laws on "abandoned and dormant accounts ... does not apply to state laws of the type upheld by the United States Supreme Court in *Anderson Nat'l Bank v. Lockett*, 321 U.S. 233 (1944),"<sup>204</sup> but the OCC says nothing whatsoever about *Lockett*'s reasoning – in particular, its rejection of the idea that federal law preempts all banking-specific laws.

In sum, the OCC's field preemption of state banking rules is best explained as an effort to protect the autonomy of private bankers rather than the national uniformity of banking rules.

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<sup>197</sup> 244 U.S. 416 (1917).

<sup>198</sup> 69 Fed. Reg. 1895-01, 2004 WL 50762, at 9-10.

<sup>199</sup> 263 U.S. 640 (1924).

<sup>200</sup> *Id.* at 12.

<sup>201</sup> 76 U.S. (9 Wall.) 353 (1869).

<sup>202</sup> 69 FR 1904-01, 2004 WL 50763, at 16-17.

<sup>203</sup> *Commonwealth*, at 362 ("Their acquisition and transfer of property, their right to collect their debts, and their liability to be sued for debts, are all based on State law").

<sup>204</sup> 12 C.F.R. §7.4007(b)(1) at n. 3.

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The former goal has a distinguished pedigree, dating back to *McCulloch*'s effort to protect the Second Bank of the United States from state harassment. The OCC, however, did not articulate such a purpose for its rule. The mismatch between rule and reason might be a ground for striking down the former under §706(2)(A). Although the standards of justification under the Administrative Procedure Act are deferential, an agency must nevertheless articulate in the administrative record the actual basis on which its actions are to be sustained.<sup>205</sup> That principle might apply all the more powerfully to the OCC's preemption rules, because there are good reasons to be skeptical about *McCulloch*'s principle that private bankers constitute federal instrumentalities entitled to exercise autonomous judgment, free from governmental oversight. By hiding behind rhetoric about the importance of national regulatory uniformity for interstate commerce, rhetoric largely unrelated to the rule that OCC promulgated, the OCC has avoided substantive analysis of *McCulloch*'s principle regarding the independence of federal instrumentalities from state law – the principle that seems to be the actual basis for the OCC's rules.

### C. Are the OCC's preemption rules consistent with the Dodd-Frank Act's standards for preemption?

Quite apart from the OCC's compliance with principles of administrative rationality, OCC's 2011 rules are arguably inconsistent with §1044(a) of the Dodd-Frank Act. The question turns on whether one reads §1044(a) as a re-assertion of the anti-banker non-delegation doctrine. There is both statutory text and legislative history suggesting that §1044(a) finally repudiates the sort of categorical field preemption that, under *McCulloch* and its post-Civil War progeny, precluded states from enforcing banking-specific rules against nationally chartered banks. One might reasonably construe §1044(a) as a third rejection, after Andrew Jackson's 1832 campaign against Nicholas Biddle and Louis Brandeis' 1912 campaign against the House of Morgan, of the idea of granting private banks broad powers of self-governance, free from state or federal oversight. To the extent that OCC's 2011 rules adopt such across-the-board preemption of state law without replacing the preempted state law with some federal substitute, those rules might fall outside §1044(a), so construed.

Section 1044(a) in the Dodd-Frank Act provides an elaborate set of rule to govern preemption of states' enforcing their "consumer financial protection laws" against national banks.<sup>206</sup> Under Dodd-Frank's preemption standard, "consumer financial protection laws" would be preempted by federal banking laws only if they discriminated against national banks or "prevent[ed] or significantly interfere[d] with the exercise by the national bank of its powers" as measured according to "the legal standard for preemption in ... *Barnett Bank of Marion County, N. A. v. Nelson, Florida Insurance Commissioner et al.*, 517 U.S. 25 (1996)."<sup>207</sup> The Dodd-

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<sup>205</sup> *State Farm; Chenery*. Etc.

<sup>206</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, §1044(a), 124 Stat. 1376 (2010) (adding 12 U.S.C. §§25b(b)(1)(B), 25b(b)(3)(A), 25b(b)(3)(B), 25b(b)(4), and 25b(c)).

<sup>207</sup> 12 U.S.C. § 25b(b)(1)(B).

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Frank Act specifically required such preemption determinations be made “on a case-by-case basis,” analyzing “the impact of a particular State consumer financial law on any national bank that is subject to that law,”<sup>208</sup> with those case-by-case determinations supported by “substantial evidence, made on the record of the proceeding.”<sup>209</sup> The statute also specifically rejected “field preemption” under either the National Bank Act or the Home Owner Loan Act.<sup>210</sup>

Section 1044(a)’s incorporation of the *Barnett Bank* standard is hardly unambiguous. In holding that a Florida law banning certain banks from engaging in the business of selling insurance, *Barnett Bank* implied that some state laws barring banking activities permissible under federal law could be deemed to “impair significantly” federal “powers that Congress explicitly granted.”<sup>211</sup> As noted in Part III, however, not all states’ laws targeting banking activities permitted by federal law could count as such “significant impairment,” or else *Barnett Bank* could not approvingly cite *Luckett* for the proposition that federal banking law does not “deprive States of the power to regulate national banks, where (unlike here) doing so does not prevent or significantly interfere with the national bank’s exercise of its powers.”<sup>212</sup> *Barnett Bank* did not explain what distinguished Kentucky’s requirement in *Luckett* that certain bank accounts be deemed abandoned and, therefore, escheat to the Commonwealth from Florida’s prohibition on certain banks’ engaging in the insurance business. In both cases, the powers prohibited by state law (*i.e.*, maintaining bank accounts or selling insurance) were permitted by federal law. One could try to distinguish *Luckett* from *Barnett* by arguing that the 1916 federal statute at issue in *Barnett Bank* more “explicitly” addressed the topic covered by the Florida law than the National Bank Act addressed the issue of abandoned bank accounts. In *Luckett*, there was, after all, no express power to maintain indefinitely bank accounts free from rules defining abandonment. By contrast, the 1916 federal statute did expressly address the topic of insurance sales – albeit not by bank holding companies, which was the type of insurance business forbidden by the preempted Florida law.

*Barnett Bank*, however, never defined the degree of specificity of federal authorization sufficient to preempt state law, aside from its two-word reference to federal powers “explicitly granted.” One might, therefore, regard Congress’ adoption of the *Barnett Bank* standard as a decision to incorporate a deliberately vague legal standard and thereby avoid resolving the contentious question of the precise degree to which federal law preempted state banking rules. The scope of federal preemption was hotly contested after the OCC’s 2004 rules were invoked to preempt states’ prohibitions on predatory lending. Consumer advocates, claiming that the OCC had been “captured” by banks on which OCC was dependent for its revenue in the form of chartering fees,<sup>213</sup> attempted to shrink the scope of banking preemption as much as possible. The

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<sup>208</sup> 12 U.S.C. §§25b(b)(1)(B) & 25b(b)(3)(A).

<sup>209</sup> 12 U.S.C. § 25b(c)

<sup>210</sup> 12 U.S.C. §25b(b)(4).

<sup>211</sup> *Barnett*, 517 U. S. 25, 32, 33 (1996).

<sup>212</sup> *Barnett*, 517 U.S. at 33.

<sup>213</sup> See Oren Bar-Gill & Elizabeth Warren, Making Credit Safer, 157 U. Pa. L. Rev. 1, 87-98 (2008)(describing OCC’s fee-based incentive to attract banks to the national charter); Vincent DiLorenzo, Federalism, Consumer Protection

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banks' advocates in Congress like Representative Melissa Bean of Illinois, by contrast, tried to preserve the preemption provided by existing precedent.<sup>214</sup> *Barnett Bank* was a convenient vehicle by which these pro- and anti-bank factions could compromise through what Professor Victoria Nourse has termed “structure-induced ambiguity,”<sup>215</sup> thereby side-stepping vetogates and resulting gridlock in the bicameral process.

One does not, however, have to know how *Barnett Bank* defines “significant impairment” of banking powers to determine that *Barnett Bank* unambiguously rejects *McCulloch*. *Barnett*'s embrace of *Luckett*, as noted above in Part II, suggests as much. Likewise, by operation of the *pari materia* canon, §1044(a) incorporates the Court's 2009 decision in *Cuomo v. Clearing House Ass'n*<sup>216</sup> just as clearly as it incorporates *Luckett*, because *Clearing House Ass'n* construed the *Barnett Bank* standard on the eve of §1044(a)'s enactment. *Clearing House Ass'n* expressly rejected the distinction between general state laws and state laws specifically targeting banking, observing that the distinction, proposed by the OCC to justify its ban on state officials' enforcing state fair lending laws, “[o]f course . . . can be found nowhere within the text of the statute” and, therefore, “attempts to do what Congress declined to do: exempt national banks from all state banking laws, or at least state enforcement of those laws.”<sup>217</sup>

*Barnett Bank*'s exclusion of broad *McCulloch*-style preemption is further suggested by §1044(a)'s requirement that the OCC's preemption determinations be made “on a case-by-case basis,” analyzing “the impact of a particular State consumer financial law on any national bank that is subject to that law,”<sup>218</sup> with those case-by-case determinations supported by “substantial evidence, made on the record of the proceeding.”<sup>219</sup> Like the *Barnett Bank* standard itself, these procedural requirements are not self-explanatory. By requiring some sort of “case-by-case” examination of the “impact” of “particular” state laws, however, these provisions preclude preemption on the basis of the mere linguistic form of the state law. Yet preemption of state

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and Regulatory Preemption: A Case for Heightened Judicial Review, 10 U. Pa. J. of Bus. & Emp. L. 274, 281 (2008) (“[T]he OCC has not acted as a neutral forum to resolve conflicting policies. Rather it has acted as an advocate for the interests of national banks and therefore an advocate for the broadest possible preemption of state law.”); Arthur E. Wilmarth, Jr., *Cuomo v. Clearing House: The Supreme Court Responds to the Subprime Financial Crisis and Delivers a Major Victory for the Dual Banking System and Consumer Protection*, in *The Panic of 2008: Causes, Consequences and Implications for Reform* 295, 335 n.89 (Lawrence E. Mitchell & Arthur E. Wilmarth, Jr. eds., 2010); Arthur E. Wilmarth, Jr., *The OCC's Preemption Rules Exceed the Agency's Authority and Present a Serious Threat to the Dual Banking System and Consumer Protection*, 23 Ann. Rev. Banking & Fin. L. 225, 315 (2004); Nicholas Bagley, Note, *The Unwarranted Regulatory Preemption of Predatory Lending Laws*, 79 N.Y.U. L. Rev. 2274, 2274 (2004) (arguing that “the OCC overstepped its congressionally delegated authority when it promulgated the regulation”).

<sup>214</sup> Extension of Remarks of Rep. Melissa Bean, 55 Cong. Rec. E3029-E3030 (Thursday, Dec. 17, 2009). For a brief overview of the preemption provision's contested legislative history, see Jamelle Sharp, *Legislating Preemption*, 53 Wm. & Mary L. Rev. 163, 221-23 (2011).

<sup>215</sup> See Victoria Nourse, *Misunderstanding Congress: Statutory Interpretation, the Supermajoritarian Difficulty, and the Separation of Powers*, 99 Geo. L. J. 1119 (2011).

<sup>216</sup> 557 U.S. 519 (2009).

<sup>217</sup> 557 U.S. at 531.

<sup>218</sup> 12 U.S.C. §§25b(b)(1)(B) & 25b(b)(3)(A).

<sup>219</sup> 12 U.S.C. § 25b(c)

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laws based on their generality seems like precisely the sort of merely formal and linguistic inquiry that §1044(a) precludes.

Section 1044(a), in sum, seems finally and unambiguously to overrule *McCulloch*'s field preemption based exclusively on the state law's targeting banking activities for special regulatory treatment. With what exactly §1044(a) replaces the *McCulloch* standard remains ambiguous – but that ambiguity does not cast doubt on §1044(a)'s unambiguously eliminating *McCulloch*'s ban on banking-specific laws after almost two centuries of on-again/off-again existence. The question, however, remains whether the OCC's 2011 rules offended §1044(a)'s unambiguous limit on preemption. Did the OCC shunt aside state regulations of national banks' deposit-taking and lending operations simply because these regulations focused on banking? Or did the OCC provide a more differentiated evaluation of particular state laws by relying on something other than their targeting banking activities?

The OCC's 2011 rules were, to the outrage of its critics,<sup>220</sup> largely copies of the 2004 rules. While making necessary adjustments to its rule regarding the exclusivity of OCC's visitorial powers to accommodate the U.S. Supreme Court's decision in *Cuomo v. Clearing House Ass'n*, OCC largely left intact its 2004 rules preempting broad categories of state laws.<sup>221</sup> The basic approach in 2011 remained the same as in 2004: The OCC listed categories of state laws that were preempted all of which specifically regulated deposit-taking or lending operations were preempted while more general state laws that did not specifically refer to banking activities were saved so long as their impact on banking was "incidental." In defense of its decision to "double down" on its 2004 revival of *McCulloch*'s approach to preemption, the OCC stated that its 2004 rules had been expressly designed to be consistent with the Court's decision in *Barnett Bank*. Since the Dodd-Frank Act specifically incorporated this standard, OCC regarded its old rules as consistent with the new statutory language. As for the requirements for a case-by-case analysis of particular state laws' impact backed by substantial evidence in the record, OCC argued that these were procedural requirements that were not intended to apply retroactively to rules enacted before the Dodd-Frank Act became effective.<sup>222</sup>

Against both the OCC's 2004 and 2011 rules, one could argue that the OCC was adopting *McCulloch*'s theory of field preemption, because the OCC's rules closely copied the Office of Thrift Supervision's ("OTS's") 1996 rules defining preemption of state law under the Home Owners' Loan Act of 1933 ("HOLA").<sup>223</sup> The OTS's 1996 rules expressly declared that they occupied the field of lending and deposit-taking.<sup>224</sup> This position followed the long-standing position of lower courts that the OTS and its predecessor agency, the Federal Home Loan Bank

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<sup>220</sup> For some characteristic criticisms, see Lauren Saunders, Statement on OCC Final Preemption Rules, July 20<sup>th</sup> 2011, available at \_\_\_\_\_ (describing OCC as "thumb[ing] its nose at state efforts to protect consumers").

<sup>221</sup> OCC deleted the reference in its 2004 rules to state laws' "obstruct[ing], impair[ing], or condition[ing]" national banks' powers.

<sup>222</sup> 76 FR 43549-01, at 43357 ("[T]hese provisions clearly apply to determinations made under the *Barnett* standard provisions of the Dodd-Frank Act that are not effective until July 21, 2011.... Future preemption determinations would be subject to the new Dodd-Frank Act procedural provisions").

<sup>223</sup> 12 U.S.C. §1461 *et seq.*

<sup>224</sup> 12 C.F.R. § 560.2(a).

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Board (“FHLBB”), were both authorized by HOLA to impose field preemption on state laws regulating federally chartered savings and loans, a view implicitly approved by the U.S. Supreme Court.<sup>225</sup> The justification for this distinction between savings and loan associations and banks was rooted in the formers’ status as “fiscal agents” of the federal government. During the 1930s and 1940s, the Home Owner’s Loan Corporation (“HOLC”) invested in shares of federally chartered savings and loans, which were authorized to use these reserves to make direct loans to homeowners, replacing the twelve federal home loan banks as lenders responsible for stabilizing the housing market.<sup>226</sup> Courts emphasizing federally chartered savings and loans associations’ status as federal instrumentalities relied on those associations’ performing a federally assigned function of aiding distressed housing market using revenues provided by the federal government.<sup>227</sup> This line of reasoning eventually led a district court in 1951 to distinguish federally chartered banks from federally chartered savings & loan associations, finding that *Luckett* did not apply to the latter because savings and loan associations were more thoroughly serving as the federal government’s agents in stimulating the depressed housing market with federal revenue.<sup>228</sup>

The FHLBB’s and OTS’s theory of field preemption, therefore, was rooted in precisely the logic of *McCulloch* – *that is*, the idea that the federal government’s fiscal agents were entitled to immunity from state law. Such a theory was plausible albeit controversial when applied to Nicholas Biddle’s second bank of the United States, which had a unique status as the exclusive depository of federal revenues. The theory had some plausibility as well when applied to savings and loans that were effectively lending out federal revenue to aid in the federal mission of making homes available to distressed homeowners and home buyers. As noted in Part III above, such a “federal instrumentality” theory had lost most of its persuasive force by the 1940s.

By conceding that its 2004 list of preempted state laws was copied from the OTS’s 1996 rules,<sup>229</sup> the OCC seemed implicitly to adopt *McCulloch*’s “federal instrumentality” theory, thereby exceeding the scope of permissible preemption under *Barnett Bank*. The OCC tried to

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<sup>225</sup> In *Fid. Fed. Sav & Loan Ass’n v. de la Cuesta*, 458 U.S. 141, 160 (1982), the Court suggested that it would be broadly deferential to the preemption decisions of the Federal Home Loan Bank Board on the theory that the HOLA was “a radical and comprehensive response to the inadequacies of the existing state systems.” (citing *Conference of Federal Sav. & Loan Assns. v. Stein*, 604 F.2d 1256, 1257 (CA9 1979), summarily aff’d, 445 U.S. 921 (1980)). *De la Cuesta* noted that “the Board need not feel bound by existing state law.” *Id.* at 162.

<sup>226</sup> See generally C. Lowell Harriss, *History and Policies of the Home Owners’ Loan Corporation* (1951)

<sup>227</sup> See, e.g., *Waterbury Sav. Bank v. Danaher*, 128 Conn. 78, 20 A.2d 455 (1941)(distinguishing between state-chartered and federally chartered savings & loan associations for the purposes of determining that only the latter were exempt from state laws requiring payment of unemployment insurance assessments).

<sup>228</sup> *People v. Coast Federal Sav. & Loan Ass’n*, 98 F.Supp. 311, (S.D. Cal. 1951)(distinguishing *Anderson Nat’l Bank v. Luckett*, 1944, 321 U.S. 233 (1948) on the ground that “[a]s to national banks, Congress expressly left open a field for state regulation and the application of state laws; but as to federal savings and loan associations, Congress made plenary, preemptive delegation to the Board to organize, incorporate, supervise and regulate, leaving no field for state supervision”).

<sup>229</sup> 69 Fed.Reg.1904, 1911 n. 56 (2004) (“The list [of preempted state laws] is also substantially identical to the types of laws specified in a comparable regulation of the OTS. See 12 CFR 560.2(b) ”)

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distance itself from such a position: Although the OCC had invited comment on whether it should expressly adopt field preemption similar to that imposed by OTS,<sup>230</sup> the OCC's 2004 statement ultimately declared that "we decline to adopt the suggestion of these commenters that we declare that these regulations 'occupy the field' of national banks' real estate lending, other lending, and deposit-taking activities."<sup>231</sup> In construing its list of preempted state laws, the OCC also noted that, unlike the OTS's list, which styled itself as "illustrative" and "without limitation,"<sup>232</sup> OCC's "rule only preempts the types and features of state laws pertaining to making loans and taking deposits that are specifically listed in the regulation."<sup>233</sup>

OCC's 2004 renunciation of field preemption, however, was belied by the absence of any other specific basis for OCC's list of preempted state laws. The only point held in common by the various state laws declared to be preempted by OCC's 2004 and 2011 rules was those state laws' focus on deposit-taking and lending. By contrast, the only point held in common by the laws declared to be outside the scope of preemption – contract, property, tort, criminal law, zoning, and so forth – was that they did not focus on banking activities. The conclusion is irresistible that OCC, in 2004, based its determinations about preemption exclusively on whether the state law in question focused on banking activities, finding that such a focus alone was sufficient to preempt a state law. That OCC was not adopting a position significantly different from OTS's theory of field preemption is further suggested by OCC's assertion in its 2004 statement of basis and purpose that "the effect of labeling of this nature [as either field or conflict preemption] is largely immaterial in the present circumstances."<sup>234</sup>

Did the OCC make any further findings in 2011 to justify a different conclusion about the type of preemption that it was imposing? The OCC certainly changed the language with which it defended its rules. Mindful of the legal standard now contained in §1044(a) of the Dodd-Frank Act, the OCC in 2011 carefully and repeatedly reiterated that OCC was applying *Barnett Bank's* "conflict" standard of preemption by relying on "an evaluation of the extent and nature of an impediment posed by state law to the exercise of a power granted national banks under Federal law."<sup>235</sup> Rejecting the idea that it needed to provide any case-by-case evaluation of such impediments for rules promulgated before §1044(a) was enacted, the OCC asserted that, "[w]here the same type of impediment exists under multiple states' laws, a single conclusion of preemption can apply to multiple laws that contain the same type of impediment—that generate the same type of conflict with a Federally-granted power." The analysis of such a "conflict" was, according to the OCC, what distinguished its variety of preemption from "the OTS's preemption rules."<sup>236</sup>

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<sup>230</sup> *Id.* at 1910 ("invited comment on whether it would be appropriate to assert occupation of the entire field of real estate lending").

<sup>231</sup> *Id.* at 1911.

<sup>232</sup> 12 C.F.R. § 560.2(b).

<sup>233</sup> OCC Interpretive Letter No. 1005, 2004 WL 3465750 (June 10, 2004).

<sup>234</sup> 69 Fed. Reg. at 1911.

<sup>235</sup> 76 FR 43549-01, at 43556.

<sup>236</sup> *Id.* at 43557, n.48.

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This careful alteration of terminology, however, did not lead to any more specific explanation for why the state laws included on its list as preempted posed a conflict with any particular federal policy. Instead, the OCC generally asserted that “[t]he types and terms of laws that are set out in the 2004 preemption rules were based on the OCC’s experience with the potential impact of such laws on national bank powers and operations.”<sup>237</sup> The OCC nowhere described that impact in anything but conclusory terms, by referencing its experience as “the primary Federal supervisor of national banks” and declaring “state laws that would affect the ability of national banks to underwrite and mitigate credit risk, manage credit risk exposures, and manage loan-related assets... would meaningfully interfere with fundamental and substantial elements of the business of national banks and with their responsibilities to manage that business and those risks.”<sup>238</sup> The essence of the OCC’s argument was simply that private banks have expertise in their business, and state laws that second-guess such expertise are preempted by the *Barnett Bank* standard.<sup>239</sup>

These general statements, however, do not distinguish the preempted state laws from any of the general state laws – for instance, contracts, torts, and property -- that OCC spared from preemption. The latter obviously “affect whether and how the bank may offer a core banking product and manage some of its most basic funding functions in operating a banking business.” Why are not such general common-law claims just as preempted? In *Johnson v. Wachovia Bank*,<sup>240</sup> for instance, the Court refused to find that the OCC’s 2004 regulations preempted a widow’s claim for constructive fraud, negligence, fraud, a declaratory judgment, violation of the state Consumer Protection Act, and rescission. The widow alleged that her deceased husband’s signature had been forged on various mortgage documents and that the banks’ staff had negligently failed to detect the forgeries. Liability under such a theory of fraud triggers precisely the same effects that, according to the OCC’s 2011 statement of basis and purpose, justifies preemption: The fraud theory plainly “implicates aspects of a bank’s overall risk management and funding strategies, including ... fraud prevention.”<sup>241</sup> Why, then, is the negligence claim spared from preemption, while the more specific state regulation directed specifically to fraud prevention is preempted?

The only plausible answer is that a state law specifically addressing anti-fraud precautions targets banking operations, while the state common-law claim is not specifically tailored to banks. This was, in fact, Judge Mott’s rationale for finding that the OCC’s savings rules for tort and contract applied the widow’s claims in *Johnson*.<sup>242</sup> The state-law claims,

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<sup>237</sup> *Id.* at 43557.

<sup>238</sup> *Id.*

<sup>239</sup> *Id.* (“Such laws affect whether and how the bank may offer a core banking product and manage some of its most basic funding functions in operating a banking business”).

<sup>240</sup> 2006 WL 278549 (D. Md. 2006).

<sup>241</sup> 76 F.R. at 43557.

<sup>242</sup> “[T]here was nothing unique about national banks in considering that question,” because anyone “is under a duty not to base a commercial transaction upon a forgery, and the standards governing performance of that duty traditionally have been established by state common and statutory law.” *Johnson*, 2006 WL 278549, at 2 (D. Md. 2006).

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therefore, were exempted from preemption by the OCC's rules preserving state "contract" and "tort" claims.<sup>243</sup> Other lower courts have reached similar conclusions, applying the OCC's rules' savings clause when the state-law claim is sufficiently general.<sup>244</sup> This reasoning, however, suggests that the real driver behind the OCC's distinctions is not degree to which a state rule "affects" deposit-taking and lending but rather the degree to which a state rule specifically singles out such activities. Such a rule is essentially *McCulloch*'s rule preempting banking-specific state laws.

The OCC's failure in both 2004 and 2011 to articulate a justification for distinguishing between common-law claims and state banking law suggests that the OCC ought not to receive a great deal of deference for the distinction. §1044(a) of the Dodd-Frank Act calls for the OCC's preemption determinations to be given *Skidmore* deference rather than *Chevron* deference.<sup>245</sup> Granting that the distinction between these two species of deference is less than crystalline,<sup>246</sup> *Skidmore* deference leaves basic policy questions for courts to resolve but authorizes courts to give "weight" to an agency's judgment based on a sliding scale of multiple considerations – for instance, the agency's consistency, exercise of expertise, thoroughness, and so forth.<sup>247</sup> On this account, §1044(a) withholds from the OCC the basic task of determining whether banking preemption should be governed by *McCulloch*'s principle of "strict scrutiny" for banking-specific state laws. Instead, the courts are given the task of resolving the basic policy question left open by *Barnett Bank*, using the OCC as an expert body akin to a special master or expert witness that can provide expert answers to more precise questions about the effects of state laws on national banking interests.

OCC never provided this analysis for the fundamental distinction between general and banking-specific state law underlying its 2004 and 2011 rules. The apparent reason is that this distinction was drawn from a legal tradition having nothing whatsoever to do with conflict preemption – a tradition, originating in *McCulloch*, of protecting federal instrumentalities from state harassment through special judicial suspicion of state laws singling out the functions performed by those instrumentalities. The OCC could not invoke this old rationale, because it is

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<sup>243</sup> 12 C.F.R. section 34.4(b)(1)-(2).

<sup>244</sup> See, e.g., *White v. Wachovia Bank, N.A.*, 563 F.Supp.2d 1358 (N.D.Ga. 2008); *Great W. Res., LLC v. Bank of Ark., Nat'l Ass'n*, No. 05-5152, 2006 WL 626375, at \*3-4 (W.D.Ark. Mar. 13, 2006) (declining to dismiss breach of contract, Arkansas Deceptive Trade Practices Act, conversion, and breach of implied covenant of good faith claims on grounds of preemption)

<sup>245</sup> 12 U.S.C. §25b(b)(5)(A). The provision quotes *verbatim* the standard from *Skidmore v. Swift & Co.*, 323 U.S. 134, 140 (1944) calling for "[a] court reviewing any determinations made by the Comptroller regarding preemption of a State law by title 62 of the Revised Statutes or section 371 of this title" to "assess the validity of such determinations, depending upon the thoroughness evident in the consideration of the agency, the validity of the reasoning of the agency, the consistency with other valid determinations made by the agency, and other factors which the court finds persuasive and relevant to its decision."

<sup>246</sup> For a summary of the conflicts among scholars and judges over whether *Skidmore* embodies an "independent judgment" or a sliding scale" model of deference, see Kristin E. Hickman & Matthew D. Krueger, *In Search of the Modern Skidmore Standard*, 107 Colum. L. Rev. 1235, 1251-59 (2007).

<sup>247</sup> Peter Strauss, *'Deference' is Too Confusing - Let's Call Them 'Chevron Space' and 'Skidmore Weight,'* 112 Colum. L. Rev. 1143 (2012). Hickman & Krueger find that the great majority of courts follow a "sliding scale" approach to *Skidmore* deference. *In Search of the Modern Skidmore Standard*, 107 Col. L. Rev. at 1271.

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the basis for the sort of field preemption that §1040(a) now prohibits. Unable to find any other basis for the OCC's 2004 and 2011 preemption rules, however, courts ought to hold that those rules are inconsistent with *Barnett Bank's* rejection of *McCulloch*.

### V. Old Hickory's Revenge: The Case for Making Preemption Conditional on the OCC's Examining the Risks Addressed by State Law

According to the OCC's 2011 statement of basis and purpose, state banking laws targeting lending and deposit-taking operations “meaningfully interfere with fundamental and substantial elements of the business of national banks and with *their* responsibilities to manage that business and those risks.”<sup>248</sup> The italicized word “their” condenses perfectly the assumption behind those rules: Private bankers have the primary responsibility to manage the risks that they create. This ideal of protecting bankers' autonomy lies at the heart of *McCulloch* and, more generally, the theory of privately owned federal instrumentalities. Whatever its protestations to the contrary, the OCC aggressively defends *McCulloch's* idea that private banks, when they receive a federal charter, are federal agencies in their own right, entitled to make banking policy even when that policy has not been reviewed by any genuinely federal official.

Section 1044(a) of the Dodd-Frank Act is the latest political effort to cut back on the idea that federal agencies should treat private banks as if they were public agencies. Endorsing the anti-banker non-delegation principle, however, does not imply that state law should play the lead role, or even any ultimate role, in regulating nationally chartered banks. Like Jackson's 1832 campaign against Nicholas Biddle's Second Bank and Brandeis' 1912 campaign against the House of Morgan, the Dodd-Frank's limits on preemption are designed not so much to preserve state law as to insure that, if state law is preempted, federal regulators carefully consider – “case-by-case” – the risks that state law attempts to mitigate. There are obvious reasons why national banks engage in a business optimally regulated by national agencies. Assessing default risk – “safety and soundness” – of banks requires a lot of information about how and why panics and insolvency occur and some expert capacity to evaluate the information. It is likely that a national agency will be better situated to acquire the necessary expertise than fifty state agencies for the usual reasons of scale economies and holdout problems in information acquisition. Financial products and services are sold across state lines; National banks operate at a national scale to pool reserves, achieve scale economies, and spread risks. For these reasons, replacing state with federal banking law might be ultimately the most sensible regime for nationally chartered banks.

Such replacement, however, should involve a genuinely public federal agency's evaluation of each state law's costs and benefits. How can preemption doctrine be nudged in the direction of insuring such an evaluation?

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<sup>248</sup> 76 FR at 43357 (emphasis added).

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In what follows, I make two suggestions for encouraging the OCC to exercise its expertise rather than delegating away its policy-making responsibilities to private bankers. First, §1044(a) should be construed to bar preemption of state law unless, in the course of the federal administrative process, OCC makes specific fact-findings about why preventing the mischief prohibited by state law does not justify a limit on private bankers' policy-making discretion. Second, courts ought to take into account functional considerations about when suppression of state law is most desirable, requiring weaker evidence that OCC has considered a risk when OCC is suppressing some evil to which state governments are unusually prone. In particular, I will suggest that courts ought to be quick to find preemption where state law (a) has an apparently protectionist purpose to insulate local providers of financial services from national banks' competition or (b) expropriates national banks' investment in a state .

### A. Prodding OCC into exercising its expertise

Preemption under §1044(a), rightly understood, can transform state law into a catalyst for the OCC's careful consideration of banking risks. The essential ingredient of such a catalyzing preemption doctrine is what Professor Catherine Sharkey has termed the "agency reference" theory of preemption<sup>249</sup>: When a private party argues that some state law should be preempted by the OCC's rules construing the National Bank Act, then the courts ought to look for some evidence in the administrative record for some coherent argument rooted in agency expertise that the OCC had previously considered the risk addressed by state law and either provided a substitute federal rule or a reasoned analysis for why no rule was necessary. Such reasoned analysis would involve some assessment of the risk addressed by the challenged state law, the adequacy of existing federal rules to address that risk, or the adequacy of consumer information and market competition to address that risk absent any such federal rule. The ultimate point of this judicial assessment of OCC's administrative record would be to determine whether the OCC has made some judgment about banking risks that is inconsistent with the implicit judgment made by state law. In Professor Sharkey's words, the OCC should provide "a fine-grained account of the precise regulatory review conducted by the agency and evidence as to its compatibility with state law ... claims."<sup>250</sup>

By preempting state law only when the OCC has assessed the adequacy of either the market or federal law, the "agency reference" approach to preemption insures that banks do not make banking policy the risks of which have never been reviewed by *any* governmental official, state or federal. The OCC's 2011 preemption rules, by contrast, give banks precisely such *carte blanche* to have the final say on banking policy.

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<sup>249</sup> On the agency reference theory, Catherine M. Sharkey, *Federalism Accountability: "Agency Forcing" Measures*, 58 Duke L. J. 2125 (2009); Catherine M. Sharkey, *Products Liability Preemption: An Institutional Approach*, 76 Geo. Wash. L. Rev. 449 (2008).

<sup>250</sup> Catherine M. Sharkey, *What Riegel Portends for Product Liability*, 102 Nw. U. L. Rev. 415, 418 (2008).

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Suppose, for instance, that a state legislature identifies some specific risk that some class of credit consumers are prone to assume excessive debt – say, a risk that banks will market credit cards to college students who lack the maturity and financial skills to make responsible borrowing decisions. Suppose, further, that, responding to this perceived risk, the legislature enacts a prohibition on the marketing of credit cards to college students except through an officially approved marketing policy that included information about good credit management.<sup>251</sup> Should the National Bank Act be construed to preempt such a law on the ground that it places conditions on “incidental powers ... necessary to carry on the business of banking” conferred by the National Bank Act?<sup>252</sup> The OCC’s preemption rule seems to preempt such state laws: It bars all “state law limitations concerning ... [d]isclosure and advertising, including laws requiring specific statements, information, or other content to be included in ... credit solicitations.”<sup>253</sup> In enacting this provision, however, the OCC never gave any consideration to the special risks posed by college students’ credit decisions. The OCC instead simply stated that “compliance with state-dictated disclosure requirements clearly present a significant interference, within the meaning of *Barnett*, with the exercise of ... national bank powers.”<sup>254</sup> Preempting the state law by invoking this very general rule would, therefore, entail that the banks become the only entity to consider how banks’ own credit card marketing to college students should be regulated. Giving banks such power to assess their marketing policies with respect to college students might make sense, if credit markets, unaided by any special rules, function well. But the OCC also made no findings about whether college students are well-informed consumers of credit: OCC said nothing whatsoever about college students. To preempt state law by citing the OCC’s general declaration that states cannot impede banks’ marketing decisions is effectively to make the banks the final arbiters of their own marketing decisions.

Does such a delegation of policy-making discretion to banks make any sense as a matter of policy? If one regarded banks as akin to federal field offices staffed by disinterested officers carrying out federal policy, then the delegation would be no different than the delegation of powers to postmasters or U.S. Attorneys. This analogy between nationally chartered banks and federal agencies lies at the heart of *McCulloch*. But there is no reason to trust banks as such disinterested federal instrumentalities: The burden of American political history, from the days of Andrew Jackson through Brandeis to Dodd-Frank, suggests that we Americans do *not* trust bankers to such an extraordinary degree. Allowing preemption of state law when the OCC simply ignores the particular issues addressed by state law, therefore, is to attribute a most improbable purpose to federal law.

The advantage of the ‘agency reference’ theory is that it assigns the costs of formulating a federal policy on a specific banking risk to the parties most capable of bearing that cost – the

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<sup>251</sup> See, e.g., New York Education Law § 6437, which provides that “[e]ach college shall prohibit the advertising, marketing, or merchandising of credit cards on college campuses to students, except pursuant to an official college credit card marketing policy.”

<sup>252</sup> 12 U.S.C. §24 (granting incidental banking powers to nationally chartered banks).

<sup>253</sup> 12 C.F.R. § 7.4008(d)(8).

<sup>254</sup> 76 FR 43549-01, at 43557.

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banks regulated by the OCC. There are three advantages to placing the burden of overcoming administrative inertia on the banks rather on consumers. First, the bankers are the OCC's natural constituency, the private parties with which the OCC must regularly work and to whom the OCC is likely to be most responsive. Second, the banks have data at their disposal concerning the credit-worthiness and borrowing behavior of consumers. Third, the "agency reference" theory gives the banks a strong incentive to demand a policy specifically addressing some banking risk being regulated by the states: Absent such a policy, the banks cannot obtain the protection of preemption. Such preemption is more valuable to banks than to consumers because, unlike consumers, banks benefit from regulatory uniformity regardless of the content of the regulation: For any enterprise doing business in more than one state, there are scale economies in operating under a single, nation-wide set of rules, because the costs of compliance (*e.g.*, researching rules, designing financial products that comply with the rules, and so forth) are reduced.<sup>255</sup>

Requiring the OCC to address the risks regulated by state law before preempting that state law, therefore, has the beneficial effect of prodding the OCC into addressing banking risks that might otherwise be ignored. State law, on this account, is not the final source of banking regulation but rather a catalyst for federal regulation.<sup>256</sup> Such a prod might be especially necessary, because, as compared to elected state officials like attorneys general or governors, federal regulators might be risk-averse to regulatory action changing the *status quo*.<sup>257</sup> Such administrative action can stir up bankers and consumer advocates to lobby Congress to place pressure on the agency – for instance, through congressional committee hearings, appropriations riders, and other forms of legislative harassment. For bureaucrats who prefer the quiet life, it is simpler to take no action whatsoever on some risk rather than support either explicit regulation or de-regulation of some particular banking risk.

This is not to say that state law can directly interfere with the federal administrative process by basing legal liability under state law on private parties' acts or omissions in the federal administrative process. Such direct state meddling with federal decision-making is generally prohibited.<sup>258</sup> There is, however, no such ban on state law's complementing federal

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<sup>255</sup> See Roderick M. Hills, Jr., *Against Preemption*, 82 NYU L Rev 1, 29-32 (2007).

<sup>256</sup> On state law as a prod for agency action, see Catherine M. Sharkey, *Federalism Accountability: "Agency Forcing" Measures*, 58 Duke L. J. 2125 (2009); David C. Vladeck & David A. Kessler, *A Critical Examination of the FDA's Effort to Preempt Failure-to-Warn Claims*, 96 Geo. L.J. 461-495 (2008). On state law as a prod for congressional action, see Roderick M. Hills, Jr., *Against Preemption*, 82 NYU L Rev at 19-39 (2007) (on anti-preemption default rules as debate-eliciting rules).

<sup>257</sup> Joel D. Aberbach, Robert D. Putnam, & Bert A. Rockman, *Bureaucrats and Politicians in Western democracies* 106-14 (1981) (contrasting bureaucrats' criteria for evaluating policy with that of politicians).

<sup>258</sup> *Buckman, Co. v. Plaintiffs' Legal Comm.*, 531 U.S. 341, 347-348 (2001) (barring state law claim of fraudulent failure to submit data to Food & drug Administration in federal administrative process). With a later "*cf.*" citation to *Buckman*, the Court suggested in *PLIVA v Mensing*, 562 U.S. \_\_\_, 131 S.Ct. 2567 (2011) that states could not predicate liability on failure communicate with the FDA. *PLIVA*, 131 S. Ct. at 2578 ("Although requesting FDA assistance would have satisfied the Manufacturers' federal duty, it would not have satisfied their state tort-law duty to provide adequate labeling. State law demanded a safer label; it did not instruct the Manufacturers to communicate with the FDA about the possibility of a safer label").

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law by imposing liability for risks that federal agencies lack personnel or time to evaluate.<sup>259</sup> State law imposes no duty on private parties to urge federal regulators to address the risks regulated at the state level: That private action is an incidental (albeit happy) side-effect, not a legal requirement, of state law.

Even if one agreed that the “agency reference” theory constituted good regulatory policy, one must still determine whether it constitutes a sound interpretation of the Dodd-Frank Act. Under §1044(a) of that Act, state laws are preempted only if they violate the *Barnett Bank* standard by “significantly impair[ing]” a banking power that Congress “explicitly granted.” As suggested in Part IV(C) above, the meaning of this italicized adverb is ambiguous. It cannot be that any banking practice is “explicitly granted” simply because the practice falls within the powers conferred by the National Bank Act: Such a reading would be inconsistent with cases cited approvingly by *Barnett Bank* such as *Luckett* and *McClellan*. But *Barnett Bank* never defined the degree of specificity of federal authorization sufficient to preempt state law.

The “agency reference” theory provides a ready-made interpretation of what it means for federal law to “explicitly” confer a power: If either Congress or a federal agency explicitly considers whether existing federal law adequately controls a particular type of risk, then federal law “explicitly” confers the power to engage in banking practices that create that risk. Such a reading reconciles *Barnett Bank*’s holding that a 1916 statute explicitly granted the power to sell insurance to national banks owned by holding companies with *Luckett*’s holding that the National Bank Act did not explicitly confer the power to maintain bank accounts past the period when they were deemed abandoned by Kentucky law. By specifically authorizing national banks to sell insurance, Congress had presumably considered the risks that the sellers would compete with local banks: One cannot sell insurance, after all, without potentially depriving competitors of business. By contrast, Congress might authorize banks to maintain bank accounts without reaching any conclusion about whether or not such accounts should be deemed abandoned when they were inactive for extended periods of time after notice had been given to account holders.

Construing “explicitly” to require some specific endorsement of a banking risk by the Congress or OCC also harmonizes the “substantial impairment” standard with §1044(a)’s various procedural safeguards. Section 1044(a) requires preemption decisions to be made by “case-by-case” determinations of a state law’s “impact” on national banks, supported by “specific findings” that are backed by “substantial evidence.”<sup>260</sup> Such language meshes well with a reading of *Barnett Bank* that stresses *Barnett Bank*’s emphasis on powers “explicitly granted,” because the procedures seem to require an individualized (“case-by-case”) evaluation of a “particular” risk addressed by state law. If that risk is already adequately addressed by federal law, then the state law’s “impact” is presumably gratuitous and, therefore, an “impair[ment]” of a national bank’s honest, safe, and sound banking practices. If instead federal

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<sup>259</sup> *Wyeth v. Levine*, 555 U.S. 555, 579 (2009) (By imposing damages on manufacturers who fail to warn about risks emerging after drugs are placed on market, state law creates “a complementary form of drug regulation” that supplements FDA’s “limited resources” for monitoring drug risks, thereby “offer[ing] an additional, and important, layer of consumer protection that complements FDA regulation”)

<sup>260</sup> 12 U.S.C. §§ 25b(b)(1)(B), (b)(1)(B), (b)(3)).

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law does not address the risk addressed by state law, then state law plugs a hole in public oversight of banking that does not “impair” but rather improves such banking. In other words, process and substance go together: Whether federal law “explicitly grant[s]” to banks the power to incur a particular risk in disregard of a state law depends on whether some federal decision-maker has explicitly considered the risk in question through some “case-by-case” assessment of the “particular” impact of the state law.

Such a reading of §1044(a) is neither required nor foreclosed by the statute’s text. Because §1044(a) specifically withholds *Chevron* deference from the OCC,<sup>261</sup> however, it remains for the courts, not the OCC, to resolve the major ambiguities in the statute. This does not mean that the OCC cannot receive any deference: The administrative process as defined by §1044(a) itself provides ample deference for OCC’s consideration of the risks addressed by state law. OCC need only point to some “substantial evidence” in the record showing that additional state regulation of some risk is unnecessary. Ordinary principles of administrative law also require that OCC respond to contrary evidence that such risks are significant and unaddressed by existing federal rules with some commentary on the evidence’s inadequacy.<sup>262</sup> Passing over “important” positions that contradict the agency’s decision in silence is a recipe for judicial reversal, even if the court refuses ultimately to weigh the relative merits of the agency’s evidence against the agency’s opponents.

There is some indication that some lower courts have already adopted such an “agency reference” model for preemption under §1044(a). For instance, *In re Overdraft Litigation* found that OCC’s rule expressly authorizing national banks to charge non-interest fees<sup>263</sup> did not authorize national banks deliberately to arrange the order of posting to maximize the possibility of an account holders’ being overdrawn. In reaching this holding, the court did not find decisive OCC’s interpretation of its own rule stating that banks need not post withdrawals in the order in which they were received. Although this guidance specifically assumed that banks could post withdrawals in any order,<sup>264</sup> the court reasoned that OCC’s guidance never stated that banks could do so specifically with the purpose of deceiving customers into incurring overdraft fees.<sup>265</sup> Because OCC had not addressed the issue covered by state law – *i.e.*, whether banks’ self-interest in maximizing fees would produce the right balance of overdraft protection given the probabilities that consumers would monitor the risks of overdraft – the court assumed that OCC’s rule on posting did not preempt the state law.

*In re Overdraft Litigation* follows other lower courts in allowing states to regulate banking risks when the regulation takes the form of a general common-law theory of liability not

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<sup>261</sup>Dodd-Frank Act, § 1044 (codified at 12 U.S.C. § 25b(b)(5)(A)).

<sup>262</sup> See, e.g. *State Farm*.

<sup>263</sup> 12 C.F.R. § 7.4002.

<sup>264</sup> See Joint Guidance on Overdraft Protection Programs, 70 FR 9127-01, 2005 WL 420970 (2005). For instance, the Guidance urged that, as part of best practices, banks should “[c]learly explain to consumers that transactions may not be processed in the order in which they occurred, and that the order in which transactions are received by the institution and processed can affect the total amount of overdraft fees incurred by the consumer.” *Id.* at 11.

<sup>265</sup> *In re Overdraft Litigation*, at 19-20.

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especially targeted at the business of banking. Where state law takes the form of banking-specific regulation, lower courts still find that such laws are preempted, even absent any specific findings that compliance with the law would be especially burdensome for the bank.<sup>266</sup> That lower courts continue to treat general and banking-specific state laws differently for purposes of preemption, even after §1044(a) of the Dodd-Frank act was enacted, illustrates the persistence of *McCulloch*'s hold on the judicial mind. As explained in Part IV(B) above, the distinction between states' general and banking-specific laws makes no sense in terms of market harmonization, minimization of banks' compliance costs, protection of banking consumers, or any other conceivable goal of federal banking law. It lives on only as a sort of doctrinal ghost haunting the doctrine long after its justification has passed away.

Fortunately, the benefits of the “agency reference” theory can be realized even if the courts insist on distinguishing between general and banking-specific state laws. If *stare decisis* leads courts to honor *McCulloch*'s distinction between banking-specific rules and more general rules, then such courts can still refuse to find preemption of state common-law liability unless the OCC evaluates the specific risks addressed by such liability. Such a barrier to preemption would still induce banks to petition OCC for a clarification of federal banking law regarding the proper regulation of such specific risks. Because, as noted above in Part IV(B), virtually any banking-specific rule can be re-framed as a common-law theory not especially targeted at banking practices, such a barrier to preemption would accomplish much if not all that complete overruling of *McCulloch* would accomplish.

### B. Presuming Preemption of Functional Grounds: A Presumption against States' Protectionism and Expropriation of National Banks

The argument for requiring the OCC to evaluate a risk before preempting state laws that regulate that risk does not imply any blanket “anti-preemption” canon. There are good reasons for federal agencies and federal courts to cast a suspicious eye on certain categories of state regulations of nationally chartered banks that are likely the products of political dysfunction to which state legislatures are prone. In particular, protectionism and expropriation are two dangers that a presumption in favor of preemption might usefully combat, while imposing very little burden on the useful “prodding” function of state law described above.

Consider, first, the dangers of protectionism through the lens of the facts of *Barnett Bank* itself. The state law at issue in *Barnett* was a Florida statute prohibiting affiliates of national holding companies from selling insurance in small towns in Florida while allowing small-town bankers to peddle such insurance. The state law was, in short, blatantly protectionist. Moreover, the Florida state law undermined a 1916 federal statute authorizing nationally chartered banks to sell insurance on the same terms as any other firm “authorized by the authorities of the State ...

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<sup>266</sup>*Parks v. MBNA America Bank, N.A.*, 54 Cal.4th 376, 394, 278 P.3d 1193 (2012)(holding that disclosure requirements for convenience checks are preempted as matter of law, even absent any proof that requirements impose compliance burdens on banks).

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to do business there.” To construe the 1916 federal statute as exempting the Florida statute from preemption simply because the latter did not single out national banks as such would be to gut the obvious purpose of the federal law – to suppress state protectionism in favor of small-town bankers and against larger-scale institutions.

Such protectionism is the first circumstance in which, on functional grounds, courts ought to adopt a presumption in favor of preemption. Small bankers are likely to have exceptional networks of organization in the state legislatures, and their labors on behalf of obscure regulatory schemes that exclude competitors providing scale economies in finance are not likely to be carefully scrutinized by voters at large. When a federal law seems, therefore, to be directed at unlocking a local market for financial services that state laws seem determined to keep closed, then courts ought to suspend their deference towards the latter and presume that the former should be given broad scope to operate outside its literal terms.

Opposition to protectionism can explain the result in decisions finding preemption even when such opposition does not appear in those decisions’ reasons. In *Franklin Nat’l Bank of Franklin Square v. New York*,<sup>267</sup> for instance, the Court held that the National Bank Act’s grant of incidental advertising powers preempted a New York statute’s prohibiting banks “from using the word ‘saving’ or ‘savings’ in their advertising or business.” The New York statute applied only to banks no chartered by the state of New York: On its face and in its stated purpose, the goal of the statute was to protect New York’s own chartered savings banks and savings and loan associations from competition by commercial banks.<sup>268</sup> *Franklin* found preemption based on the general idea that advertising was “one of the most usual and useful of weapons” in banking, such that the Court could not accept that “the incidental powers granted to national banks should be construed so narrowly as to preclude the use of advertising in any branch of their authorized business.”<sup>269</sup> The Court did not, however, explain why this state limit on incidental powers was distinct from the myriad of other state laws with which national banks had to comply. The protectionist character of the preempted state law, however, supplies an answer to this question: Unlike, say, a general ban on false advertising, New York’s actual regulation was explicable only in protectionist terms.

Even when a state law does not facially discriminate against non-resident or nationally chartered banks, it is often not difficult to infer a protectionist purpose from a severe protectionist effect. In *U.S. Bank Nat’l Ass’n v. Schipper*,<sup>270</sup> for instance, the district court held preempted Iowa’s law requiring anyone providing a central routing unit for ATM transactions to appoint consumer, business, and agricultural representatives to the CRU’s policy-making body. Iowa’s law “effectively prohibited” national banks “from providing CRU services to other banks in Iowa” unless they re-structured their board of directors to comply with Iowa’s representation rules.<sup>271</sup> So effective was Iowa’s law that only one company (a local firm named “SHAZAM”)

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<sup>267</sup>347 U.S. 373(1954).

<sup>268</sup> *Franklin*, 347 U.S. at 374.

<sup>269</sup> *Franklin* 347 U.S. at 378.

<sup>270</sup>812 F.Supp.2d 963 (S.D. Iowa 2011).

<sup>271</sup>*Schipper*, 812 F.Supp.2d at 972.

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had been approved by Iowa's regulators to act as a CRU for all of Iowa.<sup>272</sup> Exclusionary effects so stark are signals of likely protectionist purpose that do not require hyper-sensitive judicial antennae to detect. *Schipper* did not rely on these exclusionary effects to find that Iowa's law was preempted, instead noting only that CRU services were "incidental" banking powers under the National Bank Act that Iowa could not significantly impair.<sup>273</sup>

As a second sort of state purpose that preemption doctrine ought to discourage, consider state desires to expropriate nationally chartered banks' sunk assets. The effort by San Francisco to prohibit banks from charging for the use of ATM machines in the early 2000s stands as the classic example of recent state anti-banking expropriation. In striking down this measure, the Ninth Circuit recited the usual rhetoric about nationally chartered banks' being federal instrumentalities that state law could not touch.<sup>274</sup> Taken literally, this rhetoric is either formalistic cant or simply untrue: State common-law imposes a myriad of legal duties on national banks that lower courts universally uphold. The better functional justification for a strong norm of preemption, however, is that imposing price controls on banks' charging for the use of their physical infrastructure looks like nothing so much as an effort to expropriate a prior investment for self-defeating populist ends. Those ends are self-defeating because such price controls discourage the very investments that the locality seeks to exploit. Moreover, the ban on ATM fees cannot be justified as an effort to protect consumers from charges about which they are likely to be ignorant: The process by which consumers use the ATM machine gives each of them ample warning of precisely the charge that the bank seeks to impose before the consumer consummates the transaction.

Why distrust state efforts at expropriation? The functional as opposed to formal reason is that states are locked into the sovereign's dilemma: They seek to encourage investments by giving assurances that those investments will be respected, but, absent an enforcement mechanism by some higher sovereign, they cannot credibly commit to honor their own assurances. The Takings and Contract clauses of the Constitution can be viewed as efforts to overcome the sovereign's dilemma, by protecting investment-backed expectations or sovereign's contractual commitments, thereby insuring that the subnational governments themselves are freed from the risk premiums that wary investors would otherwise charge sovereigns not so constrained. It is no favor for robust federalism to "liberate" subnational governments from such constraints. Banking preemption can supplement such doctrines by barring price controls that serve no function other than to expropriate pre-existing infrastructure like ATM machines.

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<sup>272</sup> *Schipper*, 812 F.Supp.2d at 967.

<sup>273</sup> *Schipper*, 815 F.Supp. 2d at 970.

<sup>274</sup> *Bank of America v. City & County of San Francisco*, 309 F.3d 551, 561-62(9th Cir.2002)(" ("National Banks are "instrumentalit[ies] of the federal government, created for a public purpose, and ... subject to the paramount authority of the United States." [citation omitted] ... The National Bank Act of 1864 was enacted to protect national banks against intrusive regulation by the States").

## *Exorcising McCulloch*

### Conclusion

It has been almost two hundred years since the U.S. Supreme Court handed down *McCulloch* and its holding that nationally chartered banks, as federal instrumentalities, must enjoy presumptive autonomy from state law. Controversial when it was handed down, it has long out-lived the historical period of which it was a creature. That a corporation especially chartered by Congress to act as the federal government's exclusive fiscal agent might be regarded as a federal agency entitled to set banking policy without further specific approval from any governmental official was plausible, albeit hotly controverted, before the Civil War. Such an assumption, however, became completely untenable when federally chartered banks are merely thousands of self-interested private enterprises with no duties to act as Congress' special fiscal agent.

There is no reason to treat such enterprises differently from any other business insofar as preemption is concerned. Where federal law provides some rule by which a banking practice is to be governed, then that rule should trump contrary state law. Moreover, given the needs of the financial sector operating in a multistate market, one might even presume that those federal rules trump any additional state regulation addressing the same risk as federal law. If there is no federal rule governing some banking activity, however, then state law should, by default, govern that activity.

Indeed, no one – not *McCulloch* itself, nor the OCC, nor the national banks – contests that *some* state law must govern such transactions for which federal law provides no rule. Even if disuniform law is bad, anarchy is worse: Banking cannot survive without laws defining contracts, property, crimes, and other matters on which commerce depends. The error of the OCC is to assume that such “general” state laws can be usefully be distinguished from state laws specifically addressed to banking, on the theory that only the former supply the “infrastructure” for banking operations with which the latter interfere. The assumption and the distinction to which it gives rise owe more to *McCulloch* than to any coherent assessment of the needs of modern banking. *McCulloch* distinguished taxes on banking operations from general property taxes on the ground that the former constituted an attack on federal supremacy.

Once one abandons the assumption that national banks' policy choices represent the presumptive policies of the federal government, then this supremacy-based argument for drawing diffuse lines between laws defining legal “infrastructure” and other sorts of state laws disappear. Instead, all state law serves the goal of filling gaps in federal law until the relevant federal regulator gets around to supplying a substitute federal rule. Rather than allow banks selectively to disregard those state laws addressing banking risks that the OCC has ignored, it is both wiser and more consistent with ordinary preemption doctrine for the OCC to evaluate the risks addressed by the states, addressing those risks with some consciously adopted federal policy.