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CITY GOVERNMENTS AND PREDATORY LENDING

Jonathan L. Entin[*] *and Shadya Y. Yazback*[†]

Predatory lending has generated increasing attention in recent years. The practice involves loans to homeowners who frequently cannot pay the associated costs and therefore lose their homes. Predatory lending is heavily concentrated in low- and moderate-income neighborhoods[1] and disproportionately affects minorities[2] and the elderly.[3] The consequences of predatory lending are devastating not only to the consumers who fall prey to unscrupulous lenders' tactics, but to the community as a whole.[4]

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1. HUD-TREASURY TASK FORCE ON PREDATORY LENDING, CURBING PREDATORY HOME MORTGAGE LENDING 47 (2000), *available at* http://www.huduser.org/Publications/pdf/treasrpt.pdf [hereinafter HUD Report]; Paul S. Calem et al., *The Neighborhood Distribution of Subprime Mortgage Lending*, 29 J. REAL EST. FIN. & ECON. 393, 401 (2004) [hereinafter Calem et al., *Neighborhood Distribution*]; Paul S. Calem et al., *Neighborhood Patterns of Subprime Lending: Evidence from Disparate Cities*, 15 HOUSING POL'Y DEBATE 603, 611 (2004) [hereinafter Calem et al., *Neighborhood Patterns*]. Although predatory loans are disproportionately subprime, not all subprime loans are predatory. *See infra* text accompanying note 8 and following note 15.

2. HUD Report, *supra* note 1, at 47; Calem et al., *Neighborhood Distribution*, *supra* note 1, at 401; Calem et al., *Neighborhood Patterns*, *supra* note 1, at 615.

3. U.S. GEN. ACCOUNTING OFFICE, CONSUMER PROTECTION: FEDERAL AND STATE AGENCIES FACE CHALLENGES IN COMBATING PREDATORY LENDING 14 (2004), *available at* http://www.gao.gov/new.items/d04280.pdf [hereinafter GAO Report].

4. The Federal Reserve Bank of Cleveland has explained:

> Predatory lending is a national problem that is reallocating public and private dollars away from low-and-moderate-income families and struggling inner-city neighborhoods to a variety of private parties. Federal and local tax dollars have been invested in such communities, adding to private donations, church contributions, bank loans made under [the Community Reinvestment Act], and work done by nonprofits and community volunteer organizations such as Habitat for Humanity.

Federal Reserve Bank of Cleveland, *Predatory Lending Strikes at the Heart of American Neighborhoods*, Community Reinvestment Forum 2 (Summer 2000), *available at* http://www.clevelandfed.org/CommAffairs/CRForum/frmsp00/Smr00.pdf.

For these reasons, many cities have tried to regulate or prohibit the practice.

This Article assesses the legal challenges that cities can face in trying to deal with predatory lending.[5] Part I provides an overview of the problem. Part II focuses on the common law and statutory claims that cities might bring, with particular emphasis on the evidentiary issues that cities can face and the requirements of standing that could severely limit the effectiveness of lawsuits brought by municipalities. The Article then turns to city efforts to regulate predatory lending pursuant to their home rule authority, efforts that can be stymied both by state laws that supersede municipal ordinances and federal regulations that preempt state and local initiatives. Part III focuses on home rule, explaining that most courts that have addressed the question have held municipal initiatives to be preempted by state laws. Part IV shows that the federal government might override much of what cities and states try to do to attack the problem. The article concludes that, despite the legal obstacles facing cities that want to regulate predatory lending, local efforts have served as a catalyst for predatory lending policies at the state level and might stimulate more effective national policies as well.

5. We do not address the wisdom or effectiveness of predatory-lending laws, a subject that has generated considerable discussion. On the wisdom of such laws, compare GAO Report, *supra* note 3, at 76 (suggesting that market forces will eventually eliminate predatory lending), with Kathleen C. Engel & Patricia A. McCoy, *Predatory Lending: What Does Wall Street Have to Do with It?*, 15 HOUSING POL'Y DEBATE 715 (2004) (arguing that the market cannot impose sufficient discipline to drive out predatory lenders), and Patricia A. McCoy, *A Behavioral Analysis of Predatory Lending*, 38 AKRON L. REV. 725 (2005) (using findings from behavioral economics to claim that borrowers do not act in accordance with the assumptions underlying the position of advocates of the market approach). On the effectiveness of North Carolina's pioneering law in this field, compare Gregory Elliehausen & Michael E. Staten, *Regulation of Subprime Mortgage Products: An Analysis of North Carolina's Predatory Lending Law*, 29 J. REAL EST. FIN. & ECON. 411 (2004) (concluding that the statute reduced the availability of credit to lower-income consumers), with Keith D. Harvey & Peter J. Nigro, *Do Predatory Lending Laws Influence Mortgage Lending? An Analysis of the North Carolina Predatory Lending Law*, 29 J. REAL EST. FIN. & ECON. 435 (2004) (finding that the measure resulted in less aggressive marketing by non-bank lenders and that minority and lower-income borrowers were less likely to get loans), and Roberto G. Quercia et al., *Assessing the Impact of North Carolina's Predatory Lending Law*, 15 HOUSING POL'Y DEBATE 573 (2004) (arguing that the law succeeded in reducing abusive practices without restricting access to legitimate subprime loans). On the limited utility of disclosure requirements as a remedy, see Lauren E. Willis, *Decisionmaking and the Limits of Disclosure: The Problem of Predatory Lending: Price*, 65 MD. L. REV. 707, 754-806 (2006).

I. A PRIMER ON PREDATORY LENDING

Predatory lending has yet to be defined in a comprehensive fashion. A joint report issued in June 2000 by the U.S. Department of the Treasury and U.S. Department for Housing and Urban Development ("HUD") noted: "Although home mortgage lending is regulated by state and federal authorities, none of the statu[t]es and regulations governing mortgage transactions provides a definition of predatory lending."[6]

Defining predatory lending is difficult for two reasons. First, loan attributes may or may not be "predatory" depending on the sophistication or financial position of the borrower.[7] Second, the definition of predatory lending cannot be static because the lending market is always evolving in light of technological, regulatory, and judicial advancements.

It is important to distinguish predatory lending from subprime lending. Subprime lending—the extension of credit to consumers who would be unable to obtain credit in the primary market—typically involves higher interest rates and fees to account for the increased risk associated with a particular consumer's credit history. The higher rates are not predatory per se. It is the circumstances surrounding the loan that typically make the loan predatory.[8] For that reason, most government agencies and academic experts define predatory lending in terms of specific elements, practices, or effects. In 2001, then-Federal Reserve Governor Edward Gramlich proposed an approach to predatory lending that, defined the practice in terms of elements:

> [T]ypically predatory lending involves at least one, and perhaps all three, of the following elements:
>
> > making unaffordable loans based on the assets of the borrower rather than on the borrower's ability to repay an obligation ("asset-based lending")
> >
> > inducing a borrower to refinance a loan repeatedly in order to charge high points and fees each time the loan is refinanced ("loan flipping")
> >
> > engaging in fraud or deception to conceal the true nature of the loan obligation from an unsuspecting or unsophisticated borrower.[9]

More expansive government definitions include a list of specific

6. HUD Report, *supra* note 1, at 1.

7. GAO Report, *supra* note 3, at 19.

8. Kathleen C. Engel & Patricia A. McCoy, *A Tale of Three Markets: The Law and Economics of Predatory Lending*, 80 TEX. L. REV. 1255, 1261 (2002).

9. Fed. Reserve Gov. Edward Gramlich, Remarks at Cleveland State University, Cleveland, Ohio (Mar. 23, 2001), *available at* http://www.federalreserve.gov/boarddocs/speeches/2001/20010323/default.htm.

practices. The U.S. Government Accountability Office (formerly known as the General Accounting Office) provides perhaps the most comprehensive definition:

> While there is no universally accepted definition, predatory lending is associated with the following loan characteristics and lending practices:
>
> > *Excessive fees.* Abusive loans may include fees that greatly exceed the amounts justified by the costs of the services provided and the credit and interest rate risks involved. Lenders may add these fees to the loan amounts rather than requiring payment up front, so the borrowers may not know the exact amount of the fees they are paying.
> >
> > *Excessive interest rates*. Mortgage interest rates can legitimately vary based on the characteristics of borrowers (such as creditworthiness) and of the loans themselves. However, in some cases, lenders may charge interest rates that far exceed what would be justified by any risk-based pricing calculation, or lenders may "steer" a borrower with an excellent credit record to a higher-rate loan intended for borrowers with poor credit histories.
> >
> > *Single-premium credit insurance.* Credit insurance is a loan product that repays the lender should the borrower die or become disabled. In the case of single-premium credit insurance, the full premium is paid all at once—by being added to the amount financed in the loan—rather than on a monthly basis. Because adding the full premium to the amount of the loan unnecessarily raises the amount of interest borrowers pay, single-premium credit insurance is generally considered inherently abusive.
> >
> > *Lending without regard to ability to repay*. Loans may be made without regard to a borrower's ability to repay the loan. In these cases, the loan is approved based on the value of the asset (the home) that is used as collateral. In particularly egregious cases, monthly loan payments have equaled or exceeded the borrower's total monthly income. Such lending can quickly lead to foreclosure of the property.
> >
> > *Loan flipping*. Mortgage originators may refinance borrowers' loans repeatedly in a short period of time without any economic gain for the borrower. With each successive refinancing, these originators charge high fees that "strip" borrowers' equity in their homes.
> >
> > *Fraud and deception*. Predatory lenders may perpetrate outright fraud through actions such as inflating property appraisals and doctoring loan applications and settlement documents. Lenders may also deceive borrowers by using "bait and switch" tactics that mislead borrowers about the terms of their loan. Unscrupulous lenders may fail to disclose items as required by law or in other ways may take

> advantage of borrowers' lack of financial sophistication.
>
> *Prepayment penalties*. Penalties for prepaying a loan are not necessarily abusive, but predatory lenders may use them to trap borrowers in high-cost loans.
>
> *Balloon payments*. Loans with balloon payments are structured so that monthly payments are lower but one large payment (the balloon payment) is due when the loan matures. Predatory loans may contain a balloon payment that the borrower is unlikely to be able to afford, resulting in foreclosure or refinancing with additional high costs and fees. Sometimes, lenders market a low monthly payment without adequate disclosure of the balloon payment.[10]

In the legal arena, Professors Engel and McCoy have produced a definition of predatory lending that focuses on the composition of the loan to determine whether it is predatory. While most of the Engel-McCoy definition is encompassed in the GAO definition, Professors Engel and McCoy also include waiver of meaningful legal redress—usually through mandatory arbitration clauses that require borrowers to waive judicial redress and class action participation—as an indicator of a predatory loan.[11]

From the above definitions, one can distill a definition of predatory lending in its broadest conception: predatory lending occurs when a lender extends to a consumer a loan with unfavorable terms that are structured to strip the equity from the home, possibly resulting in foreclosure on the home used to secure the loan and personal bankruptcy for the consumer.

The definitional complexity makes it difficult to quantify the aggregate costs of predatory lending. The Home Mortgage Disclosure Act[12] ("HMDA") requires that mortgage lenders with an office in a metropolitan statistical area disclose data related to all the home mortgages they make each year.[13] HMDA data cover approximately 80 percent of all home loans nationwide.[14] The HMDA data show that 26.2 percent of covered loans had annual percentage rates sufficient to trigger coverage by the

10. GAO Report, *supra* note 3, at 18-19.

11. Engel & McCoy, *supra* note 8, at 1260; *see also* Kathleen Engel & Patricia McCoy, *Predatory Lending and Community Development at Loggerheads* 5 (Cleveland Marshall Legal Studies Paper 05-105, 2006), *available at* http://ssrn.com/abstract=687161.

12. 12 U.S.C. §§ 2801-2811 (2000).

13. A metropolitan statistical area is defined by the U.S. Bureau of the Census based on economic and commuting flows between contiguous counties based on decennial census data. *See* Population Div., U.S. Bureau of the Census, Current Lists of Metropolitan and Micropolitan Statistical Areas and Definitions (2006), http://www.census.gov/population/www/estimates/metrodef.html.

14. Robert B. Avery et al., *Higher-Priced Home Lending and the 2005 HMDA Data*, FED. RES. BULL., Sept. 2006, at A123, A123.

federal predatory lending laws,[15] but not all loans covered by the federal predatory lending laws are necessarily predatory in nature. Even if comprehensive data were available about every home loan, it would still be impossible to identify the number of loans that are predatory, as no data set could accurately measure the lender's intent—a critical element of predatory lending. Despite the problems of data availability, some researchers have attempted to quantify the costs: an oft-cited 2001 report estimated that predatory lending cost consumers roughly $9.1 billion annually.[16]

II. CITIES AS LITIGANTS: STANDING AND OTHER DIFFICULTIES

Because the direct victims of predatory lending are disproportionately the elderly, minorities, and the less affluent, one might expect that cities would seek to represent these victims by asserting claims on their behalf against those engaging in these destructive practices. After all, the Supreme Court has long recognized the legitimacy of *parens patriae* suits in which governments represent the interests of their constituents. The earliest decision to this effect came in the 1900 case of *Louisiana v. Texas*,[17] which rejected the claim on the merits but nevertheless observed that "the State is entitled to seek relief in this way because the matters complained of affect her citizens at large."[18] The Court's most comprehensive discussion of *parens patriae* standing appears in *Alfred L. Snapp & Son, Inc. v. Puerto Rico ex rel. Barez*.[19] According to *Snapp*, a *parens patriae* action seeks to vindicate "quasi-sovereign" interests.[20] Those interests include a government's concern for "the health and well-being—both physical and economic—of its residents in general."[21] The action must promote "an interest apart from the interests of particular private parties" and involve "a sufficiently substantial segment of [the] population."[22]

It is unclear whether cities could maintain *parens patriae* actions over predatory lending. All of the Supreme Court cases discussed in the

15. *Id.* at A132.

16. ERIC STEIN, CTR. FOR RESPONSIBLE LENDING, QUANTIFYING THE COST OF PREDATORY LENDING 2 (2001), *available at* http://www.responsiblelending.org/pdfs/Quant10-01.pdf.

17. 176 U.S. 1 (1900).

18. *Id.* at 19.

19. 458 U.S. 592 (1982). For a review of other *parens patriae* cases, see *Hawaii v. Standard Oil Co. of Cal.*, 405 U.S. 251, 257-60 (1972).

20. *Snapp*, 458 U.S. at 602.

21. *Id.* at 607.

22. *Id.* The Court has also made clear that states may not pursue *parens patriae* cases against the federal government. Massachusetts v. Mellon, 262 U.S. 447, 485-86 (1923).

previous paragraph involved claims by states.[23] The Court has never specifically considered whether cities or other political subdivisions may pursue such claims, but its treatment of these subordinate units strongly implies that they may not do so. For example, the "state action" exemption from the antitrust laws[24] does not apply to municipalities, counties, or similar subordinate units. Those units do not enjoy the attributes of sovereignty that states possess.[25] Specifically, our system "has no place for sovereign cities."[26] This position reflects a more general view that cities and other political subdivisions do not enjoy the protection of the Eleventh Amendment because they are not sovereign. The Court so held in the 1890 case of *Lincoln County v. Luning*.[27] Although that decision has come under widespread criticism,[28] it has been consistently reaffirmed, most recently in the 2001 case of *Board of Trustees v. Garrett*.[29]

Despite the Supreme Court's silence, lower federal courts have consistently held that municipalities and other political subdivisions may not pursue *parens patriae* actions.[30] Those rulings rely on those units' lack

23. The statute under which *Snapp* arose treated Puerto Rico as a state. *Snapp*, 458 U.S. at 594 n.1, 608 n.15.

Nothing in *Massachusetts v. EPA*, 127 S. Ct. 1438 (2007), affects the analysis here. Whatever that case's implications for the scope of *parens patriae* standing in general, the dispute there had nothing to do with municipal standing. The only issue dividing the Court was whether a state had standing to challenge the federal government's refusal to regulate greenhouse gas emissions. *Compare id.* at 1454-55 & n.17 *with id.* at 1465-66 & n.1 (Roberts, C.J., dissenting).

24. *See* Parker v. Brown, 317 U.S. 341 (1943).

25. Cmty. Commc'ns Co. v. City of Boulder, 455 U.S. 40, 53-54 (1982); City of Lafayette v. La. Power & Light Co., 435 U.S. 389, 411-12 (1978) (plurality opinion).

26. *Cmty. Commc'ns*, 455 U.S. at 53.

27. 133 U.S. 529, 530 (1890) (observing that "while the county is territorially a part of the state, yet politically it is also a corporation created by, and with such powers as are given to it by, the state"). *Lincoln County*, which held that political subdivisions did not enjoy Eleventh Amendment protection, was decided on the same day as *Hans v. Louisiana*, 134 U.S. 1 (1890), which significantly expanded the protection that states enjoy under that provision.

28. *See* Melvyn R. Durchslag, *Should Political Subdivisions Be Accorded Eleventh Amendment Immunity?*, 43 DEPAUL L. REV. 577, 580 (1994) (summarizing the negative scholarly reaction to the decision).

29. 531 U.S. 356, 369 (2001); *see also, e.g.*, Mt. Healthy City Sch. Dist. Bd. of Educ. v. Doyle, 429 U.S. 274, 280 (1977); Griffin v. County Sch. Bd., 377 U.S. 218, 233 (1964).

30. Some lower courts have avoided the issue in situations where a ruling on the point was not essential to the decision. *See, e.g.*, City of Olmsted Falls v. FAA, 292 F.3d 261, 268 (D.C. Cir. 2002) (finding that the city had standing to sue on the basis of injury to itself); La Crosse County v. Gershman, Brickner & Bratton, Inc., 982 F.2d 1171, 1175 (7th Cir. 1993) (holding that the county had standing to sue as a direct purchaser of services); City of N.Y. v. Heckler, 742 F.2d 729, 733 n.3 (2d Cir. 1984) (observing that there was no dispute over the standing of other parties), *aff'd sub nom.* Bowen v. City of N.Y., 476 U.S. 467 (1986).

of sovereignty, precisely the grounds that the Supreme Court has emphasized in the Eleventh Amendment and antitrust contexts.[31] Accordingly, cities concerned about predatory lending almost certainly could not pursue *parens patriae* cases in federal court.[32]

State courts might be more hospitable to such claims, but the *parens patriae* jurisprudence involving municipalities is sparse.[33] Most of the states that have considered the question agree with the federal courts that municipalities and other political subdivisions may not pursue *parens patriae* actions because those units lack sovereignty.[34] Several other states have focused more narrowly, concluding that political subdivisions may not assert claims on behalf of their residents against other government bodies while at least implicitly leaving open the possibility of *parens patriae* actions in other circumstances.[35]

We have found only one state where courts have clearly held that municipalities may pursue *parens patriae* actions on behalf of their

31. City of Sausalito v. O'Neill, 386 F.3d 1186, 1197 (9th Cir. 2004); Mount Evans Co. v. Madigan, 14 F.3d 1444, 1453 n.3 (10th Cir. 1994); Colo. River Indian Tribes v. Town of Parker, 776 F.2d 846, 848 (9th Cir. 1985); United States v. City of Pittsburg, 661 F.2d 783, 786-87 (9th Cir. 1981); City of Rohnert Park v. Harris, 601 F.2d 1040, 1044-45 (9th Cir. 1979); *In re* Multidist. Vehicle Air Pollution M.D.L. No. 31, 481 F.2d 122, 131 (9th Cir. 1973).

32. *See* Kathleen C. Engel, *Do Cities Have Standing? Redressing the Externalities of Predatory Lending*, 38 CONN. L. REV. 355, 365-66 (2006).

33. Several state courts, like their counterparts in the lower federal judiciary, have avoided the issue of political-subdivision standing to pursue *parens patriae* claims. *See, e.g.*, Hayen v. County of Ogle, 463 N.E.2d 124, 127 (Ill. 1984) (noting that the issue had not been raised in the lower courts and that private parties clearly had standing in their own right); Town of Holbrook v. Town of Randolph, 373 N.E.2d 941, 943 (Mass. 1978) (rejecting the claim on the merits without resolving *parens patriae* standing).

34. *See, e.g.*, Bd. of County Comm'rs v. Denver Bd. of Water Comm'rs, 718 P.2d 235, 241 (Colo. 1986); Bd. of Comm'rs v. Kokomo City Plan Comm'n, 330 N.E.2d 92, 101 (Ind. 1975); Clark County v. City of Las Vegas, 574 P.2d 1013, 1014 n.1 (Nev. 1978); County of Lexington v. City of Columbia, 400 S.E.2d 146, 147 (S.C. 1991).

35. *See* Douglas County Sch. Dist. 0001 v. Johanns, 694 N.W.2d 668, 673-74 (Neb. 2005) (holding that a school district had failed to rebut the presumption that the state would adequately represent its interests in a challenge to the system of funding public schools); State v. City of Dover, 891 A.2d 524, 530-32 (N.H. 2006) (concluding that municipalities had not shown a compelling interest that would justify their independent lawsuits against manufacturers, suppliers, and distributors of the gasoline additive MBTE when the state was already pursuing its own lawsuit); Twp. of Stafford v. Stafford Twp. Zoning Bd. of Adjustment, 711 A.2d 282, 289 (N.J. 1998) (finding that "a municipal agency's *parens patriae* interest in protecting the general public is insufficient to support standing to challenge an exercise of power by another municipal agency"); County of Bergen v. Port of N.Y. Auth., 160 A.2d 811, 815 (N.J. 1960) (finding that "each governmental entity is parens patriae within the orbit of its own political responsibility" but that "the Port Authority rather than the county . . . represents the residents of the Port District with respect to the public function entrusted to it").

residents. That state is New York, where two cases have held that local governments have authority to litigate *parens patriae* claims on behalf of their residents. In *City of New York v. Wyman*,[36] the supreme court justice (the trial judge in that state) held that the city had *parens patriae* standing to challenge a state policy limiting public funding for abortions for indigent women. The city was seeking to vindicate "a two-fold public interest": a financial interest in avoiding unnecessary medical and social costs and a social interest in the health, safety, and welfare of city residents.[37] The New York City charter explicitly authorized "actions in law or equity" in "any court" on behalf of "the city or any part or portion thereof, or of the people thereof," so the municipal government had *parens patriae* standing.[38] Although this decision was ultimately reversed on the merits, neither the New York Court of Appeals nor the dissenter in the appellate department (which affirmed the supreme court's judgment) questioned the city's standing.[39] More recently, in *Town of Riverhead v. Long Island Lighting Co.*,[40] a local government was held to have *parens patriae* standing to abate a public nuisance.[41] It is possible that other local governments that enjoy strong home-rule authority could assert *parens patriae* claims for predatory lending.[42] At this point, however, it seems unlikely that very many cities could do so.[43]

Even though cities probably lack *parens patriae* standing to go after predatory lenders, they might well be able to sue on their own behalf to seek relief for harm to the community itself. Several courts that either did

36. 321 N.Y.S.2d 695 (Sup. Ct.), *aff'd per curiam on other grounds*, 322 N.Y.S.2d 957 (App. Div. 1971), *rev'd on other grounds*, 281 N.E.2d 180 (N.Y. 1972).

37. *Id.* at 712-13.

38. *Id.* at 712.

39. *See* City of N.Y. v. Wyman, 322 N.Y.S.2d 957, 958 (App. Div. 1971) (Steuer, J., dissenting), *rev'd*, 281 N.E.2d 180 (N.Y. 1972).

40. 685 N.Y.S.2d 792 (App. Div. 1999) (mem.).

41. The court cited only *Snapp* in support of its conclusion that the town could sue on behalf of its residents. *Id.* at 793. *But see* Inc. Vill. of Northport v. Town of Huntington, 604 N.Y.S.2d 587, 589 (App. Div. 1993) (finding no *parens patriae* standing where a local government simply aggregated "a collection of private suits" that did not assert quasi-sovereign interests but allowing village trustees to sue as individual residents of the community).

42. For further discussion of home rule, see *infra* Part III.

43. An Illinois court has characterized "home rule units" (such as the City of Chicago) as "quasi-sovereign entities." *In re* County Collector, 774 N.E.2d 832, 847 (Ill. App. Ct. 2002). One commentator has characterized this language as supporting the notion that Illinois cities may bring *parens patriae* claims. Engel, *supra* note 32, at 366. Perhaps so, but that case did not address *parens patriae*. Rather, the dispute concerned the legality of property taxes levied by the City of Chicago. The Illinois Supreme Court chose not to decide whether "home rule units" or other political subdivisions may pursue *parens patriae* actions. Hayen v. County of Ogle, 463 N.E.2d 124, 127 (Ill. 1984); *see supra* note 33.

not reach the *parens patriae* issue or concluded that political subdivisions had no such authority nonetheless have held that those governmental units had standing in their own right. Most recently, the Ninth Circuit, in *City of Sausalito v. O'Neill*,[44] held that a municipality had standing to challenge the adequacy of an environmental impact statement about plans to develop a former military base. Although the city lacked sovereignty and thus could not sue as *parens patriae*,[45] it did have standing to assert various harms to its proprietary interests. Among those proprietary harms were increased traffic congestion that would raise management and traffic safety concerns, disrupt the community's aesthetic appeal, reduce its tax revenues, impair air quality, increase air pollution, and degrade local parks, trails, and shore areas.[46] Similarly, the D.C. Circuit, in *City of Olmsted Falls v. FAA*,[47] did not resolve the question of *parens patriae* standing in a suburb's challenge to the approval of a runway improvement project at Cleveland Hopkins International Airport because the suburb had asserted harm to its own economic interests, which was sufficient to confer standing.[48]

State courts have reached similar conclusions. Two Colorado cases illustrate the point. In *Board of County Commissioners v. Denver Board of Water Commissioners*,[49] the state supreme court ruled that suburban counties lacked *parens patriae* standing but could sue in their own right to force the Denver water agency to continue supplying water on favorable terms.[50] More recently, in *Board of County Commissioners v. City of Denver*,[51] a state appellate court held that suburban governments could sue as direct parties to a contract limiting noise levels at the Denver International Airport even though the suburbs could not pursue *parens*

44. 386 F.3d 1186 (9th Cir. 2004).

45. *Id.* at 1197.

46. *Id.* at 1198-1200.

47. 292 F.3d 261 (D.C. Cir. 2002).

48. *Id.* at 268. *See also* Mount Evans Co. v. Madigan, 14 F.3d 1444, 1451-53 (10th Cir. 1994) (holding that a county had standing, based on loss of revenue, to challenge the U.S. Forest Service's decision not to rebuild an income-generating structure that had been destroyed by a fire); Colo. River Indian Tribes v. Town of Parker, 776 F.2d 846, 848-49 (9th Cir. 1985) (concluding that the town had standing, based on diminished sales tax revenue, to challenge the tribe's regulation of liquor sales on land within the town); *cf.* City of Rohnert Park v. Harris, 601 F.2d 1040, 1044-45 (9th Cir. 1979) (finding that a city that wanted to develop its own regional shopping center lacked antitrust standing to assert its own proprietary interests in an effort to prevent a nearby community from developing a similar shopping center).

49. 718 P.2d 235 (Colo. 1986).

50. *Id.* at 241.

51. 40 P.3d 25 (Colo. Ct. App. 2001).

patriae actions.[52]

In short, cities interested in litigating predatory-lending claims will probably have to assert their own interests. To do so in federal court they will have to satisfy both constitutional and prudential requirements. The constitutional minima are that a plaintiff allege a legally cognizable "injury in fact" that is "fairly traceable" to the defendant's conduct and likely to be "redressed by a favorable decision."[53] On the prudential side, a plaintiff must assert its own interests rather than those of third parties, may not sue over generalized grievances, and must be within the zone of interests protected by any statute on which it relies.[54] Similar standing rules apply in many state courts, although some states have less stringent requirements in this regard.[55]

One possible claim that a city might assert would be based on the Fair Housing Act.[56] As relevant to predatory lending, that statute prohibits racial discrimination in residential real estate transactions, including the financing of such transactions.[57] Because predatory lending disproportionately affects persons of color,[58] it is possible that the practice might violate the Fair Housing Act. This suggestion raises two questions: (1) do cities have standing to sue under the Fair Housing Act, and (2) may a Fair Housing Act plaintiff prevail on a disparate-impact theory? The answer to both questions is a qualified yes.

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52. *Id.* at 32.

53. *See, e.g.*, Friends of the Earth, Inc. v. Laidlaw Envtl. Servs. (TOC), Inc., 528 U.S. 167, 180-81 (2000); Lujan v. Defenders of Wildlife, 504 U.S. 555, 560-61 (1992).

54. *See, e.g.*, Allen v. Wright, 468 U.S. 737, 751 (1984); Valley Forge Christian Coll. v. Ams. United for Separation of Church and State, Inc., 454 U.S. 464, 474-75 (1982); Warth v. Seldin, 422 U.S. 490, 499-500 (1975).

55. States are free to apply more permissive rules for standing in cases involving federal questions. ASARCO, Inc. v. Kadish, 490 U.S. 605, 617 (1989). Some do so. *See* Engel, *supra* note 32, at 360-61; Helen Hershkoff, *State Courts and the "Passive Virtues": Rethinking the Judicial Function*, 114 HARV. L. REV. 1833, 1835-37 (2001). For a critique of permissive state standing requirements, see Michael E. Solimine, *Recalibrating Justiciability in Ohio Courts*, 51 CLEV. ST. L. REV. 531, 541-50 (2004).

56. 42 U.S.C. §§ 3601-3631 (2000).

57. Section 805(a) of the Fair Housing Act provides:

> It shall be unlawful for any person or other entity whose business includes engaging in residential real estate-related transactions to discriminate against any person in making available such a transaction, or in the terms or conditions of such a transaction, because of race, color, religion, sex, handicap, familial status, or national origin.

42 U.S.C. § 3605(a). Section 805(b)(1) defines covered transactions to include "the making or purchasing of loans or providing other financial assistance" for the purchase, construction, improvement, repair, or maintenance of a dwelling as well as loans or other financial assistance that are "secured by residential real estate." *Id.* § 3605(b)(1).

58. *See supra* note 2 and accompanying text; Engel, *supra* note 32, at 356 & n.6.

As to standing, the Supreme Court held in *Gladstone, Realtors v. Village of Bellwood*[59] that a municipality can sue for its own injuries that result from Fair Housing Act violations. At issue in that case were claims that real estate firms engaged in racial steering, showing African American customers homes in a twelve-by-thirteen-block section of town while showing white customers homes outside that area.[60] The village argued that this practice unlawfully manipulated its housing market, undermining the stability of an integrated neighborhood and encouraging white flight.[61] This in turn would reduce property values and the tax base needed to support the provision of local services.[62] Although the Fair Housing Act does not refer to municipalities or other governmental institutions as potential plaintiffs, the Court held that the village could be an "aggrieved person" for purposes of the statute. The Act defines an "aggrieved person" as anyone "claim[ing] to have been injured by a discriminatory housing practice."[63] Congress may "expand standing to the full extent permitted by" the Constitution[64] and had in fact done so in the Fair Housing Act.[65] Because the legislative branch had overridden prudential factors, standing under this statute was not limited to direct victims of discrimination. All that mattered was that the village had suffered "actual injury as a result of the defendant's conduct."[66] The key question was "not who possesses the legal rights protected by [the Fair Housing Act], but whether [Bellwood was] genuinely injured by conduct that violates *someone's* [statutory] rights."[67] In other words, the village had to satisfy only the constitutional test for standing: injury in fact, causation, and redressability. The complaint alleged that the real estate firms had engaged in racial discrimination that caused Bellwood to suffer a legally cognizable harm that could be rectified by a favorable judicial ruling. That was sufficient for standing.[68]

59. 441 U.S. 91 (1979).

60. *Id.* at 95.

61. *Id.* at 109-10.

62. *Id.* at 110-11.

63. 42 U.S.C. § 3602(i)(1) (2000).

64. *Gladstone*, 441 U.S. at 100.

65. *Id.* at 109 (holding that standing under the Fair Housing Act is "as broa[d] as is permitted by Article III of the Constitution") (quoting Trafficante v. Metro. Life Ins. Co., 409 U.S. 205, 209 (1972) (internal quotation marks omitted)).

66. *Id.* at 103 n.9.

67. *Id.*

68. *Id.* at 111, 115. Elsewhere in the opinion the Court cautioned that there might be limits to the geographical scope of a neighborhood that could be encompassed by a Fair Housing Act complaint. That point appears in the discussion of the standing of individual plaintiffs. *Id.* at 114. It is not clear whether this observation applies to claims brought by

As to disparate impact, the Supreme Court has never determined whether discriminatory intent is necessary to establish a Fair Housing Act claim.[69] The courts of appeals have generally held that proof of discriminatory intent is not necessary, but they have taken somewhat different approaches to disparate-impact claims.[70] At the same time, there is general agreement that a showing of disparate impact does not suffice to prove a statutory violation.[71]

This discussion suggests that a city might have standing to assert a Fair Housing Act claim against predatory lenders. The city would have to allege that predatory lenders were engaging in racial discrimination in real estate financing and that this discrimination harmed the city financially or socially. These allegations would presumably satisfy the constitutional test for standing. The city would not have to prove that the lenders intentionally discriminated against borrowers on the basis of race, but to prevail on the merits it would have to establish a disproportionate impact on residents of color that was not sufficiently justified. The likelihood of success in such an endeavor is unclear. Suffice it to say that we have not found any reported case in which a city has advanced a Fair Housing Act claim for predatory lending.

One leading commentator has suggested that, in light of the complexity of standing doctrine, cities face potentially insurmountable obstacles to pursuing some alternative claims against predatory lending.[72] Other such claims could be difficult to prove on the merits.[73] For our purposes, what matters is that cities face numerous uncertainties if they decide to litigate directly against predatory lending. For this reason, many communities have chosen instead to try to regulate the practice. As the next section makes clear, that approach presents its own challenges.

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cities or other political subdivisions.

69. Peter E. Mahoney, *The End(s) of Disparate Impact: Doctrinal Reconstruction, Fair Housing and Lending Law, and the Antidiscrimination Principle*, 47 EMORY L.J. 409, 425 n.54 (1998).

70. *See, e.g.*, Langlois v. Abington Hous. Auth., 207 F.3d 43, 49 (1st Cir. 2000); Huntington Branch, NAACP v. Town of Huntington, 844 F.2d 926, 934-36 (2d Cir.), *aff'd per curiam*, 488 U.S. 15 (1988); Arthur v. City of Toledo, 782 F.2d 565, 575 (6th Cir. 1986); Smith v. Town of Clarkton, 682 F.2d 1055, 1065 (4th Cir. 1982); Metro. Hous. Dev. Corp. v. Vill. of Arlington Heights, 558 F.2d 1283, 1290 (7th Cir. 1977).

71. *See, e.g.*, *Langlois*, 207 F.3d at 49-50.

72. Engel, *supra* note 32, at 378-82 (discussing fraud and unfair or deceptive practices claims).

73. *Id.* at 382-86 (discussing public nuisance and unjust enrichment).

III. CITIES AS REGULATORS: THE MEANING AND LIMITS OF HOME RULE

Traditionally, cities had very limited authority. Under the influential Dillon's Rule, municipalities could exercise only those powers that the state explicitly granted or that flowed by clear and necessary implication from explicit grants, with all doubts resolved against the existence of local authority.[74] The restrictive approach embodied in Dillon's Rule proved to be quite controversial, because many people believe that local autonomy promotes important social and political values.[75] The great majority of states eventually conferred some variant of home rule on municipalities.[76] Even when cities have home rule, however, state law might preempt local initiatives. This section focuses on state preemption of local ordinances, with particular reference to cases that have resulted in reported judicial

74. *See* JOHN F. DILLON, TREATISE ON THE LAW OF MUNICIPAL CORPORATIONS § 55, at 101-02 (2d ed. 1872) ("It is a general and undisputed proposition of law that a municipal corporation possesses, and can exercise, the following powers, and no others: First, those granted in *express words*; second, those *necessarily or fairly implied* in, or *incident* to, the powers expressly granted; third, those *essential* to the declared objects and purposes of the corporation—not simply convenient, but indispensable."); *see also* JOHN F. DILLON, COMMENTARIES ON THE LAW OF MUNICIPAL CORPORATIONS § 237, at 448-49 (5th ed. 1911) ("It is a general and undisputed proposition of law that *a municipal corporation possesses and can exercise the following powers, and no others*: First, those granted in *express words*; second, those *necessarily or fairly implied* in, or *incident* to, the powers expressly granted; third, those *essential* to the declared objects and purposes of the corporation—not simply convenient, but indispensable.") (internal citations omitted).

The Supreme Court similarly held that cities, as creatures of the state, generally enjoyed no federal constitutional protections against the states. *See* Hunter v. City of Pittsburgh, 207 U.S. 161, 178-79 (1907) ("The state, . . . at its pleasure, may modify or withdraw [any governmental] powers [it has entrusted to municipal corporations] . . . with or without the consent of the [city's] citizens, or even against their protest.").

75. Supporters note that home rule promotes democratic participation, facilitates the adoption of public policies that take account of local needs and local opinion, promotes and enhances a sense of community, and affords opportunities for reform and innovation. *See* Richard Briffault, *Home Rule for the Twenty-first Century*, 36 URB. LAW. 253, 258-60 (2004).

76. Prominent scholars disagree over the extent to which home rule actually empowers cities and whether municipal autonomy necessarily promotes the public interest. *Compare* Gerald E. Frug, *The City as a Legal Concept*, 93 HARV. L. REV. 1057 (1980) (contending that the legal authority of cities remains unacceptably weak), *with* Richard Briffault, *Our Localism: Part I—The Structure of Local Government Law*, 90 COLUM. L. REV. 1 (1990) (arguing that home rule prevents effective regional approaches to social problems and aggravates many of them), *and* Richard Briffault, *Our Localism: Part II—Localism and Legal Theory*, 90 COLUM. L. REV. 346 (1990) (criticizing unquestioning support for local autonomy); *see also* David J. Barron, *Reclaiming Home Rule*, 116 HARV. L. REV. 2255 (2003) (suggesting that home rule embodies a complex mixture of both grants and limitations on local authority).

decisions.[77]

Since North Carolina enacted its pioneering predatory lending law in 1999,[78] almost twenty cities and other local governments have considered similar proposals.[79] Almost all of the measures that passed faced immediate legal challenges as well as efforts to obtain preemptive state legislation.[80] Courts in three large states—New York, California, and Ohio—have issued published decisions addressing the question of state preemption of local predatory lending ordinances. The New York and California courts ruled against the cities, but the situation in Ohio is more complex: the state's appellate courts have taken divergent approaches to the issue, but a recent supreme court ruling has found two municipal ordinances to be preempted by state law. These decisions suggest that, at the very least, local laws and policies face a high likelihood of frustration if opponents can influence state authorities to act.

The first of the state preemption cases, *Mayor of New York v. Council of New York*,[81] invalidated an ordinance that forbade the city from doing business with predatory lenders.[82] The court held that the state's banking

77. More than two dozen states have enacted predatory lending laws. Local governments had not acted in most of those states, so preemption was not always at issue. For a summary of the provisions of the state laws, see Baher Azmy, *Squaring the Predatory Lending Circle*, 57 FLA. L. REV. 295, 361-78 (2005).

78. N.C. GEN. STAT. ANN. §§ 24-1.1E, 24-10.2 (West 2004); *see supra* note 5 (citing evaluations of this measure).

79. *See* Giang Ho & Anthony Pennington-Cross, *The Impact of Local Predatory Lending Laws*, app. B, at 44 (Fed. Reserve Bank of St. Louis Working Paper No. 2005-049B, 2005), *available at* http://research.stlouisfed.org/wp/2005/2005-049.pdf.

80. In Philadelphia, for example, opponents filed suit in state court. Even before the court could rule on the ordinance's validity, the state legislature enacted its own bill that expressly preempted all municipal regulation of predatory lending. *See* Kimm Tynan, Note, *Pennsylvania Welcomes Predatory Lenders: Pennsylvania's Act 55 Preempts Philadelphia's Tough Ordinance But Provides Little Protection for Vulnerable Borrowers*, 34 RUTGERS L.J. 837, 872-84 (2003). Meanwhile, in Atlanta, a trial court enjoined the enforcement of a local ordinance; the state legislature subsequently passed its own bill that preempted municipal initiatives. *See* Azmy, *supra* note 77, at 362 n.348; Anne-Marie Motto, Note, *Skirting the Law: How Predatory Mortgage Lenders Are Destroying the American Dream*, 18 GA. ST. U. L. REV. 859, 896 n.298 (2002) (citing Milo Ippolito, *Finance Statutes Defeated in Courts*, ATLANTA J. CONST., Nov. 3, 2001, at 4H).

81. 780 N.Y.S.2d 266 (Sup. Ct. 2004).

82. The case arose in an odd posture: the city council passed the ordinance over the mayor's veto, after which the mayor sought a declaratory judgment that the ordinance was invalid so that he would not have to enforce the measure. *Id.* at 269 & n.1. This was not the only recent legal dispute between the mayor and the city council over the validity and enforceability of a New York City ordinance. Another dispute involved the validity of a measure (also enacted over a mayoral veto) forbidding the city from contracting with businesses that fail to provide benefits to registered domestic partners of their employees equal to those afforded to the spouses of their married workers. *See* Council of N.Y. v. Bloomberg, 846 N.E.2d 433, 435 (N.Y. 2006). The complexity of those issues is reflected

law, which included specific provisions dealing with "high-cost" loans, preempted the ordinance.[83] The opinion suggests two separate grounds for preemption: field and conflict. As to the former, the state statute was "a comprehensive regulatory scheme" that occupied the entire field.[84] Indeed, the banking law specifically "provide[d] for 'uniform regulation of the residential mortgage lending process.'"[85] Accordingly, the absence of language expressly preempting local predatory lending measures could not save the ordinance; the detailed state law suggested that there was no room for local legislation relating to predatory lending.[86] As to the latter, the city ordinance contained provisions that were "in substantial conflict" with the state law and would therefore "disrupt the operation" of that statute.[87]

Just over a year later, a closely divided California Supreme Court, in *American Financial Services Ass'n v. City of Oakland*,[88] ruled that state law preempted another predatory lending ordinance. Both measures directly regulated home loans.[89] Oakland's ordinance was stricter than the California statute.[90] Notwithstanding that difference, the majority relied on field preemption and only indirectly addressed conflict preemption. The state had implicitly occupied the field. Therefore, despite the absence of language of express preemption, the state measure left no room for local regulation.[91] The state, rather than local governments, traditionally had regulated mortgage lending even before the adoption of the predatory lending law.[92] Moreover, statewide regulation was essential. The housing market was "critical" to the California economy, and statewide regulation was "essential" because mortgage-backed securities were sold nationwide.[93] Allowing municipalities to set their own standards would

in the close division in the New York Court of Appeals, which split 4-3 in that case. *Id.* at 447.

83. The state law was adopted shortly after the mayor vetoed the ordinance. *Mayor of New York*, 780 N.Y.S.2d at 274.

84. *Id.*

85. *Id.* at 273-74 (quoting N.Y. BANKING LAW § 589 (McKinney 2006)).

86. *Id.* at 274.

87. *Id.* at 275. The court also held that the city ordinance was "substantially" preempted by federal law. *Id.* at 276; *see infra* notes 150-57 and accompanying text.

88. 104 P.3d 813 (Cal. 2005).

89. The state law was enacted eight days after the ordinance. *Id.* at 815.

90. For example, the Oakland ordinance applied to holders in due course, prohibited most prepayment penalties, and required either that borrowers be provided with loan counseling or that they explicitly waive such counseling. The state law did not apply to holders in due course, permitted prepayment penalties, and required only that borrowers be encouraged to seek loan counseling. *See id.* at 819.

91. *Id.* at 820.

92. *Id.* at 822.

93. *Id.* at 823.

undermine the "centralized and uniform" rules necessary for the economic welfare of all California residents.[94]

Everyone involved in the Oakland case, including the city and the dissenting justices in this 4-3 decision, agreed that the state had a powerful interest in predatory lending.[95] This consensus mattered, because the California Constitution allows local governments to "make and enforce . . . all local, police, sanitary, and other ordinances and regulations not in conflict with general laws"[96] and also permits home rule communities to "make and enforce all ordinances and regulations in respect to municipal affairs, . . . and in respect to other matters they shall be subject to general laws."[97] If predatory lending was not a municipal affair but rather a question of statewide concern, the case turned on whether the Oakland ordinance conflicted with the state law.

Disagreement centered on the strength of the evidence that the legislature had implicitly preempted local initiatives and on whether the state's regulatory interest was sufficiently powerful to trump the city's interest in dealing with the adverse social and economic consequences of the practice within its own borders. The dissenters emphasized undisputed evidence in the legislative history that mortgage lenders had strongly and unsuccessfully lobbied for language expressly preempting measures such as the Oakland ordinance.[98] In fact, that measure was specifically discussed in a state senate committee hearing.[99] In the end, supporters of the bill that the legislature ultimately enacted chose to say nothing at all about preemption for fear that including such a provision would doom the measure.[100] This evidence strongly suggested that the legislature had not implicitly preempted the Oakland ordinance.[101] Moreover, the city had persuasive grounds for adopting its own rules to supplement the state's approach to predatory lending. The practice was unusually common in Oakland, disadvantaging both the borrowers who were victimized by abusive practices and the community as a whole.[102] Under the

94. *Id.* at 825.

95. *Id.* at 820 (noting that the city "reasonably concedes regulation of predatory practices in mortgage lending is one of statewide concern"); *id.* at 832 (George, C.J., dissenting) (observing that "regulation of predatory lending undoubtedly is an area of statewide concern").

96. CAL. CONST. art. XI, § 7.

97. *Id.* § 5(a).

98. *City of Oakland*, 104 P.3d at 830-31 (George, C.J., dissenting).

99. *Id.* at 830.

100. *Id.* at 831.

101. *Id.*

102. *Id.* at 832-33.

circumstances, it was at least as plausible to conclude that the legislature intended to establish minimum statewide standards that local governments could supplement as to find an unarticulated intention to preempt the entire field of predatory lending regulation.[103] The Oakland ordinance did not "undermine" or "subvert" state regulations but simply afforded "additional protections" to city residents who were "especially vulnerable" to the shady practices of predatory lenders.[104]

The majority rejected both lines of this analysis. First, this was a case of implied preemption.[105] Determining whether the legislature implicitly preempted local measures must be inferred not simply from the statutory text but also from the nature, purpose, and scope of the state regulatory scheme.[106] Any other approach would effectively eliminate the entire doctrine of implied preemption.[107] Second, the structure and purpose of the state law showed that it left no room for local regulation. Allowing more stringent city ordinances would discourage legitimate subprime lenders from making loans and either increase the cost or eliminate the availability of such loans to lower-income borrowers.[108] The nature of the problem suggested a need for "centralized and uniform" rules, which in turn undercut the argument that the state statute set minimum standards that cities could augment.[109]

We need not determine which side had the better of the arguments. For present purposes, it suffices that in California, as in New York, courts have held that state laws preempt city ordinances addressing predatory lending. The situation in Ohio has been somewhat settled until very recently. The applicable home rule guarantee in that state provides: "Municipalities shall have authority to exercise all powers of local self-government and to adopt and enforce within their limits such local police, sanitary and other similar regulations, as are not in conflict with general laws."[110] Three large cities in the Buckeye State have adopted predatory lending ordinances; different districts of the Ohio Court of Appeals have reached divergent conclusions about the validity of those ordinances; the Ohio Supreme Court recently held that two of those ordinances were unconstitutional.

103. *Id.* at 834.
104. *Id.* at 835.
105. *Id.* at 820 (majority opinion).
106. *Id.* at 826-27.
107. *Id.* at 827.
108. *Id.* at 824.
109. *Id.* at 825.
110. OHIO CONST. art. XVIII, § 3.

The first Ohio decision came in *City of Dayton v. State*,[111] in which the Ohio Court of Appeals for the Second District found a local ordinance to be preempted by state law. As in Oakland and New York City, Dayton adopted its predatory lending ordinance before the state legislature enacted a statute dealing with the same subject.[112] Shortly after the state law became effective, the city sought a declaratory judgment that the statute's preemption provision violated the home rule provision of the Ohio Constitution.[113] The appellate court first concluded that Dayton's predatory lending ordinance did not deal with a matter of "local self-government" within the meaning of the constitutional home rule guarantee, but rather with "the use of police powers."[114] Applying a two-part test, the court went on to hold that the preemption provision of the state statute was a general law and that the Dayton ordinance conflicted with it, so the local measure had to give way.[115]

First, the state preemption provision satisfied the applicable four-part test for general laws.[116] That measure was part of a comprehensive bill that addressed many aspects of predatory lending. Gaps and possible imperfections in that bill did not render it less than comprehensive.[117] Moreover, the statute applied throughout the state, dealt with the police power, and established a general rule of conduct.[118]

Second, although the home rule provision allows cities to adopt stricter regulations than the state,[119] Dayton's ordinance conflicted in several particulars with the state law. The only example the court cited was the annual percentage rate ("APR") for loans defined as predatory. The state law defined as predatory those loans with an APR that exceeds the yield on benchmark Treasury bills by more than ten percentage points,[120] while

111. 813 N.E.2d 707 (Ohio Ct. App. 2004).

112. *Id.* at 710; *see also supra* note 81 and accompanying text (discussing New York City and New York State); *supra* text accompanying notes 98-99 (discussing Oakland and California). City ordinances in other states also seem to have stimulated state action. *See supra* note 80 (discussing ordinances in Philadelphia and Atlanta that apparently led to the passage of state laws in Pennsylvania and Georgia).

113. *City of Dayton*, 813 N.E.2d at 712. For the language of the home rule provision, see *supra* text accompanying note 110.

114. *City of Dayton*, 813 N.E.2d at 714.

115. *Id.* at 722, 725. Before getting to the two-part test, the court extensively reviewed and found it impossible to resolve the Ohio Supreme Court's conflicting rulings about the meaning of "statewide concern" and preemption. *Id.* at 714-21, 721-22.

116. *See* City of Canton v. State, 766 N.E.2d 963, 964-65 (syl.), 968 (Ohio 2002).

117. *City of Dayton*, 813 N.E.2d at 723.

118. *Id.* at 724.

119. *Id.* at 725-26.

120. *Id.* at 711, 725.

Dayton's ordinance apparently set a lower threshold.[121] This disparity represented an impermissible implied conflict.[122] Moreover, a provision in the ordinance that forbade the city from contracting with predatory lenders—a measure analogous to the New York City ordinance that was struck down a few months earlier[123]—was an illegitimate effort by the city to do indirectly what state law prohibited it from doing directly, to regulate predatory lending.[124]

Six months later, in *American Financial Services Ass'n v. City of Cleveland*,[125] the Ohio Court of Appeals for the Eighth District reached the opposite conclusion and upheld a different predatory lending ordinance as a legitimate exercise of home rule. At issue here, as in *City of Dayton*, was the validity of the preemption provision in the state law. Although the analytical framework was the same in both cases, the Eighth District in *City of Cleveland* fundamentally disagreed with the Second District in *City of Dayton*. Both courts did find that predatory lending ordinance was in every important respect a police power regulation, not an exercise of local self-government.[126] In all other respects, however, the *City of Cleveland* court came out the other way than did its *City of Dayton* counterpart.

The Eighth District's analysis in *City of Cleveland* began by observing that the Ohio Constitution's home rule guarantee prevents the legislature from completely preempting municipal authority.[127] Focusing exclusively on the preemption provision instead of the entire state statute, the court held that this measure could not be a general law because it did not apply to "citizens generally" but covered only local legislative bodies.[128] For this reason, the preemption provision was unconstitutional.[129]

Turning next to preemption, the *City of Cleveland* court found no conflict between the city ordinance and the state law. The state law set minimum standards that the city was free to strengthen. The city had not explicitly allowed anything specifically prohibited by state law, nor did the state law expressly allow anything specifically prohibited by the city ordinance.[130] Of course, there might be an implicit conflict between the

121. *Id.* at 725. Curiously, the opinion does not specify the threshold set by the ordinance.

122. *Id.* at 726-27.

123. *See supra* notes 81-87 and accompanying text.

124. *City of Dayton*, 813 N.E.2d at 727.

125. 824 N.E.2d 553 (Ohio Ct. App. 2004), *rev'd*, 858 N.E.2d 776 (Ohio 2006).

126. *Id.* at 558.

127. *Id.* at 559.

128. *Id.* at 560.

129. *Id.*

130. *Id.*

statute and the ordinance.[131] That possibility had no legal significance, however, because the Eighth District saw no justification in Ohio law for recognizing the doctrine of implied preemption.[132]

About six months after this ruling (and just over a year after *City of Dayton* was decided), the Ohio Court of Appeals for the Sixth District, in *American Financial Services Ass'n v. City of Toledo*,[133] upheld the main provisions of yet another predatory lending ordinance using an analysis similar to that in *City of Cleveland*. The opinion in *City of Toledo*, however, contained a more detailed analysis of the issues. The Sixth District, like the Second District in *City of Dayton*,[134] began by focusing on the entire state predatory lending statute rather than on its preemption provision, and concluded that the state measure was a general law.[135] Nevertheless, relying heavily on the Eighth District's analysis in *City of Cleveland*, the *City of Toledo* court held that the statute's preemption provision violated the Ohio Constitution's home rule guarantee.[136] Although the preemption provision did not invalidate the entire Toledo ordinance, two relatively minor provisions of the ordinance did conflict with the state law.[137] Both of those provisions were severable,[138] so the balance of the ordinance remained a valid exercise of municipal authority.[139]

This brief summary makes clear that Ohio courts have disagreed not only about whether cities have home rule authority to regulate predatory lending but also about how to analyze that question. The Second District in *City of Dayton* held that cities do not have such authority, while the Eighth District in *City of Cleveland* and the Sixth District in *City of Toledo* held

131. The Cleveland ordinance had lower thresholds for interest rates, points, and fees as well as somewhat different disclosure requirements than did the state law. The ordinance also dealt with several issues that the state law did not address at all. *See id.* at 557.

132. *Id.* at 560.

133. 830 N.E.2d 1233 (Ohio Ct. App. 2005), *rev'd*, 859 N.E.2d 923 (Ohio 2006).

134. *See supra* notes 111-24 and accompanying text.

135. *City of Toledo*, 830 N.E.2d at 1243-44.

136. *Id.* at 1244. In support of its conclusion on this issue, the *City of Toledo* court quoted two pages of the *City of Cleveland* opinion. *See id.* at 1244-45 (quoting Am. Fin. Servs. Ass'n v. City of Cleveland, 824 N.E.2d 553, 560-61 (Ohio Ct. App. 2004), *appeal allowed*, 825 N.E.2d 622 (Ohio 2005)).

137. One conflict concerned the penalties for payments under a home-improvement contract, the other with the cancellation period for credit insurance. *Id.* at 1246-47.

138. *Id.* at 1248.

139. The court also found that the private right of action created by the ordinance violated the separation of powers doctrine by intruding on judicial authority and that two other provisions were void for vagueness, but all of these relatively minor provisions also were severable. *Id.* at 1249-51. It bears emphasis that the problems with these provisions had nothing to do with the city's home rule powers.

that they do. At the same time, the Sixth and Eighth Districts disagreed about whether to focus exclusively on the state law's preemption provision or on the statute as a whole. The Sixth District in *City of Toledo* agreed with the Second District in *City of Dayton* that what mattered was the entire statute, but they disagreed about whether that statute displaced municipal regulation of predatory lending.

As this Article was going to press, the Ohio Supreme Court reversed the Eighth District and held that the Cleveland ordinance was unconstitutional. In *American Financial Services Ass'n v. City of Cleveland*,[140] the court concluded that the state's legislation regulating predatory lending was a general law[141] and that the more stringent provisions of the Cleveland ordinance conflicted with the state measure.[142] A concurring justice reasoned that the state had validly expressed its intention to occupy the field and that the ordinance was therefore preempted regardless of any conflict with state law.[143] Two dissenting justices would have upheld the Cleveland ordinance. One found no conflict with state law;[144] the other thought that regulation of mortgage lending was not a matter of statewide concern and hence that municipalities remained free to adopt more stringent rules about predatory lending than the legislature had enacted.[145] A month later, relying on this ruling, the court struck down the Toledo ordinance as well.[146]

The divergent approaches in the Ohio courts should not obscure the lesson of this section: it is far from clear that cities have home rule authority to regulate predatory lending at all, at least if the state has enacted its own legislation in this field. Even if the Ohio Supreme Court upholds the power of Buckeye State cities, the New York and California decisions involving the New York City and Oakland ordinances stand as a warning that in two of our largest and most influential states, municipalities have no power to regulate predatory lending no matter how much harm that practice may do to local residents and the local social fabric. This does not necessarily mean that cities should sit idly by in the face of abuses. After

140. 858 N.E.2d 776 (Ohio 2006).

141. *Id.* at 784.

142. *Id.* at 785-86.

143. *Id.* at 790 (O'Connor, J., concurring in judgment only).

144. *Id.* at 791 (Resnick, J., dissenting).

145. *Id.* at 795, 797-98 (Pfeifer, J., dissenting). A thorough evaluation of these issues is beyond the scope of this Article. One of the authors is working on a separate paper that does seek to analyze the proper scope of home rule authority to regulate predatory lending in Ohio. *See* Shadya Y. Yazback, Home Lending and Home Rule in Ohio: Municipal Regulation of Predatory Lending (unpublished manuscript on file with the authors).

146. Am. Fin. Servs. Ass'n v. City of Toledo, 859 N.E.2d 923 (Ohio 2006) (mem.).

all, some states might permit cities to adopt their own ordinances. Even in states that do not allow local action, city initiatives might well stimulate state legislation. This was the pattern in all three of these states and in others as well.[147] Nevertheless, the several decisions discussed in this section serve as a warning about the limits of municipal action against predatory lending.

IV. FEDERAL PREEMPTION

Even if some cities have authority under state law to regulate predatory lending, they might face yet another insurmountable obstacle: federal preemption. Many lending institutions that make home loans are regulated by the federal government. The National Bank Act authorizes the Office of the Comptroller of the Currency to regulate nationally chartered banks,[148] and the Home Owners Loan Act authorizes the Office of Thrift Supervision to regulate federal savings associations.[149]

In *Mayor of New York v. Council of New York*,[150] a case discussed earlier in connection with home rule,[151] the court held that New York City's ordinance prohibiting the city from doing business with predatory lenders was preempted by federal law to the extent that the ordinance applied to federally chartered banks and federal savings associations. With respect to nationally chartered banks, regulations issued by the Office of the Comptroller of the Currency preempted several provisions of the ordinance,[152] and the Exportation Doctrine of the National Bank Act preempted local restrictions on interest rates.[153] Even without a clear conflict between the ordinance and Comptroller of the Currency regulations, allowing the city to apply its requirements to national banks would create an obstacle to the fulfillment of federal policies. That sufficed to find these provisions of the ordinance preempted to the extent

147. *See supra* notes 80, 83, 98-100; *supra* text accompanying note 112.

148. 12 U.S.C. §§ 1, 371 (2000).

149. *Id.* §§ 1462a-1464.

150. 780 N.Y.S.2d 266 (Sup. Ct. 2004).

151. *See supra* notes 81-87 and accompanying text.

152. *Mayor of New York*, 780 N.Y.S.2d at 272.

153. *Id.* The Exportation Doctrine is based on 12 U.S.C. § 85 (2000) (allowing a national bank to charge interest "at the rate allowed by the laws of the State, Territory, or District where the bank is located"). *See* Smiley v. Citibank (S.D.), N.A., 517 U.S. 735 (1996); Marquette Nat'l Bank of Minneapolis v. First of Omaha Serv. Corp., 439 U.S. 299 (1978). For a comprehensive discussion of the Exportation Doctrine, see Elizabeth R. Schiltz, *The Amazing, Elastic, Ever-Expanding Exportation Doctrine and Its Effect on Predatory Lending Regulation*, 88 MINN. L. REV. 518, 539-600 (2004).

that it applied to national banks.[154] Moreover, to the extent that enforcement of some parts of the ordinance entailed giving the city access to the records of national banks and allowing it to regulate activities permitted by federal law, those parts purported to confer on the city impermissible visitorial power over such banks without proper authorization.[155] With respect to federal savings associations, Office of Thrift Supervision regulations expressly preempted many provisions of the New York ordinance.[156] In any event, federal regulation was sufficiently pervasive as to occupy the field, leaving no room for local initiatives applicable to such institutions.[157]

The possibility of federal preemption goes well beyond local initiatives, however. Both the Office of the Comptroller of the Currency and the Office of Thrift Supervision have taken the position that federal law preempts state as well as municipal predatory lending initiatives.[158] No court has yet addressed that position with regard to state predatory lending laws. At the same time, a federal district court in *Office of the Comptroller of the Currency v. Spitzer*[159] recently held that federal regulations prevent state authorities from enforcing fair housing laws against national banks.[160]

Assuming that federal law and regulations do preempt state and local predatory lending initiatives,[161] cities that have home rule authority to act

154. *Mayor of New York*, 780 N.Y.S.2d at 272.

155. *Id.; see* 12 U.S.C. § 484(a) (2000) ("No national bank shall be subject to any visitorial powers except as authorized by Federal law, vested in the courts of justice or such as shall be, or have been exercised or directed by Congress or by either House thereof or by any committee of Congress or of either House duly authorized."). The Office of the Comptroller of the Currency has promulgated a regulation that defines visitorial authority as "exclusive," and to include "conducting examinations, inspecting or requiring the production of books or records of national banks." 12 C.F.R. §§ 7.4000(a)(3), 7.4000(a)(1) (2007).

156. *Mayor of New York*, 780 N.Y.S.2d at 271 & n.7.

157. *Id.* at 272. Finally, the court found that section 501 of the Depository Institutions Deregulation and Monetary Control Act, 12 U.S.C. § 1735f-7a (2000), expressly preempted interest rates, points, and fees for first mortgages on one- to four-family residences. *Mayor of New York*, 780 N.Y.S.2d at 272-73.

158. *See* Julia Patterson Forrester, *Still Mortgaging the American Dream: Predatory Lending, Preemption, and Federally Supported Lenders*, 74 U. CIN. L. REV. 1303, 1339-40 (2006).

159. 396 F. Supp. 2d 383 (S.D.N.Y. 2005).

160. *See also* Clearing House Ass'n v. Spitzer, 394 F. Supp. 2d 620 (S.D.N.Y. 2005) (reaching the same conclusion in a case brought by commercial banks).

161. Resolving whether federal law should preempt such initiatives is beyond the scope of this Article. Most commentators have criticized broad federal preemption as either unauthorized by current law or unwise as a matter of policy. *See, e.g.*, Nicholas Bagley, Note, *The Unwarranted Regulatory Preemption of Predatory Lending Laws*, 79 N.Y.U. L. REV. 2274 (2004); Keith R. Fisher, *Toward a Basal Tenth Amendment: A Riposte to*

might still have some reason to adopt predatory lending ordinances. After all, federal preemption applies only to federally regulated financial institutions. Not all home loans are made by such institutions or by entities that are related to them. Although precise data are hard to come by, a noticeable fraction of these loans is made by so-called nondepository institutions, i.e., entities other than commercial banks, savings institutions, and credit unions.[162] Information compiled by the Federal Reserve System shows that mortgage companies (which are nondepository institutions) received more than 60 percent of all home loan applications in 2005 even though such companies made up only about one-fifth of the total number of lenders.[163] Some mortgage companies are affiliated with federally regulated depository institutions, but approximately 15 percent were independent and therefore not subject to federal regulation.[164] We should treat these figures with caution, however, because the Federal Reserve study covers only about 80 percent of the country's home lending.[165] Although we are dealing with an estimate, there is no reason to doubt that at least some predatory loans are not subject to federal regulation. That leaves room for state and local measures applicable to lenders that are not encompassed by expansive federal preemption.

The justification for cities with home rule power to adopt predatory lending ordinances might be stronger in some communities than in others. Subprime lending—which is not necessarily, but often is, predatory[166]—has grown significantly in recent years, and that growth has not been uniform.[167] In some places, as many as half of all home loans are made by entities that are not subject to federal oversight.[168] Cities facing that situation might find it important to fill this regulatory void, even if local ordinances might be able to address only part of the predatory lending

National Bank Preemption of State Consumer Protection Laws, 29 HARV. J.L. & PUB. POL'Y 981 (2006); Forrester, *supra* note 158, at 1359-70; Diana McMonagle, Note, *In Pursuit of Safety and Soundness: An Analysis of the OCC's Anti-Predatory Lending Standard*, 31 FORDHAM URB. L.J. 1533 (2004).

162. Avery et al., *supra* note 14, at A129.

163. *Id.*

164. *Id*.

165. *Id.* at A123.

166. *See supra* text accompanying note 8.

167. *See* Susan M. Wachter et al., *Subprime Lending: Neighborhood Patterns Over Time in US Cities* (Univ. of Pa. Law Sch. Inst. for Law and Econ. Research Paper No. 06-19, 2006), *available at* http://ssrn.com/abstract_id=920847.

168. *See, e.g.*, Becky Gaylord, *City Let Banks Ignore Law*, CLEVELAND PLAIN DEALER, Sept. 22, 2006, at A1 (citing a study finding that, in Cleveland, banks and other regulated entities made about 70 percent of home loans in 2000 but only around 50 percent of such loans in 2005).

problem.

CONCLUSION

Communities that experience the abuses associated with predatory lending have powerful reasons for seeking to combat the many harms resulting from that phenomenon. Unfortunately, they have only limited legal tools available for this purpose. Cities cannot sue as *parens patriae* in federal court, and they might not be able to do so in many state courts. They might have standing to seek relief for harm to the community, as opposed to individual residents, but such lawsuits could founder on difficult problems of proof. Directly regulating predatory lending poses additional challenges. It is far from clear that cities have authority under their home rule powers. Even if they do, state statutes might preempt important aspects of municipal ordinances. Perhaps more daunting, the prospect of federal preemption of even state laws to the extent that those laws apply to federally regulated lenders further limits the possibilities for effective local measures.

Nevertheless, there might be good reasons for cities to consider adopting their own regulations. Most important, some cities might have the authority to act. Even if that authority is limited or nonexistent, municipal ordinances have stimulated state legislation. To be sure, state measures have not been as strong as the local initiatives that prompted them. At the same time, getting even a weak statute enacted provides an opportunity for strengthening amendments in the future. Perhaps state measures can help to persuade federal authorities either to cut back on the scope of preemption or to take more vigorous action against predatory lenders within the sphere of their authority. Additionally, federal preemption applies only to national banks, federal savings associations, and their affiliates. Although that covers a wide swath of residential lending, it still allows for local action against other lenders that might have a significant effect on a city's social fabric. In the end, cities working alone cannot solve the predatory lending problem. Some of them might, however, help to serve as catalysts for whatever solutions might be devised.