Gulf Federal Savings and Loan v. Federal Home Loan Bank Board: A New Judicial Attitude toward the Regulation of Financial Institutions?

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Erratum
The student comment which appeared in Volume 31 at page 233, entitled Gulf Federal Savings And Loan v. Federal Home Loan Bank Board: A New Judicial Attitude Toward The Regulation Of Financial Institutions, was authored by Mary Thorton Horne. Her name was mistakenly omitted.

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INTRODUCTION

Over the past several decades federal regulation of financial institutions has been one of the most striking examples of administrative capacity for complex and exhaustive supervision of a private industry. Congress' broad grants of discretionary power to the banking agencies, combined with judicial reluctance to interfere in the system, have provided the banking agencies with almost unlimited discretion in the promulgation and enforcement of regulations. Although the courts have been criticized for virtually rubber-stamping the agencies' decisions, recognition of four factors has lent respectability to the tradition of very limited review of agency action: (1) maintenance of a sound and viable banking system is of inestimable importance to the government and the public at large; (2) Congress cannot feasibly provide for all possible threats to sound and ethical banking in a statute; (3) the federal banking agencies have experience and expertise in what has become a highly technical field; and (4) it is clearly desirable that the banking laws be applied with as much uniformity as possible.²

In a recent decision, however, the Fifth Circuit moved to curtail the wide discretion traditionally granted the banking agencies. In Gulf Federal Savings and Loan Association v. Federal Home Loan Bank Board,³ the court overturned a cease and desist order issued by the Federal Home Loan Bank Board which required the petitioning savings and loan to cease calculating interest in violation of its loan contracts and to reimburse borrowers for excess interest charges resulting from the erroneous calculations. The deci-

2. See generally infra notes 46-57 & 76-85 and accompanying text.
sion, which rejected both the Bank Board's exercise and interpretation of its cease and desist authority, has drawn the protest of all the federal banking agencies.

In the wake of current legislative efforts to deregulate financial institutions, the implications of the Gulf Federal decision may reach beyond the immediate limitation of the Bank Board's discretion. Recognition in the banking industry of the deference paid to the banking agencies by the courts has in the past allowed the regulatory agencies to discourage unsound and unethical practices quickly and informally without litigation. By substituting its discretion for that of the Bank Board, the Gulf Federal court has issued an invitation for frequent court challenges to agency supervision and may have destroyed the informal, non-coercive relationship that federal banking agencies have enjoyed with their charges. Thus, while several congressmen and the banking agencies struggle to produce a formula to revitalize the banking industry, and especially the troubled savings and loan system, the Gulf Federal court may have signaled the industry to facilitate its own deregulation by testing the legitimacy of previously unconsidered practices in the courts.4

This Comment will explore the traditionally wide discretion given the banking agencies, the sound reasons supporting the traditional attitude, and the areas in which the Gulf Federal decision departs from this reasoning. The first section will present the facts and reasoning of Gulf Federal. The second section will discuss the cease and desist authority of the federal banking agencies and the exceptionally broad discretion that has been given these agencies in defining "unsafe and unsound practices," the criteria

4. Although this Comment is critical of the Gulf Federal court, it should be noted that the Bank Board failed to brief the court on recent caselaw from within the Fifth Circuit supporting its position. While there were several relevant decisions handed down by the Fifth Circuit in the five years preceding Gulf Federal, see infra notes 52 & 84 and accompanying text, the Bank Board's briefs mention only one of these recent cases, without providing discussion. See Brief in Support of Proposed Findings of Fact, Conclusions of Law and Recommended Order, In re Gulf Fed. Sav. & Loan Ass'n of Jefferson Parish, Fed. Home Loan Bank Bd. Resolution No. 77-171, Gulf Fed. Sav. & Loan Ass'n v. FHLBB, 651 F.2d 259 (5th Cir. 1981) [hereinafter cited as Respondent's Brief]; Supplemental Brief in Reply for Respondent Fed. Home Loan Bank Bd., Gulf Fed. Sav. & Loan Ass'n v. FHLBB, 651 F.2d 259 (5th Cir. 1981) [hereinafter cited as Supplemental Brief]. On its petition for rehearing en banc, however, the FHLBB presented Fifth Circuit caselaw in much greater detail. See Petition for Rehearing en banc, Gulf Fed. Sav. & Loan Ass'n v. FHLBB, 651 F.2d 259 (5th Cir. 1981) [hereinafter cited as Petition for Rehearing].
for exercise of the cease and desist authority. The third section will discuss the appropriate standards of review of agency action in general and of banking agency action in particular. The final section will discuss possible implications of the Gulf Federal decision.

I. Gulf Federal Savings and Loan v. Federal Home Loan Bank Board

A. Regulatory Context of Gulf Federal

The Federal Home Loan Bank Board was created by Congress in 1932 to provide a reliable source of long term credit for homeowners, primarily in response to the financial crisis of the late 1920s and the 1930s. The current regulatory structure of the Board was created in 1933 with the enactment of the Home Owner's Loan Act (HOLA). The HOLA authorized the Board to issue rules and regulations for "the organization, incorporation, examination, operation, and regulation of associations to be known as 'Federal Savings and Loan Associations' . . . and to issue charters therefor, giving primary consideration to the best practices of local mutual thrift and home-financing institutions in the United States." The express purpose of the Act was "to provide local mutual thrift institutions in which people may invest their funds and . . . to provide for the financing of homes." All federal savings and loans are required by the HOLA to become members of a Federal Home Loan Bank. Following enactment of the HOLA, the Federal Savings and Loan Insurance Corporation was created by the National Housing Act to provide insurance for federal savings and loans and other qualified institutions similar to that provided for commercial banks by the Federal Deposit Insurance Corporation (FDIC).

Prior to 1966 the Bank Board's only enforcement mechanisms were its powers to terminate an association's insurance or to appoint a receiver. Congress added the Board's authority to issue

6. See 75 Cong. Rec. 12,606, 12,627, 12,721, 14,452, 14,590, 14,593 (1932).
9. Id.
12. 12 U.S.C. § 1426(i) (1976); See also S. Rep. No. 1482, 89th Cong., 2d Sess. 4-6,
cease and desist orders to the HOLA in 1966 to provide a flexible, intermediate sanction. The Board's cease and desist authority allows it to issue a cease and desist order following notice of charges and a hearing upon the charges, where it is determined at the hearing (1) that a savings and loan association is violating, has violated or is about to violate a law, rule, regulation, or other condition imposed in writing by the Board, or (2) that the association is engaging, has engaged, or is about to engage in an unsafe or unsound practice. The order may require the association to refrain from the violation or practice and require affirmative action to correct conditions resulting from the violation or practice. A savings and loan association with respect to which a cease and desist order is issued is entitled to petition for review of the order in a federal court of appeals.

B. Gulf Federal

The petitioning savings and loan association in Gulf Federal sought review of a Bank Board order requiring it to cease and desist from calculating interest in a manner contrary to the terms of its mortgage agreements and to reimburse borrowers for overpayments of interest resulting from the erroneous calculations. In June of 1969, pursuant to a resolution by its Board of Directors, Gulf Federal Savings and Loan Association replaced provisions in its mortgage agreements calling for interest to be calculated according to 360 day interest tables with provisions calling for calculation according to 365 day tables. The 365 day tables were never used in practice and the Board of Directors reversed itself and reinstated use of 360 day tables in October, but Gulf Federal inadvertently continued to use loan agreements providing for use of 365 day tables until February 1973. As a result, interest on 444 loans was calculated according to an interest schedule different from that expressly contained in the loan contracts and 444 bor-

reprinted in 1966 U.S. CODE CONG. & AD. NEWS 3532, 3536-38 [hereinafter cited as S. REP. No. 1482].
15. Id.
rowers were charged an additional five days interest per year.\textsuperscript{18}

In March of 1977, the Bank Board issued a Notice of Charges and Hearing against Gulf Federal. The notice alleged that the association was breaching the interest calculation provisions of 444 loan contracts, and that the breaches constituted an unsafe and unsound practice within the meaning of the HOLA and were violations of federal common law and the “sound and economical home financing” provisions of the Bank Act.\textsuperscript{19} Gulf Federal’s answer admitted to charging interest in violation of the contractual provisions in question, but denied that the violation was a breach of contract or an unsafe or unsound practice. The association also affirmatively asserted that the Bank Board lacked authority to bring the cease and desist action.\textsuperscript{20} Following an administrative hearing, however, an administrative law judge recommended that the Bank Board issue a cease and desist order requiring Gulf Federal to refrain from calculating interest in violation of its contracts and to repay overcharged interest to the 444 borrowers issued “365 day” contracts.\textsuperscript{21} The full Board issued the order and based its authority on its determination that, as alleged in the Notice of Charges, Gulf Federal was breaching its loan contracts and this breach constituted an “unsafe or unsound practice” and was a violation of federal common law and the Bank Act.\textsuperscript{22}

Gulf Federal petitioned the Fifth Circuit Court of Appeals for review of the order, claiming, \textit{inter alia}, that the Bank Board had exceeded its cease and desist authority in an attempt to engage in consumer protection. The Board’s function, it argued, is to protect

\textsuperscript{18} Id. at 261-62; Respondent’s Brief, supra note 4, at 2-6.


\textbf{[T]he Board may, after hearing, remove any member from membership . . .

if, in the opinion of the Board, such member . . . (iii) has a management or home financing policy inconsistent with sound and economical home financing.}

\textsuperscript{20} Petition for Rehearing, supra note 4, at 3. Gulf Federal argued that the term “unsafe and unsound practices” referred solely to practices which threaten the financial stability of the institution. Respondent’s Brief, supra note 4, at 10. The Bank apparently based its claim that it was not breaching the loan contracts on the fact that its continued use of the 365 day contracts was a mistake. \textit{Id.} at 6.

\textsuperscript{21} Petition for Rehearing, supra note 4, at 3.

\textsuperscript{22} Id. at 3-4.
the financial stability of savings and loan associations, not to pro-
tect consumers. In particular, Gulf Federal urged that the phrase "unsafe and unsound practices" referred only to "those practices that threaten the financial stability of insured institutions" and as-
serted that the Bank Board's order, not the disputed contracts, threatened its financial stability.

The Bank Board responded that the order was a proper exer-
cise of its statutory authority, maintaining that its regulatory re-
sponsibility extended to all aspects of federal savings and loans' operations. The Board denied that its cease and desist authority based on the "unsafe and unsound" provision was limited to erad-
cating practices which jeopardized financial stability, but neverthe-
less argued that Gulf Federal's overcharge practice "created an ab-
normal risk of loss or damage" to the association and was "contrary to generally accepted standards of prudent lend-
ing." The overcharge practice, the Board argued, created potential lia-
ibility on Gulf Federal's part for the overcharged interest and puni-
tive damages, and jeopardized the integrity and community stand-
ing of the association and other savings and loan associations in
the area.

Upon review of the order, the Gulf Federal court reversed the
Board's decision, holding that there was no statutory authority for
the order. In support of its decision the court referred to the legis-
lative history of the Bank Board's cease and desist authority and
noted the fears expressed by several members of Congress during
debate that the statute, and the "unsafe and unsound" practice
formula in particular, was too vague and delegated unlimited au-
thority to the banking agencies. Citing reassurances from support-
ers of the bill in response to these fears, the court concluded that it
was the intent of Congress that the "unsafe and unsound" practice
formula be restricted to practices which "threaten the financial in-
tegrity of the association." The argument that authority to inter-

23. Gulf Federal, 651 F.2d at 263.
24. Id. at 261-62; Respondent's Brief, supra note 4, at 10, 35.
25. Respondent's Brief, supra note 4, at 10.
26. 651 F.2d at 262.
27. Respondent's Brief, supra note 4, at 7, 15.
28. 651 F.2d at 264. In particular, the court notes the following statement by Congress-
man Patman, the sponsor of the bill:

[O]f course, it should be clear to all that the cease-and-desist powers and man-
agement removal powers are aimed specifically at actions impairing the safety or
vene was present in the instant case due to the risk of potential liability was rejected on the ground that liability would become immediate were the Bank Board's order upheld. The loss of public confidence rationale for Bank Board intervention was rejected because the court feared it would result in open-ended supervision of savings and loans. The court concluded: "If the Board can act to enforce the public's standard of fairness in interpreting contracts, the Board becomes the monitor of every activity of the association in its role of proctor for public opinion. This departs entirely from the congressional concept of acting to preserve the financial integrity of its members."  

The court also suggested that cease and desist authority founded on a violation of law might similarly be restricted to violations threatening the financial stability of the institution, but the issue was not resolved as no violations were found. Further, the court rejected the Bank Board's argument that Gulf Federal's violation of its loan agreements was inconsistent with the "sound and economical home-financing" required of federal savings and loan associations by the Bank Act and concluded that there was no violation of this provision. The court reasoned that the "sound and

soundness of our insured financial institutions. These new flexible tools relate strictly to the insurance risk and to assure [sic] the public sound banking facilities.

Id.
29. 651 F.2d at 264-67.
30. Id. at 264-65.
31. 651 F.2d at 265-66. The court also held that federal law governs only the internal management of federal savings and loan institutions and does not apply to contractual agreements between the petitioner and its borrowers which were made under Louisiana law. Id. at 266. The Supreme Court, citing Gulf Federal, recently criticized the internal/external distinction as without support in the language of the HOLA or its legislative history. Fidelity Fed. Sav. & Loan Ass'n v. De La Cuesta, _U.S_, 102 S. Ct. 3014, 3031 n.23 (1982).

The Gulf Federal court found no violation of Louisiana contract law as it determined that the loan agreements calling for interest calculation according to 365 day tables also included a statement of the amount of each payment to be made by borrowers calculated under 360 day tables. The court held that Louisiana law required conflicting contractual provisions to be construed to effect the probable intent of the contracting parties. 651 F.2d at 267. The court either did not accept or failed to notice the Bank Board's findings that the petitioner's agreements stated the proper amount of payment as calculated under 360 day tables and that the 360 day calculations only appeared in the amortization of the mortgages on petitioner's books. Petition for Rehearing, supra note 4, at 16. Cf. La. Civ. Code art. 1957 (West 1977) (ambiguous contracts are construed against the party who drafted the contract). See also Rayford v. Louisiana Sav. Ass'n, 380 S.2d 1232, 1238 (La. Ct. App. 1980).
economical home financing" provision established criteria for membership in the federal savings and loan system and did not specify a standard of conduct capable of violation. The court did not specifically address the Board’s argument that, as it was expressly authorized to terminate an association’s membership where the association’s policies were inconsistent with “sound and economical home financing,” it should certainly be deemed to possess the discretion to rely on an intermediate remedy, the cease and desist order, to correct these policies where possible. The court did, however, conclude that the “sound and economical home financing” provision was, like the “unsafe and unsound” provision, addressed to policies that might “lead to future insolvency,” not to policies deemed unfair or usurious by the Bank Board.

II. UNSAFE AND UNSOUND PRACTICES

Congress has never defined “unsafe and unsound practices,” yet the formula appears in nearly every enforcement device available to the banking agencies. In the event of “unsafe or unsound practices,” the agencies are authorized to issue cease and desist orders, remove or suspend officers and directors, impose civil sanctions, and terminate insurance. The existence of the “unsafe and unsound practices” formula in the statutory authorization for so many enforcement devices, combined with the discretion granted the agencies by the courts, has permitted the agencies to select from a variety of enforcement devices to correct imprudent practices, enhancing the flexibility and efficiency of the regulatory scheme.

The Gulf Federal court, however, treated Congress’ abstention from definition of the formula as if it were an oversight, although the legislative history of the Bank Board’s cease and desist authority belies this conclusion. Quoting remarks made during House debate by Congressman Patman, the sponsor of the bill, the court suggests that Congress believed that the unsafe and unsound prac-

33. 651 F.2d at 265.
34. Respondent’s Brief, supra note 4, at 19.
35. 651 F.2d at 265-66.
tice formula was exact and clearly restricted to practices posing a
direct threat to an insured institution's financial stability. In ad-
dition, the court placed particular reliance on a memorandum on
the meaning of "unsafe and unsound practices" submitted by John
Horne, then Chairman of the Bank Board, and adopted by both
Houses in their records. Chairman Horne's memorandum sug-
gested an often quoted guideline for identifying "unsafe and un-
sound practices" which holds that "unsafe and unsound practices"
are those which are "contrary to generally accepted standards of
prudent operation, the possible consequences of which, if contin-
ued, would be abnormal risk or loss or damage to an institu-
tion. . . ." The court asserted that this guideline is the "authori-
tative definition" of "unsafe and unsound practices." In addition,
the court noted several examples of "unsafe and unsound" prac-
tices listed by Chairman Horne, all involving imprudent loans or
other outlay of capital, to support its limitation of the "unsafe and
unsound" formula to practices threatening the financial stability of
the association.

The court, however, failed to mention a warning issued by
Chairman Horne just prior to the excerpted portions of his memo-
randum. Chairman Horne stated that the concept of "unsafe and
unsound practices" extended to every aspect of a financial institu-
tion's operation and consequently eluded definition. He warned
that any attempt to impose a definition on the formula would work
to exclude practices not encompassed in the definition which may
nevertheless be injurious to the institution in light of the factual
circumstances. The court failed to heed Chairman Horne's advice

40. See supra note 28.
41. 651 F.2d at 264. See also 112 Cong. Rec. 24,984 (1966) (House); id. at 26,474 (Sen-
ate). The full text of the portion of Chairman Horne's memorandum that was excerpted by
the court is as follows:

Generally speaking, an "unsafe or unsound practice" embraces any action, or
lack of action, which is contrary to generally accepted standards of prudent op-
eration, the possible consequences of which, if continued, would be abnormal
risk or loss or damage to an institution, its shareholders, or the agencies ad-
ministering the insurance funds.

42. Id.
43. 651 F.2d at 264.
45. Id.
46. The full text reads:
although it deemed his memorandum an authoritative indication of congressional intent.

This imposition of a restriction upon the "unsafe and unsound" formula thwarts Congress' deliberate abstention from restriction. Moreover, the limitations imposed by the court severely frustrate the aim of the authors of the bill to provide a flexible, discretionary enforcement mechanism. In suggesting that the "Congressional concept" of cease and desist orders was "action to prevent financial collapse," the court overlooked the frequently stated understanding of Congressman Patman and other authors of the bill that the cease and desist power would provide the Board with an intermediate remedy to complement the breadth and discretion of the regulatory power necessary to ensure a system of sound and economical home financing. The express purpose of the statute was to provide a remedy suitable for less than drastic situations. The legislative history demonstrates that the concept of cease and desist authority was meant to include effective au-

The concept of 'unsafe or unsound practices' is one of general application which touches upon the entire field of the operations of a financial institution. For this reason, it would be virtually impossible to attempt to catalog within a single all inclusive or rigid definition the broad spectrum of activities which are embraced by the term. The formulation of such a definition would probably operate to exclude those practices not set out in the definition, even though they might be highly injurious to an institution under a given set of facts or circumstances or a scheme [sic] developed by unscrupulous operators to avoid the reach of the law. Contributing to the difficulty of framing a comprehensive definition is the fact that particular activity not necessarily unsafe or unsound in every instance may be so when considered in the light of all relevant facts.

Id.

47. Id.

48. E.g., during House debate, Congressman Patman stated that the cease and desist authority:

[i]s needed, not for the benefit of the Federal supervisory agencies, but for the millions of depositers who have their checking accounts and personal savings in these institutions. Of course, the benefits of improved supervision accrue not merely to those persons whose accounts are insured, but to everyone who is a depositer or creditor of these institutions. And, let us not forget the millions of borrowers who depend on these institutions for their business needs and their personal needs such as consumer goods and home financing. So, it is not that we feel that Government officials should have more authority because this bill does not give them expanded authority since nothing could exceed their present power to terminate insurance. The cease and desist power and the very limited officer removal power represent flexible, intermediate supervisory tools to be used short of the last resort of insurance termination.

Id. at 24,984.
authority to make viable the goals of the founders of the Bank Board—to provide a reliable source of credit for homowners. The broad statutory mandate given the Bank Board, i.e., promoting "the best practices of local mutual thrift and home financing institutions," requires attention to every detail of the operation of federal savings and loan associations. The authors of the bill creating the Bank Board's cease and desist authority intended that authority to be co-extensive with the statutory duties of the Bank Board. They also believed that the situations calling for exercise of cease and desist authority could not be defined without reference to particular circumstances and that such definition was best entrusted to those in close contact with these circumstances and familiar with the regulatory scheme.

In previous decisions, the Fifth Circuit has noted the intention of Congress that the banking agencies’ cease and desist authority be of a flexible, discretionary character. Emphasis has been placed on the interpretive discretion accorded the regulatory agencies, as in the leading case of Groos National Bank v. Comptroller of the Currency. The Groos National court rejected the petitioner's argument that the phrase "unsafe and unsound," lacking definite meaning, could not be used to deprive it of rights, stating:

The phrase 'unsafe or unsound banking practice' is widely used in the regulatory statutes and in case law, and one of the purposes of the banking acts is clearly to commit the progressive definition and eradication of such


50. See Independent Bankers Ass'n of Am. v. Herman, 613 F.2d 1164, 1168-69 (D.C. Cir. 1979); Reich v. Webb, 336 F.2d 153 (9th Cir. 1964). In Reich, the Court of Appeals for the Ninth Circuit rejected the contention that the Bank Board did not have the authority under the HOLA to enforce common law fiduciary duties. The court reasoned:

Construing the statute as a whole and in light of its purpose . . . it is manifest that Congress envisioned a strong Bank Board with broad regulatory power to redeem and make viable the initial condition of charter issuance that primary consideration [be given] to the best practices of local mutual thrift and home financing institutions in the United States.

336 F.2d at 157-58 (citations omitted).


52. Id. at 26,474 (Horne memorandum).

53. See cases discussed infra notes 54-60 and accompanying text. The fact that the prior Fifth Circuit cases were decided by different panels than that which decided the Gulf Federal case is noteworthy.

54. 573 F.2d 889 (6th Cir. 1978).
practices to the expertise of the appropriate regulatory agencies.\textsuperscript{55}

Quoting this language from \textit{Groos National}, the Fifth Circuit in \textit{First National Bank of Lamarque v. Smith} refused to grant declaratory judgment for a petitioner who challenged the Comptroller of the Currency's authority to issue letters identifying the receipt by bank insiders of commissions from the sale of credit life insurance as an unsafe and unsound practice.\textsuperscript{56}

The comptroller's interpretive discretion was also emphasized in \textit{Independent Bankers Association of America v. Heimann}, where petitioners sought to enjoin the Office of the Comptroller from enforcing a regulation prohibiting insiders from benefiting from the sale of insurance.\textsuperscript{57} Upholding the comptroller's authority, the court expressed the traditional judicial attitude towards the banking agencies' enforcement authority:

National banks are perhaps as meticulously regulated as any industry. Every aspect of their affairs is scrutinized to assure financial soundness and ethical practice. The Comptroller's statutory duties require the closest monitoring and continuous supervision of these institutions. Thus the Comptroller's discretionary authority to define and eliminate "unsafe and unsound" conduct is to be liberally construed.\textsuperscript{58}

The \textit{Gulf Federal} court ignored the tradition of liberal construction of the banking agencies' authority to characterize "unsafe and unsound practices" established by these decisions, as well as the discretion intentionally vested in the agencies by Congress. Arguably these previous decisions upheld action to eliminate threats to financial stability,\textsuperscript{59} but in \textit{Gulf Federal} the court made no attempt to distinguish the precedent it ignored. The court did, however, implicitly acknowledge that within the sphere of activity directly affecting the financial condition of federal savings and loans, the Board's authority is discretionary.\textsuperscript{60} The court repeatedly sug-

\textsuperscript{55} Id. at 897.

\textsuperscript{56} 610 F.2d 1258, 1265 (5th Cir. 1980).

\textsuperscript{57} 613 F.2d 1164 (D.C. Cir. 1979).

\textsuperscript{58} Id. at 1168-69.

\textsuperscript{59} \text{The petitioner in \textit{Groos Nat'l} was ordered to cease extending high risk credit to its controlling shareholder and his relatives and associates. In \textit{Independent Bankers Ass'n and First Nat'l Bank of Lamarque}, the comptroller's letter and regulation were aimed at receipt of commissions by bank insiders from the sale of credit life insurance which may encourage extension of high risk credit. Thus, all three of these cease and desist orders may fall within the \textit{Gulf Federal} court's threat to financial stability test.}

\textsuperscript{60} \text{See 651 F.2d at 264-65. The court further states:}
gested that it accepted the petitioner's argument that the regulatory power and responsibility of the Bank Board is confined to guaranteeing the financial stability of savings and loans and does not extend to consumer protection. Arguably, therefore, the court did not usurp the Bank Board's discretionary authority to define "unsafe and unsound practices," but merely confined it to "the Board's traditional sphere of activity" (i.e., protecting the government's interest as an insurer).

Even this position, however, ignores clear evidence that Congress expects the Bank Board to play a role in ensuring the consumer and the community of the integrity of federal savings and loans and, where necessary, to use its cease and desist power to do so. The Bank Board is charged with responsibility for enforcing the Truth in Lending Act, Home Mortgage Disclosure Act, Community Reinvestment Act, and other consumer and community oriented laws as they apply to federal savings and loans and is consequently responsible for including an assessment of an institution's compliance with those laws in its periodic examinations of the institution. In many cases the Bank Board is explicitly directed to use its cease and desist power to correct violations of these statutes. Thus Congress contemplated that the Bank Board's regulatory activity in general, and its cease and desist power in particular, should, when appropriate, encompass consumer protection. Indeed, it would be quite an anomalous situation if the Bank Board were charged with responsibility for enforcing these statutes but could not use its only intermediate sanction, the cease and desist order, to enforce them and was forced to resort to

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61. See supra notes 24-25 and accompanying text.
62. 651 F.2d at 262 (petitioner's argument).
termination of insurance or appointment of a receiver.  

Recent congressional discussion regarding amendments to the Federal Trade Commission Act (FTCA) even further undermines the court's position that the Bank Board's cease and desist authority is restricted to actions having a direct effect on the financial stability of insured institutions. The amendments, intended to eliminate duplicative regulation of savings and loans, exempted savings and loan associations from the scope of the FTCA on the grounds that the Bank Board had "the necessary regulatory tools to protect consumers from unfair or deceptive acts or practices by savings and loan associations." The House committee, in fact, included a letter from the Chairman of the Federal Home Loan Bank Board discussing the Gulf Federal cease and desist order in its report on the amendments. The letter states:

The interest of the Bank Board in policing unfair or deceptive trade practices is indicated by a cease and desist order it issued this past year which required restitution by an S. & L. to mortgagors of over-payments in interest, where the particular method used for computing interest (a 360 day year) was clearly legally permissible and in fact the dominant method used in the State, but the S. & L.'s form instruments indicated a 365 day schedule.

Congress has thus implicitly endorsed the consumer protection efforts of the Bank Board as well as the cease and desist order issued to Gulf Federal. Clearly the intent of Congress and the traditional position of the courts has been that it is within the authority of the Bank Board to guarantee not only the financial stability of federal savings and loans but also the integrity of these institutions as a reliable source of credit for homeowners.

III. Judicial Review of Agency Action

As discussed above, the Gulf Federal decision is disconcerting in that it fails to acknowledge congressional and judicial interpretation of the Bank Board's enforcement authority. Even broader in its implications for the future, however, is the fact that the court ignored voluminous precedent and statutory mandate in refusing to apply the traditional standards of review of agency action. The


71. Id. at 376-77.
court supported its refusal to apply the traditional deferential standards of review by arguing that the boundaries of the Board's cease and desist authority were at issue in *Gulf Federal* and that definition of these boundaries required judicial and not administrative expertise.\textsuperscript{72}

Review of all administrative action has been limited by two controlling maxims of judicial review: (1) courts will not substitute their judgment for that of the agency;\textsuperscript{73} and (2) great deference is given to an administrative agency's interpretation of its enabling statutes.\textsuperscript{74} These maxims require that courts uphold an interpretation of a statute by the agency charged with its enforcement where reasonable, even if the interpretation is not the only reasonable one, or even, in the opinion of the court, the most reasonable.\textsuperscript{75} The tradition of deference to an agency's construction of its enabling statutes rests on respect for the expertise of administrative agencies in often highly technical fields and recognition of congressional intent to entrust the task of uniform statutory enforcement to the agencies.\textsuperscript{76}

In many cases, the complexity of financial institution regulation has promoted especially strict adherence to the principle of deference to an agency's expertise.\textsuperscript{77} Neither the courts nor Con-

\textsuperscript{72} 651 F.2d at 263.


\textsuperscript{77} The Fifth Circuit, in Philbeck v. Timmers Chevrolet, Inc., 499 F.2d 971 (5th Cir. 1974), articulated the reasons for deference to agency interpretation when it upheld the Federal Reserve's interpretation of a regulation, promulgated under the Truth in Lending Act, stating that the Federal Reserve Board's interpretations "are entitled to great weight, for they constitute part of the body of informed experience and judgment of the agency to whom Congress delegated appropriate authority." *Id.* at 976. Notably the Fifth Circuit also
gress are capable of staying abreast of the multitude of factors that work to keep the banking system running smoothly. Mr. Justice Rutledge expressed this view eloquently in his concurring opinion in Federal Research System v. Agnew, where the Supreme Court upheld the Federal Reserve's removal of national bank directors for violation of the Banking Act. Regarding the Federal Reserve Board of Governor's, Mr. Justice Rutledge stated:

Not only because Congress has committed the system's operation to their hands, but also because the system itself is a highly specialized and technical one, requiring expert and coordinated management in all its phases, I think their judgment should be conclusive upon any matter which, like this one, is open to reasonable difference of opinion. Their specialized experience gives them an advantage judges cannot possibly have, not only in dealing with the problems raised for their discretion by the system's working, but also in ascertaining the meaning Congress had in mind in prescribing the standards by which they should administer it.

The Gulf Federal court, however, determined that judicial expertise was better suited to interpreting the meaning of "unsafe and unsound practices" and "policy . . . inconsistent with sound and economical home financing" than was the expertise of the Bank Board. The distinction noted above upon which the court apparently rests this determination (i.e., that between judicial determination of the statutory boundaries of agency authority and ordinary review of an agency's decisions) is ill-founded on two grounds. First, the tradition of deference to agencies' views has been followed in review of all types of administrative action, and often precisely where that agency action has been challenged, as in Gulf Federal, on the grounds that it exceeds the statutory author-

expressed this view, subsequent to its decision in Gulf Federal, in Till v. Unifirst Fed. Sav. & Loan Ass'n, 653 F.2d 152 (5th Cir. 1981), where it stated: "[I]n matters of statutory interpretation, courts should be attentive to the views of the administrative entity appointed to apply and enforce a statute." Id. at 160. The Unifirst Federal panel was composed of different judges than the Gulf Federal panel. See also Ford Motor Credit Co. v. Milhollin, 444 U.S. 555, 559 (1980); Mourning v. Family Publications Serv., Inc., 411 U.S. 356 (1973); First Bank of La Marque v. Smith, 610 F.2d 1258 (5th Cir. 1980); Groos Nat'l Bank v. Comptroller of the Currency, 573 F.2d 889 (5th Cir. 1978).

79. 329 U.S. 441 (1947).
80. Id. at 450.
81. See infra note 97 and accompanying text.
Considerations of agency expertise are every bit as viable when the question is whether governmental interference is necessary to maintain the statutory scheme as they are when the question is factual. This is particularly true of banking agency decisions, as the concept of sound banking cannot be applied in the abstract. Determination of when interference is necessary requires knowledge of the condition of individual banks, the communities they serve, the people they employ, and various other factors, as well as familiarity with the workings of the technically complex system of regulations governing the banking system and the type of activity that, although not specifically proscribed, could work to undermine the regulatory structure.

The second difficulty with the court's distinction between determining the bounds of agency authority and general review of agency action is that the distinction between the bounds of statutory authority and the areas of decisionmaking committed to agency expertise is not valid in regard to the Bank Board's cease and desist authority. Because "unsafe and unsound practices" and "violation of law" are not defined in the statute, each exercise of cease and desist authority will necessarily identify a particular activity as an "unsafe or unsound practice" or a "violation of law."

The Bank Board defines the bounds of its cease and desist authority by its determination that some particular activity jeopardizes the safety or soundness of the institution or institutions involved, or violates some aspect of the regulatory scheme or law. Recognition of the fact that rulemaking is contemporaneous with enforcement of the statutory mandate of the banking agencies is at the core of the courts' traditionally exceptional deference to their decisions.


83. See generally cases cited supra note 82.

84. See generally Ford Motor Credit Co., 444 U.S. at 559-60; Agnew, 329 U.S. at 450 (Rutledge, J., concurring); Reich, 336 F.2d at 158. See also 112 Cong. Rec. 26,474 (1966).

85. See Independent Bankers Ass'n, 613 F.2d at 1168-69.

86. See Groos Nat'l Bank v. Comptroller of the Currency, 573 F.2d 889 (5th Cir. 1978);
The *Gulf Federal* decision, however, failed to recognize that the enforcement power of the banking agencies is necessarily discretionary. The court would limit the Bank Board's cease and desist power to practices which directly threaten the government's insurance interest and, more importantly, would appropriate for the courts the power to identify practices which threaten this interest. The court not only rejected the agency's interpretation of its enabling statute, but rejected the Bank Board's determination that Gulf Federal's violation of its loan contracts fell within the court's interpretation of the statute. Furthermore, the court rejected this primarily factual determination without reference to any standard of review traditionally applied to agency determinations.

In addition to the respect due an agency's interpretation of its enabling statutes under the maxims discussed above, supplementary guidelines for judicial review of administrative action are codified in the Administrative Procedure Act (APA), which delineates different levels of review varying with the nature of the activity challenged.⁸⁷ Review of cease and desist orders and other agency action based on adjudicatory or fact-finding proceedings is limited by the APA to determination that the action or decision is or is not supported by substantial evidence.⁸⁸ The Supreme Court gave the authoritative definition of "substantial evidence" in *Consolo v. Federal Maritime Commission.*⁹⁰ Holding that "substantial evidence" is such evidence as a reasonable mind would find satisfactory to support the conclusion,⁹₀ the Court stated: "This is something less than the weight of the evidence, and the possibility of

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drawing two inconsistent conclusions from the evidence does not prevent an administrative agency's finding from being supported by substantial evidence."  

The original Senate bill creating the cease and desist authority of the financial regulatory agencies stipulated that cease and desist orders should be reviewed under the stricter "weight of the evidence" rule rather than the "substantial evidence" rule which would apply absent a provision to the contrary. This stipulation was made in response to fears expressed by members of the banking industry that the statute would subject them to the arbitrary dictates of bureaucrats which would not be adequately reviewed under the substantial evidence standard. The House, however, deleted the weight of the evidence rule from the bill and, after conference, the Senate conferees reported to the full Senate that the industry's fears were unfounded.

Congress thus expressly mandated that the banking agencies' cease and desist authority be reviewed under the substantial evidence standard. This standard is especially appropriate to the type of flexible enforcement tool Congress envisioned when it created the cease and desist authority. It reduces the incentive for dilatory litigation and the potential for judicial imposition of criteria for exercise of administrative authority. The Supreme Court summarized these advantages in Consolo stating:

Congress was very deliberate in adopting this standard of review. It frees the reviewing courts of the time consuming and difficult task of weighing the evidence, it gives proper respect to the expertise of the administrative tribunal and it helps promote the uniform application of the statute. . . . [A]gency determinations frequently rest upon a complex and hard-to-review mix of considerations. . . . [C]ongress places a premium upon agency expertise, and, for the sake of uniformity, it is usually better to minimize the opportunity for reviewing courts to substitute their discretion for that of the agency.

In Gulf Federal, review under the substantial evidence test would have required the court to set aside the Bank Board's cease

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91. 383 U.S. at 620.
92. 112 Cong. Rec. 26,473 (1966). The "weight of the evidence" rule holds that the agency's fact findings must be supported "by the preponderance or greater weight of the evidence." See G. H. Miller & Co. v. United States, 260 F.2d 286, 288 (7th Cir. 1958).
94. Id.
95. See infra text accompanying note 96.
96. 383 U.S. at 620-21.
and desist order only if it could not reasonably be concluded from the factual findings of the Board that petitioner's deviation from the provision of its loan agreements was an "unsafe or unsound" practice or inconsistent with "sound and economical home financing." Even if the court were correct in interpreting the statute as granting authority only to prevent practices which threaten the integrity of federal savings and loans, it ought not to have set aside the cease and desist order unless the Bank Board's conclusion that Gulf Federal's financial integrity was threatened by potential liability stemming from the overcharging practice was insupportable. This approach was followed by the Fifth Circuit three years earlier in Groos National Bank v. Comptroller of the Currency where, affirming a cease and desist order issued by the Comptroller of the Currency, it held that there was substantial evidence to support the comptroller's finding that the petitioning bank's extension of high risk credit to its controlling shareholder and his family was an "unsafe and unsound" banking practice. 9

The Gulf Federal court, however, makes no reference to the "substantial evidence" standard ignoring statutory and precedential authority. These standards of review are based on sound policy considerations. Deference to the Bank Board's expertise may, in a particular case, yield distasteful results, but as a principle of judicial review it relieves the courts of having to familiarize themselves with the many considerations which may enter into regulatory decisions in this highly technical field and permits uniform regulation by the experts to whom Congress has assigned the task.

IV. IMPLICATIONS OF GULF FEDERAL

Under any circumstances the Gulf Federal court's cavalier attitude toward the Bank Board's authority would be disturbing. The current precarious condition of the savings and loan industry renders the court's decision doubly imprudent. While the Bank Board, the FDIC, and several congressmen are struggling to rescue the industry from bankruptcy, the Gulf Federal court has moved to weaken the authority of the Bank Board in a decision which implicitly endorses what is at least an unethical practice.

The immediate effect of the Gulf Federal decision is to weaken the congressionally contemplated and judicially affirmed

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97. 573 F.2d at 897.
scheme of Bank Board supervision of the most detailed aspects of savings and loan operation. The long term effects of the Gulf Federal decision are as yet unclear. The decision may drastically alter the effectiveness and efficiency of the financial institution regulatory structure if it is perceived as an indication that the courts have decided to facilitate deregulation of the financial industry on their own. The tacit recognition within the industry that the banking agencies prevail in court has induced quick and uncoerced compliance with agency recommendations in the past. If the Gulf Federal decision is accepted, regulated institutions may seek to challenge the agencies' discretion in court on a regular basis. The damage that may result from costly and dilatory litigation over agency action is unpredictable. However, it is doubtful that the troubled savings and loan industry will wait for legislative deregulation to test the legitimacy of previously unconsidered practices if Gulf Federal is perceived as a shift in judicial attitude towards banking agency discretion. As a consequence, the over-extended resources of both the federal government and the savings and loan industry may be further depleted and the current efforts of the Bank Board and the FDIC to solve the industry's problems may be impeded and delayed.

CONCLUSION

The Gulf Federal decision is an ill-timed departure from traditional judicial recognition of congressional intent that the banking agencies have great discretion in applying and selecting their enforcement techniques. The decision implicitly draws determinations traditionally made by banking experts into the sluggish and expensive federal court system at a time when the savings and loan industry's resources are running out. Furthermore, the Gulf Federal court violated cardinal principles of judicial review of agency action by substituting its discretion and interpretation of agency authority for that of the agency in question. These principles have evolved over years of judicial consideration of agency action and congressional intent. The court's disregard of the traditional principles of judicial review at such an inappropriate moment is likely to produce the results that they were intended to prevent by opening the door to judicial rather than administrative or congressional supervision of financial institutions.