

SCHWARTZ & BALLEN LLP

1990 M STREET, N.W. • SUITE 500

WASHINGTON, DC 20036-3465

(202) 776-0700

FACSIMILE
(202) 776-0720

WWW.SCHWARTZANDBALLEN.COM

MEMORANDUM

May 31, 2007

To Our Clients and Friends

Re: Appellate Decision on Sale of Gift Cards by National Banks and FSBs

The United States Court of Appeals for the First Circuit has upheld the authority of national banks and federal savings associations to use nonbank third parties to market stored value gift cards issued by the institutions without regard to state laws that purport to limit such activities. In SPGGC, LLC; Metabank; U.S. Bank, N.A. v. Ayotte (No. 06-2326), a national bank, federal savings association and third party marketer challenged a New Hampshire law that prohibited the use of expiration dates and certain administrative fees in connection with the sale of stored value gift cards. A lower court had concluded that the New Hampshire law was pre-empted by the National Bank Act and the Home Owners' Loan Act ("HOLA").

PROGRAM DESCRIPTION

Under the program reviewed by the court, the bank and savings association were the issuers of stored value gift cards sold over the Internet and at shopping malls. The cards were sold by a third party marketer, who loaded stored value onto the cards and provided the purchasers with disclosures developed by the banks. The third party received a commission from the banks for each card sold. The cardholder agreement was between the purchaser and the bank that issued the card, and not with the third party marketer. The banks were responsible for servicing the cards and the banks were liable for charges made with the cards. The banks also set the fees associated with the cards. The third party marketer could not alter the terms and conditions of the agreement between cardholders and the banks.

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COURT RULING

The court approached the case as a straightforward case of federal pre-emption. It first determined that national banks may issue and sell stored value gift cards. It also stated that in order to exercise that power effectively, national banks may use third parties to market and sell stored value gift cards. Finally, the court concluded that the New Hampshire law that effectively prohibited a national bank's agent from selling the bank's gift cards "significantly interferes" with the exercise of the bank's powers under the National Bank Act and therefore is pre-empted.

The court applied a similar analysis in reviewing the issues relating to federal savings associations. The court stated that the Office of Thrift Supervision ("OTS") regulation of federal thrifts has been described as "cradle to grave." Noting that the OTS has interpreted its regulations to permit federal associations to issue stored value gift cards, the court concluded that they may also retain third parties to market and sell the cards. Because New Hampshire law indirectly prohibits a federal association from exercising powers granted to it by HOLA and OTS regulations, the court found an "irreconcilable conflict" between state and federal law, and therefore concluded that the state law was pre-empted by HOLA and OTS regulations.

A copy of court's decision can be found on our web site at http://www.schwartzandballen.com/whats_new.html.

If you have any questions, please call Gilbert Schwartz, Robert Ballen, Tom Fox or Heidi Wicker at (202) 776-0700.