POST-CANTERO, THE SECOND AND NINTH CIRCUITS POISED TO ISSUE NEW RULINGS ON NBA'S PREEMPTION (ON ESCROW ACCOUNT INTEREST)

by Kathy Shakibi, Esq. and T. Robert Finlay, Esq.

The one-year anniversary of the Supreme Court of the United States's ruling in *Cantero v. Bank of Am., N.A.*, 602 U.S. 205 (2024), is soon approaching, and the Second and Ninth Circuit Court of Appeals are poised to issue new rulings on whether the National Bank Act preempts state laws requiring interest on mortgage escrow accounts. New briefings have been submitted, and oral arguments have been completed in March 2025. Now our watch for the new rulings on the issue of preemption begins.

Refresher on *Cantero* Ruling

On May 30, 2024, the Supreme Court of the United States ("SCOTUS"), in *Cantero v. Bank of Am., N.A.*, 602 U.S. 205 (2024), passed on an opportunity to resolve a split between the United States Court of Appeals for the Second Circuit[1] ("Second Circuit"), and the United States Court of Appeals for the Ninth Circuit[2] ("Ninth Circuit"), regarding whether the National Bank Act of 1863 ("NBA") preempts states laws requiring interest on mortgage escrow accounts. The Second Circuit in *Cantero v. Bank of Am., N.A.*, 49 F.4th 121 (2022), vacated and remanded, 602 U.S. 205 (2024), had held that NBA preempts New York General Obligation Law § 5-601, which requires interest on mortgage escrow accounts to be paid at a rate of not less than two percent or a rate prescribed by the superintendent of financial services, whichever is higher.

The Ninth Circuit, on the other hand, in an unreported opinion in *Kivett v. Flagstar Bank, FSB*, 2022 U.S. App. LEXIS 13347, had held that NBA does not preempt California's Civil Code §2954.8(a), which requires financial institutions to pay borrowers interest on mortgage escrow accounts at a rate of at least two percent. In ruling in *Kivett*, the Ninth Circuit relied on its prior ruling in *Lusnak v. Bank of Am., N.A.*, 883 F.3d 1185 (2018), where the Ninth Circuit had also held that the NBA does not preempt California's Civil Code §2954.8(a).

Continued on page 14

[1] The Second Circuit encompasses Connecticut, New York, and Vermont.
[2] The Ninth Circuit encompasses Alaska, Arizona, California, Guam, Hawaii, Idaho, Montana, Nevada, Northern Mariana Islands, Oregon and Washington.

Post-Cantero Rulings on NBA Preemption (continued from page 13)

In *Cantero*, SCOTUS vacated the Second Circuit's ruling and remanded with instruction to analyze NBA's preemption under the standard that SCOTUS articulated in *Barnett Bank of Marion County, N.A. v. Nelson* 517 U.S. 25 (1996), which has been codified in 12 U.S.C.S. §25b(b)(1)(B) of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, known as the Barnet Standard. Under the Barnett Standard, a state consumer financial law is preempted, only if the law prevents or significantly interferes with a national bank's exercise of its powers. Prevention is not an issue in this instance, thus, significant interference with a national bank's exercise of powers is to be analyzed and decided. The Barnett Standard does not establish a clear line test for when a state law significantly interferes with a national bank's exercise of its powers. Instead, SCOTUS's analysis in *Barnett* looked to prior cases where state law was preempted, as well as cases were state law was not preempted. In remanding *Cantero*, SCOTUS required a similar nuanced comparative analysis of prior case law.

A few days after remanding *Cantero* to the Second Circuit, on June 10, 2024, SCOTUS also vacated the Ninth Circuit's ruling in *Kivett* and remanded with instruction to analyze NBA's preemption in light of *Cantero*.

Post-Remand Developments in *Cantero* in the Second Circuit

After the remand, the Second Circuit ordered the parties to submit briefings addressing whether New York General Obligation Law § 5-601 "significantly interferes" with Bank of America, N.A.'s exercise of its powers and the propriety of remanding the case back to the district court (for further fact finding).

The *Cantero* borrower in his brief, in sum, maintained that the interference by New York's law is minimal, arguing that available evidence indicates that interest-on-escrow laws have not had a material effect on national banks' ability to create and fund escrow accounts, and Bank of America has not made an evidentiary showing of significant interference. The *Cantero* borrower opposed a remand to the district court and contended it was not necessary.

Bank of America in turn, argued that preemption under the Barnett Standard is a legal question and the focus is on the kind of interference, not each case's facts. Bank of America argued that New York's law, by mandating interest, impermissibly modifies the terms of a mortgage, which is a federally authorized national bank product and threatens a patchwork of inconsistent, disruptive state laws which undercut the uniform exercise of a national bank's powers to offer mortgage escrow accounts. Bank of America also deemed a remand to the district court unnecessary.

Amici, the Conference of State Bank Supervisors and American Association of Residential Mortgage Regulators submitted a joint amicus brief, where they argued that Bank of America has not shown that New York General Obligation Law § 5-601, would cause national banks to suffer net losses on mortgage escrow accounts, and that preemption of § 5-601 would give national banks an unwarranted competitive advantage over state-chartered and state-licensed competitors.

On the other hand, amici, the Bank Policy Institute, American Bankers Association, the Chamber of Commerce of the United States of America, Consumer Bankers Association and Mortgage Bankers Association, in their joint amicus brief, framed the question before the Second Circuit as whether the NBA preempts a State from imposing price controls on the products and services of national banks. They argued that the Second Circuit's decision could have a broad impact on State attempts to set price controls on national bank products.

Oral arguments were held on March 3, 2025, and the Second Circuit is now poised to issue its ruling.

Continued on page 15

Post-Cantero Rulings on NBA Preemption (continued from page 14)

Post-Remand Developments in *Kivett* in the Ninth Circuit

After the remand, the Ninth Circuit in *Kivett v. Flagstar Bank, FSB*[3], 2022 U.S. App. LEXIS 13347, initially issued a memorandum reaffirming its prior decision, but upon Flagstar filing a Petition for Rehearing or Rehearing En Banc, the Ninth Circuit withdrew its memorandum, and requested the parties to submit briefings addressing whether the NBA preempts California's Civil Code §2954.8(a) under the standard described in *Cantero*.

The *Kivett* borrowers in their brief, in sum, argued that Flagstar had not produced facts in support of assertion that compliance with Civil Code §2954.8(a) would significantly interfere with the exercise of its banking powers. The *Kivett* borrowers maintained that under the methodology required by SCOTUS in *Cantero*, California's Civil Code §2954.8(a) is not preempted.

Flagstar, in turn, argued that "Preemption does not turn on whether national banks *could* comply with both federal and state law in theory, nor on what compliance with the state law could cost any individual bank or national banks as a whole." Rather, preemption hinges on how a state law interferes with national bank powers. Flagstar reasoned that California's interest on escrow account law "dictates a national bank's pricing and terms of its mortgage products," "limits national bank's broad authority to set the pricing terms of their mortgage escrow accounts…," and "impermissibly inhibits the flexibility that federal law provides." Flagstar also raised the argument of a disparate patchwork of state laws, which if applied to national banks, would result in disuniformity.[4]

Notably, Flagstar had preserved its argument on appeal that the Ninth Circuit's prior ruling in *Lusnak* was wrongly decided, and Flagstar contended that the preemption analysis in *Lusnak* should not be controlling because that analysis is not reconcilable with the analysis that SCOTUS required in *Cantero*. Flagstar requested that the Ninth Circuit hold that California's Civil Code §2954.8(a) is preempted, reverse the district's court judgment, and remand with instruction to enter judgment for Flagstar.

Amici, the Conference of State Bank Supervisors and American Association of Residential Mortgage Regulators who had submitted a joint amicus brief in *Cantero*, in the Second Circuit, also submitted a joint brief in *Kivett* in the Ninth Circuit. Likewise, amici, the Bank Policy Institute, American Bankers Association, the Chamber of Commerce of the United States of America, Consumer Bankers Association and Mortgage Bankers Association, who had submitted a joint amicus brief in *Cantero*, in the Second Circuit, also submitted a joint brief in *Kivett*, in the Ninth Circuit.

Oral arguments were completed on March 18, 2025, and the Ninth Circuit is now poised to issue a new ruling.

The Impact of the Rulings

In addition to California's Civil Code §2954.8 (a), Flagstar's brief lists the following state laws requiring interest on escrow accounts: "See Conn. Gen. Stat. § 49-2a; Mass. Gen. Laws ch. 183, § 61; Md. Code Ann., Com. Law § 12-109(b)(1); Me. Rev. Stat. Ann. tit. 33, § 504; Minn. Stat.§ 47.20, subdiv. 9(a); N.H. Rev. Stat. Ann. § 383-B:3-303(a)(7)(E); N.Y.G.O.L. § 5-601; Or. Rev. Stat. §§ 86.205, 86.245; R.I. Gen. Laws § 19-9-2; Utah Code Ann. § 7-17-3; Vt. Stat. Ann. tit. 8, § 10404."[5]

Continued on page 16

[3] Effective December 1, 2022, Flagstar Bank, FSB, a federally chartered savings bank converted to a federally chartered national bank.

[4] On pages 34 and 35 of its brief filed on February 6, 2025, in *Kivett* (Ninth Circuit case number 21-15667), Flagstar discussed the inconsistencies among the various state laws requiring payment of interest on mortgage escrow accounts.

[5] Flagstar's brief filed on February 6, 2025, in *Kivett* (Ninth Circuit case number 21-15667), on page 6, footnote 1. Also stating that "Wisconsin no longer requires paying interest on escrow for mortgage loans originated after April 2018, *see* Wis. Stat. § 138.052(5)(a)-(am), while Iowa law permits, but does not require paying interest on escrow funds, Iowa Code § 524.905(2).

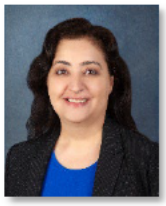
Post-Cantero Rulings on NBA Preemption (continued from page 15)

The Second Circuit encompasses Connecticut, New York and Vermont, and the Ninth Circuit encompasses California and Oregon, all of whom have enacted state laws on interest on escrow accounts. The Second and Ninth Circuits' rulings impact a national bank's mortgage escrow accounts in those jurisdictions, and potentially more broadly impact a national bank's other products, as argued in the amicus brief. Additionally, states may amend the existing interest on escrow account laws to expand the scope of their coverage. With such far-reaching consequences, our watch for the new rulings on the issue of NBA's preemption begins.

How The Ruling Could Also Impact Interest on Insurance Proceeds Following the LA Wildfires

Assembly Bill 493 proposes amending California Civil Code §2954.8 (a) to require lenders to pay interest on insurance proceeds. AB 493 is still being debated and will likely be amended. But the tie in with the NBA preemption issue is timely.

If you have any questions on this issue, please feel free to contact Kathy Shakibi at kshakibi@wrightlegal net or Robert Finlay at rfinlay@wrightlegal.net.



Kathy Shakibi, Esq.
kshakibi@wrightlegal.net

Kathy Shakibi is a Senior Associate Attorney at WFZ.

T. Robert Finlay, Esq.
rfinlay@wrightlegal.net

Robert Finlay is a founding Partner of WFZ.