Cullen | Dykman

Federal Appeals Court Holds that New York Mortgage Escrow Account Law is Preempted as to National Banks

September 20, 2022

A federal appeals court has held that a New York State law requiring mortgage lenders to pay interest on certain residential mortgage escrow accounts is preempted as to national banks, and that such banks do not have to comply with the state law. The decision reverses a 2019 opinion of a federal district court and unless this case is appealed to the U.S. Supreme Court and overturned, national banks may cease paying interest on mortgage escrow accounts under New York law.

Background

New York General Obligations Law § 5-601 states that any mortgage investing institution which maintains a mortgage escrow account on any one to six family residence occupied by the owner or on any property owned by a cooperative apartment corporation must, for each quarterly period in which such escrow account is established, provide a minimum rate of interest on such accounts at a rate of no less than two percent per year. [1]

National banks had generally taken the view for years that state laws requiring lenders to pay interest on mortgage escrow accounts, including New York's law, were preempted under the National Bank Act and general preemption principles. The Office of the Comptroller of the Currency, the regulator of national banks, had concurred in this view. However, a federal appeals court in 2018 held that a California law requiring mortgage lenders to pay interest on certain mortgage escrow accounts was *not* preempted as to national banks.[2] That case was followed in 2019 by an opinion from the Federal District Court in the Eastern District of New York that New York's law requiring the payment of interest on mortgage escrow accounts was also not preempted as to national banks. It is that 2019 District Court opinion that has now been reversed.

Second Circuit Opinion

In *Cantero v. Bank of America, N.A.*,[3] the United States Court of Appeals for the Second Circuit reviewed general preemption principles and how those principles applied to a state law imposing an obligation on a national bank to pay interest on mortgage accounts. The court found that the state law "target[s], curtail[s], and hinder[s] a power granted to national banks by the federal government." The court concluded that "under ordinary preemption rules, GOL § 5-601 is preempted" and that "no interest is due to plaintiffs under 'federal law and the

law of New York State.'"

As the Second Circuit opinion in *Cantero* now conflicts with the Ninth Circuit's 2019 opinion in *Lusnak*, there is the potential that this issue could be resolved by the U.S. Supreme Court.

Please note that while this decision applies expressly to national banks and not to other federally chartered financial institutions, the decision provides a strong basis to argue that federal savings associations are also exempt from the New York interest on mortgage escrow requirement. In addition, the decision is an important precedent for a similar claim of exemption by federal credit unions.

We will continue to monitor developments on this issue. If you have any questions regarding this case or federal preemption issues for federally-chartered institutions in general, please feel free to contact Joseph D. Simon at (516) 357-3710 or via email at **jsimon@cullenllp.com,** Elizabeth A. Murphy at (516) 296-9154 or via email at **emurphy@cullenllp.com,** or Gabriela Morales at (516) 357-3850 or via email at **gmorales@cullenllp.com**.

Footnotes

[1] The New York State Department of Financial Services issued an order in 2018 allowing state-chartered institutions to pay the *lesser of* two percent or the six-month yield on United States Treasury securities on the last business day of the immediately preceding calendar quarter.

[2] *Lusnak v. Bank of America*, No. 14-56755, 2018 WL 1122298 (9th Cir. Mar. 2, 2018).

[3] *Cantero v. Bank of America*, Nos. 21-400, 21-403, 2022 WL 4241359 (2d Cir. Sep. 15, 2022). *Cantero* was combined with the case which was the subject of the 2019 District Court decision, *Hymes v. Bank of America*, No. 18-CV-2352 (RRM) (ARL), 2019 WL 4888123 (E.D.N.Y. Sept. 30, 2019).

Practices

- Banking and Financial Services
- Regulatory and Compliance

Attorneys

- Joseph D. Simon
- Elizabeth A. Murphy
- Gabriela Morales