

Client Alert

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Proposed Narrowing of Licensing Exemption under California Finance Lenders Law

By Henry M. Fields and Joe Gabai

The California Department of Business Oversight (“CDBO”) has proposed to narrow a long-standing interpretation of a statutory licensing exemption for certain lenders under the California Finance Lenders Law (“CFLL”).¹ The interpretation applies the exemption to nonbank subsidiaries of banks and bank holding companies.

Section 22050(a) of the California Financial Code (“CFC”) provides an exemption for licensing under the CFLL for:

“any person doing business under any law of any state or of the United States relating to banks, trust companies, saving and loan associations, insurance premium financing agencies, credit unions, small business investment companies, community advantage lenders, California business and industrial development corporations when acting under federal law or other state authority, or licensed pawnbrokers when acting under the authority of that license.”

In 1988, the California Commissioner of Corporations construed a statutory exemption containing nearly the identical language with respect to an operating subsidiary of a national bank located in Massachusetts.² The Commissioner noted that the language in question had already been construed to apply to banks but not to nonbank subsidiaries of bank holding companies or subsidiaries of national banks. In concluding that the exemption applied to such nonbank entities, the Commissioner acknowledged the cumulative effect of federal laws and regulations to which the nonbank affiliates of banks are subject, including Federal Reserve regulation of nonbank subsidiaries of bank holding companies and oversight and control by the Office of the Comptroller of the Currency (“OCC”) of operating subsidiaries of national banks.³

In addition, the specific language of the exemption supports its application to nonbank subsidiaries of bank holding companies and operating subsidiaries of national banks. The exemption is for persons doing business under laws “relating to” banks. The text of the exemption does not specifically limit itself to “banks” or to the other institutions enumerated in that Section.

The CDBO now proposes to issue a regulation that will eliminate the license exemption for a “nondepository operating subsidiary, affiliate, or agent” of a national bank (or of a federal savings association). It does not propose to eliminate the exemption for nonbank subsidiaries or affiliates of state-licensed banks (or savings

¹ California Financial Code, Section 22000 *et seq.* At the same time, the CDBO has proposed to narrow construction of a similar exemption under the California Residential Mortgage Lending Act (“CRMLA”). California Financial Code, Section 50000 *et seq.*

² Commissioner’s Opinion, File No. OP 5792, 1988 Cal. Sec. LEXIS 11, December 1, 1988. This precedent, which is cited in footnote 8 of the Invitation for Comments, dealt with one of the predecessor statutes to the CFLL, the Commercial Finance Lenders Law.

³ See also Commissioner’s Opinion, File No. OP 5862, 1989 Cal. Sec LEXIS 3, February 24, 1989.

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associations). In support of this action, the CDBO proposal cites the savings clause in Section 1045 of the Dodd-Frank Act. The savings clause provides that neither Section 24 of the Federal Reserve Act nor any provision of the Dodd-Frank Act shall be construed as preempting, annulling, or affecting the applicability of state law to any subsidiary, affiliate, or agent of a national bank (other than a subsidiary, affiliate, or agent that is chartered as a national bank). However, the 1988 interpretation did not rely on federal preemption but rather on the salutary effect of regulation and supervision of subsidiaries of national banks by the OCC and of nonbank subsidiaries of bank holding companies by the Federal Reserve.⁴

If adopted, the proposed regulation would require subsidiaries and affiliates of national banks (and federal savings associations) that lend in California to become licensed under the CFLL, and to become subject to the CFLL's regime of substantive regulation. In the absence of an exemption, the CFLL requires licensing for entities that make commercial as well as consumer loans in California and thus has a broader reach than most state licensing laws applicable to lenders.

Interested parties are invited to comment by May 7, 2014. Comments may be submitted electronically to regulations@corp.ca.gov (identifying the comments as relating to PRO 03/13), or to the California Department of Business Oversight, Legal Division, 1515 K Street, Suite 200, Sacramento, CA 95814-4052: Attention: Karen Fong (PRO 03/13).

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⁴ The Commissioner of Corporations could not in any event have relied on federal preemption as a justification for not applying the CFLL due to the prohibitions in Calif. Const. Article III, § 3.5.