No. 22-842

IN THE
Supreme Court of the United States

THE NATIONAL RIFLE ASSOCIATION OF AMERICA,
Petitioner,
v.
MARIA T. VULLO,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF OF FINANCIAL AND BUSINESS LAW SCHOLARS AS *AMICI CURIAE* IN SUPPORT OF PETITIONER

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INTEREST OF THE *AMICI CURIAE*[1]

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Petitioner's case is important to *amici* because it involves financial regulators' unique powers to bind regulated firms even via informal and indirect statements and guidance.

SUMMARY OF THE ARGUMENT

The Court should grant the Petition because the court below erred in finding that the lack of explicit binding language or threats from the New York Department of Financial Services in its guidance letters meant that no reasonable regulated firm would consider itself bound by those letters. The reality of banking and insurance regulation is that firms

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[1] No counsel for any party has authored this brief in whole or in part, and no entity or person, aside from *amici curiae*, the Mercatus Center, and their counsel, made any monetary contribution intended to fund the preparation or submission of this brief. All parties have received timely notification of the filing of this brief.

frequently feel that they risk sanction if they do not comply with nominally non-binding guidance. The Court should grant the Petition and review this recurring issue of significant importance.

ARGUMENT

In its opinion upholding the dismissal of Petitioner's suit, the Second Circuit opined that because Superintendent Vullo's statements were "written in an even-handed, nonthreatening tone" and "employed words intended to persuade rather than intimidate," they did not "intimat[e] that some form of punishment or adverse regulatory action [would] follow the failure to accede to the … request."[2] The Second Circuit relied on this conclusion to hold that Petitioner's complaint failed even to "plausibly alleg[e] unconstitutional threats or coercion."[3]

But the Second Circuit did not appreciate that the unique relationship between financial regulators and their regulated firms tends to make those firms feel bound, on penalty of sanction, by even the most prosaic sounding guidance. Regulated firms have historically faced formal and informal penalties for failure to conform to guidance that was nominally non-binding.

This Court should grant the Petition and reverse.

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[2] Pet.App.29.

[3] Pet.App.31.

I. Banks and Insurance Firms Are Subject to a Uniquely Vague and Opaque Regulatory Environment.

Banking and insurance are vital services without which it is hard, if not impossible, to function in the modern economy.[4] Yet banks and insurance firms are subject to a regulatory regime that enables regulators to exercise significant discretion with very limited transparency.[5] Regulators are able to exercise a level of control over regulated firms that can make them look more like co-managers of the firm than outside regulators, including, for example: influencing what

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[4] *See* Brian Knight & Trace Mitchell, *Private Policies and Public Power: When Banks Act as Regulators within a Regime of Privilege*, 13 N.Y.U. J. L. & LIBERTY 66, 132–33 (2020) (discussing views on the importance of banking); George A. Mocsary, *Administrative Browbeating and Insurance Markets* 1–7, Working Paper, MERCATUS CTR. AT GEO. MASON UNIV. (Dec. 2022), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4296576 (discussing importance of insurance for the modern economy).

[5] *See Guidance, Supervisory Expectations, and the Rule of Law: How Do the Banking Agencies Regulate and Supervise Institutions: Hearing Before the S. Comm. on Banking, Housing, and Urban Affairs*, 116th Cong. 36 (2019) (statement of Margaret E. Tahyar, Partner, Davis Polk and Wardwell LLP) ("[Bank] [s]upervision happens behind closed doors. It relies on secrecy and involves a system of discretionary actions by supervisory staff."); Julie Hill, *Regulating Bank Reputation Risk*, 54 GA. L. REV. 523, 568–70 (2020); Mocsary, *supra* note 4, at 8–9 (discussing the opacity and limited political accountability of insurance regulation).

lawful products they offer or decline to offer,[6] and deciding whether banks can open new locations or change locations,[7] whether the bank and insurance company can do business at all, and whether to remove the firms' directors and officers and even ban them from the industry.[8]

Further, banks and insurance firms are subject to pervasive ongoing supervision. Regulators actively monitor firms for current and future compliance, rather than merely react to perceived problems.[9] Examination and supervision are usually done confidentially, with the conversations and determinations made by supervising regulators remaining out of public view.[10]

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[6] Hill, *supra* note 5, at 576–78 (discussing efforts by the FDIC, using aggressive tactics, to discourage banks from offering tax refund anticipation loans, a lawful product disfavored by regulators); Mocsary, *supra* note 4, at 11–12.

[7] 12 C.F.R. §§ 5.30–5.31 (OCC regulations requiring OCC approval before national banks and federal savings associations may establish or move branches); N.Y. BANKING LAW §§ 28, 29 (McKinney) (requiring NYDFS Superintendent approval before a New York bank may change location or open a branch).

[8] Knight & Mitchell, *supra* note 4, at 75–82 (discussing government-imposed barriers to entry in banking.); 12 U.S.C. § 1818; N.Y. INS. LAW § 1102(d) (McKinney); N.Y. BANKING LAW § 41 (McKinney); N.Y. COMP. CODES R. & REGS. tit. 3, §§ 2.2, 2.4.

[9] Randal K. Quarles, Vice Chair, Bd. of Governors of the Fed. Res. Sys., Law and Macroeconomics: The Global Evolution of Macroprudential Regulation, Address at Geo. Univ. L. Ctr. (Sept. 27, 2019), https://www.federalreserve.gov/newsevents/speech/quarles20190927a.htm.

[10] Tahyar, *supra* note 5.

1. Bank and insurance regulators have largely adopted a "risk-focused" regulatory approach where regulators monitor firms for threatening risks.[11] In addition to obvious risks such as credit risk and legal risk, regulators monitor banks' "reputation risk." While the definition varies somewhat by regulator, the concept is broad. For example, the Office of the Comptroller of the Currency states that reputation risk includes "risk to [the bank's] current or projected financial condition and resilience arising from negative public opinion."[12] The relevant audience for assessing risk to a bank's reputation includes not only customers, but also "shareholders, regulators, … other stakeholders, and the community at large."[13] The Federal Reserve does not list specific audiences but rather states that "[r]eputational risk is the potential that negative publicity regarding an institution's business practices, whether true or not, will cause a decline in the customer base, costly litigation, or revenue reductions."[14] These definitions are sweeping and vague, and provide significant discretion to examiners.

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[11] Hill, *supra* note 5, at 544–46 (discussing rise of risk-based regulation).

[12] OFF. OF THE COMPTROLLER OF THE CURRENCY, COMPTROLLER'S HANDBOOK: SAFETY AND SOUNDNESS, CORPORATE AND RISK GOVERNANCE 4 (July 2019).

[13] *Id.*

[14] BD. OF GOVERNORS OF THE FED. RES. SYS., SR 95-51, RATING THE ADEQUACY OF RISK MANAGEMENT PROCESSES AND INTERNAL CONTROLS AT STATE MEMBER BANKS AND BANK HOLDING COMPANIES (Nov. 4, 1995).

Despite, or perhaps because of, this ambiguity, the concept of reputation risk has permeated federal banking regulatory guidance.[15] It has expanded to include not only reputation risk caused by the bank's conduct, but also by the bank's customers, on the theory that a controversial customer—even one who does nothing illegal—may alienate other constituencies and harm the bank's financial position.[16]

At the federal level, reputation risk is usually found in regulatory guidance rather than a rule or statute.[17] As Professor Julie Hill notes, this means that enforcement actions targeting reputation risk would generally need to be tied to an "unsafe or unsound" practice to have a legal basis.[18]

But that fails to serve as a meaningful check because the exact scope of what constitutes an "unsafe or unsound" practice that can enable a regulator to act is likewise open-ended and often disputed. In the federal context, bank regulators have asserted a broad definition that includes any action or nonaction posing an "abnormal risk or loss or damage to an institution, its shareholders, or the agencies administering the

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[15] Hill, *supra* note 5, at 549–53 (discussing the proliferation of reputation risk in federal banking regulation).

[16] *Id*. at 552.

[17] *Id*. at 557.

[18] *Id*. at 557–58.

insurance funds[,]" even if the loss would not imperil the institution.[19]

Courts are divided on how broadly "unsafe and unsound" is defined in federal law. Although the Third, Fifth, and D.C. Circuits have narrowed the definition to encompass only risks that threaten bank stability,[20] the Second, Eighth, and Eleventh Circuits have embraced the broader standard advocated by federal regulators—i.e., any "abnormal risk."[21] Given the Second Circuit's outsized influence in matters of finance, its broad approach to allowing such investigations is especially significant.

Taken together, regulators can launch investigations into institutions' "reputation risk" premised only on how the public or the regulators themselves may view the institution and its customers, often with no meaningful consideration of whether that "risk" actually affects the institution's financial soundness. This lets regulators directly tie legal oversight with an institution's provision of services to entities or individuals who are unpopular in some camps or with whom the regulator disagrees as a policy matter.

The regulatory structure also discourages regulated firms from challenging their regulators and

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[19] *Id.* at 558 (quoting *Financial Institutions Supervisory and Insurance Act of 1966: Hearings on S. 3158 and S. 3695 Before the H. Comm. on Banking and Currency*, 89th Cong. 50 (1966) (memorandum submitted by John Horne, Chairman of the Federal Home Loan Bank Board)).

[20] Hill, *supra* note 5, at 558–60.

[21] *Id.* at 560.

makes it hard to point to a concrete act that could give rise to a discrete legal challenge. Because banks and insurance firms are locked into an ongoing supervisory relationship with their regulators, they know that resistance to the regulator on one topic may result in informal—but no less painful—reprisal over time.[22] The regulator can make the regulatory process itself the punishment. This makes it difficult or impossible to challenge in court. Moreover, a lawsuit would only further alienate the regulator.

2. While the New York State Department of Financial Services (NYDFS) is governed by New York rather than federal law, its regulation of banks and insurance companies has many parallels. The NYDFS is tasked with ensuring that banks[23] and insurance[24] companies operate in a safe and sound manner. New York law grants the NYDFS broad latitude to pursue this objective. For example, the Superintendent of the NYDFS has the discretion to refuse to grant an insurance license if she does not believe that granting a license would be in the best interest of New Yorkers.[25] Likewise, the Superintendent may reject a request to form a bank under the laws of New York if

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[22] *Id.* at 579–83 (discussing Nicholas R. Parrillo, *Federal Agency Guidance and the Power to Bind: An Empirical Study of Agencies and Industries*, 36 YALE J. REG. 165, 174 (2019)).

[23] N.Y. BANKING LAW § 14(q) (McKinney).

[24] ROBERT H. JERRY, II & DOUGLAS R. RICHMOND, UNDERSTANDING INSURANCE LAW §§ 20, 22 (5th ed. 2012); N.Y. INS. LAW § 309 (McKinney).

[25] N.Y. INS. LAW § 1102(d) (McKinney).

she believes the bank would not promote the "public convenience and advantage."[26]

This significant power does not end after initial permission is granted. For example, the NYDFS has broad authority to examine banks[27] and insurance companies.[28] It also uses the concept of reputation risk in its regulation of banks and insurance firms.[29] In fact, reputation risk was explicitly highlighted in the industry letters sent by NYDFS asking banks[30] and insurance firms[31] to evaluate their relationships with the National Rifle Association of America (NRA) and other "gun promotion" groups. In its opinion below, the Second Circuit summarized the basis for the Superintendent's actions: "a business's response to social issues can directly affect its financial stability" and fall within the ambit of NYDFS's jurisdiction.[32]

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[26] N.Y. BANKING LAW § 24 (McKinney).

[27] *Id.* § 36.

[28] N.Y. INS. LAW § 309 (McKinney).

[29] Hill, *supra* note 5, at 553–56 (discussing the NYDFS's use of reputation risk in regulation).

[30] Letter from Maria T. Vullo, Superintendent, N.Y. Dept of Fin. Servs., to the CEO or Equivalents of N.Y. State Chartered or Licensed Fin. Insts. (Apr. 19, 2018), https://www.dfs.ny.gov/system/files/documents/2020/03/il20180419_rm_nra_gun_manufacturers_banking.pdf.

[31] Letter from Maria T. Vullo, Superintendent, N.Y. Dept of Fin. Servs., to the CEO or Equivalents of All Insurers Doing Business in the State of New York (Apr. 19, 2018), https://www.dfs.ny.gov/system/files/documents/2020/03/il20180419_rm_nra_gun_manufacturers_insurance.pdf.

[32] Pet.App.30.

Thus, just as with federal regulators, the NYDFS can directly invoke regulatory power simply because institutions provide service to a customer that can be cast as unpopular or with whom the NYDFS disagrees on policy matters.[33]

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Banking and insurance operate within a uniquely nebulous and opaque regulatory environment. They are also under regular supervision and must rely on their regulator for permission to operate. These traits contribute to an environment where banks and insurance firms are likely to believe that guidance is de facto binding, including specifically in the realm of providing services to customers with whom the regulators may disagree politically.

II. The Nature of Banking and Insurance Regulation Encourages Regulated Firms to Feel Bound by Guidance and Subject to Sanction for Noncompliance.

Banking and insurance face unique regulatory structures and incentives that cause firms to treat regulatory guidance as binding. As such, there is often an implied threat of sanction even when agency guidance lacks an explicit threat. Banking or insurance firms would thus reasonably believe that failure to comply with NYDFS guidance would result

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[33] For example, New York courts once upheld a pre-NYDFS Superintendent's decision to liquidate a beneficial organization on the basis that it was hazardous to the public because it "operated as an arm of the Communist party." *In re Int'l Workers Order, Inc.*, 280 A.D. 517, 519 (N.Y. App. Div. 1952).

in some sort of punishment, either formally or informally.

For example, a study for the Administrative Conference of the United States (ACUS) by Professor Nicholas Parrillo found that in the context of federal regulation, regulated parties "often face overwhelming practical pressure to follow what a guidance document 'suggests.'"[34] He notes that banks are likely to find themselves bound by guidance because they are so dependent on maintaining good relationships with their regulators.[35] This ranges from receiving regulator approval for engaging in certain business activities, like opening branches, to being subject to regular examination by their regulator. And because complete compliance with banking regulations is likely impossible, banks are concerned that failing to comply with guidance will cause regulators not to work cooperatively with them on other issues.[36]

This problem is exacerbated by the strong incentive, discussed above, for entities not to challenge regulator decisions because the regulator can "'make life miserable' for a bank in all sorts of ways"[37] that do not necessarily involve a formal

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[34] Nicholas R. Parrillo, *Federal Agency Guidance and the Power to Bind: An Empirical Study of Agencies and Industries*, 36 YALE J. REG. 165, 174 (2019); *see also* Nicholas R. Parrillo, *Federal Agency Guidance: An Institutional Perspective,* ADMIN. CONF. OF THE U.S. (Oct. 12, 2017).

[35] Parrillo, *supra* note 34, 36 YALE J. REG. at 192.

[36] *Id.* at 192–95.

[37] *Id.* at 195; Hill, *supra* note 5, at 579–83.

enforcement action. In short, bank regulators fully understand that they can control bank behavior by merely "raising an eyebrow."[38]

Informed by Parrillo's study, ACUS promulgated a recommendation on how agencies could avoid giving the mistaken impression that their guidance statements were legally binding.[39] One of its recommendations was that an agency's statement should prominently disclaim that it was binding and explicitly state that the target of the guidance could take alternative lawful approaches.[40] While the ACUS recommendation is nonbinding and not directly aimed at state regulators like NYDFS, it is worth noting that the NYDFS's statements lacked language comparable to the ACUS recommendation. Rare is the regulator that would so honestly disclaim its own asserted powers.[41]

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[38] Parrillo, *supra* note 34, 36 YALE J. REG. at 195; *see also* Hill, *supra* note 5, at 581–82.

[39] ADMIN. CONF. OF THE U.S., ADMINISTRATIVE CONFERENCE RECOMMENDATION 2017-5, AGENCY GUIDANCE THROUGH POLICY STATEMENTS (Dec. 14, 2017), https://www.acus.gov/sites/default/files/documents/Recommendation%202017-5%20%28Agency%20Guidance%20Through%20Policy%20Statements%29_2.pdf.

[40] *Id.* at 7.

[41] The exception that proves the rule is the 15-month period from October to 2019 to January 2021 during which Executive Order 13,891 was in effect, which "require[d] that [federal] agencies treat guidance documents as non-binding both in law and in practice." *See* Exec. Order No. 13,891, § 1, 84 Fed. Reg. 55,235 (Oct. 15, 2019), *revoked by* Exec. Order No. 13,992, 86 Fed. Reg. 7049 (Jan. 20, 2021).

III. Prior Incidents in Banking and Insurance Regulation Make Clear that Failing to Adhere to Guidance Could Result in Sanction.

Banks and insurance firms that have failed to adhere to nominally nonbinding guidance have repeatedly suffered reprisal at the hands of their regulators. These incidents generated sufficient controversy that bankers and insurance companies were well aware of them by the time NYDFS released its guidance regarding the NRA and "other gun promotion organizations." The lessons from these incidents would have colored regulated firms' assessment of whether they would face sanction for failing to comply with the NYDFS's guidance.

1. The most poignant example is the Federal Deposit Insurance Corporation's (FDIC's) recent effort to use risk, including "reputation risk," as a justification to pressure banks to stop offering refund anticipation loans (RALs) to consumers and to stop providing banking services to so-called "payday lenders." In both cases, the FDIC could not prohibit the banks' conduct outright but instead relied on guidance combined with "moral suasion" and ratcheting up the intensity of supervisory and examination activities to "persuade" the banks that it was not in their best interest to maintain relationships with the disfavored industries.[42]

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[42] *See generally* OFF. OF INSPECTOR GEN., FED. DEPOSIT INS. CORP., REPORT NO. OIG-16-001, REPORT OF INQUIRY INTO THE FDIC'S SUPERVISORY APPROACH TO REFUND ANTICIPATION LOANS

RALs are lawful products but became disfavored after advocacy organizations lobbied FDIC leadership in 2008.[43] FDIC leadership began pressuring the handful of banks that provided the service to stop.[44] As the FDIC's Office of the Inspector General (OIG) notes, because RALs were legal, FDIC staff relied on "risk management" as a justification to engage with the banks. According to the OIG, the justification for discouraging RALs "morphed over time."[45] The FDIC promulgated no rule or guidance related to RALs, but instead used "more generic guidance" as the standard to which they sought to hold banks.[46]

The FDIC was ultimately successful in driving banks out of the RAL market,[47] but only through what the OIG described as "unprecedented efforts to use the FDIC's supervisory and enforcement powers" and the

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AND THE INVOLVEMENT OF FDIC LEADERSHIP AND PERSONNEL iii (Feb. 2016) [hereinafter FDIC OIG REPORT NO. OIG-16-001] (the FDIC OIG did not release the full report because it contained "sensitive information"); OFF. OF INSPECTOR GEN., FED. DEPOSIT INS. CORP., REPORT NO. AUD-15-008, THE FDIC'S ROLE IN OPERATION CHOKE POINT AND SUPERVISORY APPROACH TO INSTITUTIONS AND CONDUCTED BUSINESS WITH MERCHANTS ASSOCIATED WITH HIGH-RISK ACTIVITIES (Sept. 2015) [hereinafter FDIC OIG REPORT NO. AUD-15-008].

[43] Hill, *supra* note 5, at 533 n.49 (citing FDIC OIG REPORT NO. OIG-16-001, *supra* note 42, at i & n.2).

[44] FDIC OIG REPORT NO. OIG-16-001, *supra* note 42, at i–ii.

[45] *Id.* at ii.

[46] *Id.*

[47] *Id.*

"circumvention of certain controls surrounding the exercise of enforcement powers."[48]

The OIG found that FDIC officials in Washington directed staff to lower Safety and Soundness report ratings of banks offering RALs, with the downgrade being predetermined before examination in at least one case.[49] The OIG also found that FDIC officials refused to accept a risk analysis that showed banks' ability to mitigate risk and that those same officials reworked the analysis until they got their desired result.[50] The FDIC prohibited a bank from pursuing its desired strategy of buying failed institutions unless it discontinued offering RALs.[51]

Additionally, the FDIC used its supervisory authority as a stick to gain compliance. An FDIC attorney "abusively" threatened the banks' leadership, in one instance telling a bank's board that "nothing would be off the table" if it refused to cease offering RALs, including the use of "extraordinary examination resources," where over four hundred examiners would examine banks that offered RALs and their tax preparer partners, in an effort to find violations the FDIC could use to justify punishing banks that refused to abide by the FDIC's guidance.[52]

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[48] *Id.*

[49] *Id.*

[50] *Id.* at iii.

[51] FDIC OIG REPORT NO. AUD-15-008, *supra* note 42, at 38.

[52] FDIC OIG REPORT NO. OIG-16-001, *supra* note 42, at iii; FDIC OIG REPORT NO. AUD-15-008, *supra* note 42, at 39.

The FDIC's tactics ultimately prevailed, but as the OIG noted, the FDIC's actions resulted in significant harm to the target banks even though there was a lack of "examination-based evidence of harm caused by RAL programs" in the first place.[53]

It is worth noting that the FDIC's actions against banks offering RALs demonstrate many of the factors Parrillo cites[54] for why firms often feel bound by guidance. The FDIC was able to prevent one bank from pursuing an unrelated business strategy by withholding permission unless the bank complied with guidance. The FDIC was also able to leverage its examination power to intimidate and punish banks that refused to comply.[55]

2. Following the RAL controversy, the FDIC became embroiled in the infamous "Operation Choke Point." Operation Choke Point began as a Department of Justice (DOJ) initiative to get banks and payments processors to cut off fraudulent companies' access to the Federal Reserve's payments system.[56] While the exact degree of the FDIC's direct involvement in DOJ's operation is disputed,[57] it is clear that FDIC

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[53] FDIC OIG REPORT NO. OIG-16-001, *supra* note 42, at ii.

[54] *See* notes 34–38, *supra*, and accompanying text.

[55] FDIC OIG Report No. OIG-16-001, *supra* note 42, at ii–iii; FDIC OIG Report No. AUD-15-008, *supra* note 42, at 38–40.

[56] Hill, *supra* note 5, at 572; FDIC OIG REPORT NO. AUD-15-008, *supra* note 42, at 1.

[57] *Compare* FDIC OIG REPORT NO. AUD-15-008, *supra* note 42, at ii ("FDIC's involvement in Operation Choke Point [was] inconsequential to the overall direction and outcome of the

guidance was used by DOJ. At a minimum, DOJ included with its subpoenas to banks a copy of the FDIC's Financial Institution Letter (FIL) FIL-3-2012. This document discussed alleged risks posed to banks from relationships with payment processors that served certain industries.[58] The FDIC guidance included a footnote with what it claimed was a non-exclusive list of industries that may have a higher incidence of fraud, including firearms, payday loans, and tobacco.[59] The guidance did not explain the FDIC's methodology or how it arrived at the list of industries.

Roughly contemporaneously with DOJ's efforts, the FDIC engaged in its own efforts to influence banks' customer choices. Before the previously mentioned guidance, the FDIC ran an article in its *Supervisory Insights* magazine that discussed risks posed to banks by third-party relationships.[60] The article identified some general criteria for what may

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initiative."), *with* STAFF OF SUBCOMM. ON ECONOMIC GROWTH, JOB CREATION, AND REGULATORY AFFAIRS, H. COMM. ON OVERSIGHT AND GOVERNMENT REFORM, FEDERAL DEPOSIT INSURANCE CORPORATION'S INVOLVEMENT IN "OPERATION CHOKE POINT" 15–16, 113TH CONG. (Comm. Print 2014), https://republicans-oversight.house.gov/report/federal-deposit-insurance-corporations-fdic-involvement-operation-choke-point/ [hereinafter COMM. REP. ON OPERATION CHOKE POINT] (alleging an active partnership between DOJ and FDIC).

[58] COMM. REP. ON OPERATION CHOKE POINT, *supra* note 57, at app. 141, *available at* https://republicans-oversight.house.gov/wp-content/uploads/2014/12/Appendix-1.pdf.

[59] *Id.* at app. 141 n.1.

[60] *Id.* at app. 152.

constitute a high-risk payment.[61] The article then provided a nonexclusive list of thirty merchant categories that it identified as being associated with high-risk activities, including firearms, coin dealers, and payday loans.[62]

Shortly after the release of these guidance documents, reports began of banks dropping customers in the identified high-risk industries.[63] It is disputed whether the FDIC intended to use the high-risk list to motivate banks to cut ties with payments processors who served those industries, either directly or through motivating examiners to view such relationships more skeptically.[64]

But the *effect* of discouraging banks from serving industries on the high-risk list is undisputed.[65] The FDIC acknowledged as much because it revised its summer 2011 *Supervisory Insights* journal article[66] to remove the list of high-risk industries.[67] It also published new and revised guidance to make clear

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[61] *Id.* at app. 155–56.

[62] *Id.* at app. 156.

[63] Hill, *supra* note 5, at 573–74.

[64] *Compare* OIG REPORT NO. AUD-15-008, *supra* note 42 at 17, *with* COMM. REP. ON OPERATION CHOKE POINT, *supra* note 57, at 3–7.

[65] OIG REPORT NO. AUD-15-008, *supra* note 42, at 19; COMM. REP. ON OPERATION CHOKE POINT, *supra* note 57, at 7.

[66] COMM. REP. ON OPERATION CHOKE POINT, *supra* note 57, at app. 152.

[67] OIG REPORT NO. AUD-15-008, *supra* note 42, at 19.

that banks that can manage the risk posed by a lawful relationship are not prohibited from doing business.[68]

3. The efforts of FDIC officials to have banks cut ties with disfavored industries, especially payday lending, did not stop at general guidance. Several FDIC officials used "moral suasion" to discourage banks from doing business with payday lenders, despite recognizing that there was no legal ground to force the banks to quit the relationships.[69] In at least one case, an FDIC Regional Director directly told a bank that partnering with a payday lender was generally "unacceptable for an insured [] institution," despite there being no legal prohibition against it,[70] as an FDIC official later acknowledged.[71] Although the bank's state regulator had no objection to the arrangement, the bank opted to terminate its

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[68] *Id*. (citing Fed. Deposit Ins. Corp., FIL-41-2014, FDIC Clarifying Supervisory Approach to Institutions Establishing Account Relationships with Third-Party Payment Processors (July 28, 2014), and Fed. Deposit Ins. Corp., FIL-43-2013, FDIC Supervisory Approach to Payment Processing Relationships with Merchant Customers that Engage in Higher-Risk Activities (Sept. 27, 2013, *rev'd*, July 2014)).

[69] Hill, *supra* note 5, at 575–76; FDIC OIG REPORT NO. AUD-15-008, *supra* note 42, at 23–28.

[70] Letter from M. Anthony Love, Regional Director, Chicago Regional Office, Fed. Deposit Ins. Corp., to Board of Directors of [name redacted], FDIC-ICR-0085 (Feb. 15, 2013), *available at* COMM. REP. ON OPERATION CHOKE POINT, *supra* note 57, at app. 121.

[71] FDIC OIG REPORT NO. AUD-15-008, *supra* note 42, at 27 ("In the end, we are getting them out of [ACH processing for a payday lender] through moral persuasion and as you know from a legal perspective we don't have much of a position, if any.").

relationship with the payday lender.[72] In a letter to the FDIC Chicago Regional Office, the bank's CEO criticized the FDIC's use of supervision as a tool to pressure the bank to end a business relationship without there being identified risks to the bank's safety and soundness other than reputation risk.[73]

The motivations, propriety, and actions of FDIC officials against payday lenders remain disputed. A lawsuit[74] filed by lenders against the FDIC and other regulators[75] alleged that they improperly pressured banks to cut ties with the plaintiffs, driven in part by the policy preferences of regulatory officials.[76] In settling the suit, the FDIC acknowledged that "certain employees acted in a manner inconsistent with FDIC policies with respect to payday lenders" and that this "created misperceptions about the FDIC's policies."[77] The letter further denounced "[r]egulatory threats, undue pressure, coercion, and intimidation designed to restrict access to financial services for lawful

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[72] *Id.* at 27–28.

[73] *Id.* at 27.

[74] *Advance Am., Cash Advance Ctrs., Inc. v. FDIC*, 251 F. Supp. 3d 78 (D.D.C. 2017).

[75] Initially the FDIC, Federal Reserve, and OCC were all sued. The claims against the Federal Reserve were dismissed prior to the suit being resolved. Complaint at 1, *Advance Am., Cash Advance Ctrs., Inc. v. FDIC*, 251 F. Supp. 3d 78 (D.D.C. 2017) (No. 1:14-cv-00953).

[76] *Id.* at 14–22.

[77] Letter from Floyd Robinson, Deputy General Counsel, Fed. Deposit Ins. Corp., to David H. Thompson (May 22, 2019), https://www.fdic.gov/news/press-releases/2019/pr19040a.pdf.

businesses."[78] The FDIC also clarified that banks were "neither prohibited nor discouraged" from providing services to lawful customers provided they could manage the risk.[79] The FDIC also announced new training for examiners and a tip line where improper examiner conduct could be reported.[80]

4. Insurance firms have likewise risked sanction if they do not follow agency guidance. In March 2015, for example, the Oklahoma Insurance Commissioner issued a bulletin regarding earthquake insurance.[81] Oklahoma had seen a marked increase in earthquakes that the U.S. Geological Survey, Oklahoma Geological Survey, and others attributed to injection of wastewater as part of oil and gas extraction (i.e., fracking).[82] This is relevant because most earthquake policies sold at the time excluded damage from "man-made" earthquakes.[83]

In that bulletin, the Oklahoma Insurance Commissioner stated that there was "no agreement at

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[78] *Id.*

[79] Statement of the Fed. Deposit Ins. Corp. (May 22, 2019), https://www.fdic.gov/news/press-releases/2019/pr19040a.pdf.

[80] Letter from Jelena McWilliams, Chairman of the Fed. Deposit Ins. Corp., to Rep. Blaine Luetkemeyer (Nov. 15, 2018), https://www.fdic.gov/news/press-releases/2019/pr19040a.pdf.

[81] State of Okla., Okla. Ins. Dep't, John D. Doak, Oklahoma Ins. Comm'r, Earthquake Ins. Bull. No. PC 2015-02, Earthquake Insurance, Excluded Loss, Inspection of Insured Property and Adjuster Training (Mar. 3, 2015), https://www.oid.ok.gov/wp-content/uploads/2019/10/030415_Earthquake-Bulletin-3-3-15.pdf [https://perma.cc/GCX8-J9ZJ] [hereinafter Doak Bulletin].

[82] Mocsary, *supra* note 4, at 10–11.

[83] *Id.* at 11.

a scientific or government level" about whether the quakes were caused by fracking.[84] The bulletin contained no explicitly binding or threatening language, but noted that the Commissioner was concerned that insurance companies might be denying claims on the basis of the "unsupported belief" that the quakes were caused by fracking. The Commissioner said that insurers denying such claims should expect "appropriate action to enforce the law."[85] The bulletin also announced the intention of the Oklahoma Insurance Commissioner's Office to pursue market conduct examinations of insurers to investigate the high rates of coverage denials.[86] The bulletin also restated the duty of the Insurance Commission to determine whether insurers were "employing fair claims practices" and expressed an expectation that adjusters would receive adequate training in claims involving earthquakes.[87]

In the wake of this guidance bulletin, premiums for earthquake insurance increased 260%, deductibles increased, and the number of insurers who offered earthquake insurance declined.[88] This is compelling circumstantial evidence that insurers in Oklahoma believed they had to comply with the thrust of the guidance, which was to avoid excluding coverage, or face regulatory sanction through examination.

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[84] Doak Bulletin, *supra* note 80; Mocsary, *supra* note 4, at 11.

[85] Doak Bulletin, *supra* note 80.

[86] *Id.*

[87] *Id.*; Mocsary, *supra* note 4, at 12.

[88] Mocsary, *supra* note 4, at 12.

Scholars have collected examples like these from across the country—they are hardly limited to New York and Oklahoma.[89]

IV. The Court Should Grant Review of this Important and Recurring Matter.

As demonstrated above, the Second Circuit assumed that firms would not consider themselves bound by guidance or at risk of sanction for noncompliance unless there was some kind of express threat by the regulators. Such an assumption is inconsistent with the nature of banking and insurance regulation, scholarship, and previous, closely analogous examples of regulated entities.

But the decision below is also emblematic of a growing effort by financial regulators to use their awesome powers to effect social change, even at the expense of protected constitutional rights. Financial services are essential to participating in the modern economy, and financial regulators have expansive, opaque power over the firms they regulate. Regulators themselves, those whom they regulate, and the public writ large have recognized that financial regulations can thus be used as a tool to drive broader societal change outside the regular legislative process.[90]

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[89] *Id.* at 9 n.53 (citing examples of insurance regulators pressuring in California, Florida, and nationwide).

[90] Hill, *supra* note 5, at 533 n.49 (discussing how FDIC crackdown on RALs began after consumer advocates sent a letter to FDIC Chairman Shelia Bair calling such loans harmful to consumers); *see also* Jonathan Stempel, *New York Governor Presses Banks, Insurers to Weigh Risk of NRA Ties*, REUTERS

This poses serious questions about the legitimate scope of the power of financial regulators and the interplay between those powers and other important considerations, most especially the constitutional rights of those targeted, or at least disadvantaged, by the actions of those regulators. The legitimate power of a regulator to protect financial safety and soundness[91] should not be used to cause regulated firms to reconsider or subject to extra scrutiny a particular lawful practice or customer relationship. This is especially true where such a move implicates important constitutional rights such as those protected by the First and Second Amendments.

This particular case involving the NYDFS and the NRA is not the first example of regulators potentially abusing their unique positions of power for political, rather than *bona fide* regulatory, purposes and—unless it is curtailed—it will certainly not be the last. The Court should grant review to address this recurring matter of great significance and reverse the decision below.

(Apr. 19, 2018), https://www.reuters.com/article/us-usa-guns-new-york/new-york-governor-presses-banks-insurers-to-weigh-risk-of-nra-ties-idUSKBN1HR04P (quoting Governor Cuomo as saying, "This is not just a matter of reputation, it is a matter of public safety").

[91] How far that power can or should sweep is an important question but outside the scope of this brief.

CONCLUSION

The Court should grant the Petition.

Respectfully submitted,

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