1994

Variable Annuity Life Insurance Company v. Clarke: A Second Look at National Bank Annuity Sales and 12 U.S.C. 92

Jonathan B. Cleveland

Comment

Variable Annuity Life Insurance Company v. Clarke: A Second Look at National Bank Annuity Sales and 12 U.S.C. § 92

Jonathan B. Cleveland

Commercial banks stand to earn billions of dollars in annual fee income[1] from selling annuity contracts.[2] Although historically the sale of annuities has been the almost exclusive domain of insurance companies, the Office of Comptroller of the Currency (OCC)[3] recently opined that national banks may sell fixed and variable annuity contracts in their branches through a brokerage subsidiary.[4] Not surprisingly, the insurance industry opposes commercial banks entering their once-protected market. An insurance company challenged the OCC opinion, claiming

1. *See Supreme Court Is Next Stop in Legal Dispute Over Bank Annuities*, BANKING POLICY REPORT, Sept. 20, 1993, at 7, 7 (stating that "billions of dollars in future business are at stake in the wake of a federal appeals court decision holding that national banks may not sell annuities"). In 1992, annuities generated $450 million in fee income for banks. Karen Talley, *Courts Leave Banks in Limbo on Right to Market Annuities*, AM. BANKER, Sept. 28, 1993, at 12, 12; *see* Arthur D. Postal, *Annuity Case Gets Push Toward Supreme Court*, FDIC WATCH, Jan. 24, 1994, at 1, 1 (noting that "annuities accounted for 7% of all bank brokerage sales activities in 1992"). During the first half of 1993, banks recorded their highest volume of annuity sales and expected strong future growth. Kalen Holliday, *Banks Benefit from Stampede to Insurance Products*, AM. BANKER, Sept. 24, 1993, at 13, 13.

2. An annuity contract creates an obligation to periodically pay a stated sum to a stated recipient for either a pre-determined fixed term, or for the life of the annuitant. *See* 1 JOHN A. APPLEMAN & JEAN APPLEMAN, INSURANCE LAW AND PRACTICE § 81 (1988).

3. The OCC is the administrator of national banks. *See* 12 U.S.C. §§ 21, 24(7), 92a(a)-(b) (1988 & Supp. IV 1993); *infra* note 12 and accompanying text (discussing OCC responsibilities).

4. *See* OCC Interpretive Letter No. 331, [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,501 (Apr. 4, 1985) (approving sale of variable annuity contracts); OCC Interpretive Letter No. 499, [1989-1990 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,090 (Feb. 12, 1990) (approving sale of fixed annuity contracts). A national bank must obtain approval from the OCC to engage in an activity not expressly described by statute. *See infra* note 12; *see also infra* note 79 and accompanying text (discussing OCC opinion permitting national banks to sell annuities).

that annuities are insurance, and that 12 U.S.C. § 92[5] prohibits national banks from selling insurance in cities with more than 5000 persons.[6]

A district court upheld the OCC opinion[7], but the Fifth Circuit overruled the OCC in *Variable Annuity Life Insurance Company v. Clarke (VALIC)*.[8] *VALIC* not only eliminates a potential billion-dollar source of fee income for national banks from the sale of annuities, but also sharply restricts national bank insurance powers. The Fifth Circuit interpreted § 92 broadly to prohibit national banks from brokering virtually any insurance company product or engaging in any insurance related activity.[9]

---

5. Section 92 provides that "any such [national bank] located and doing business in any place the population of which does not exceed five thousand inhabitants . . . may, under such rules and regulations as may be prescribed by the Comptroller of the Currency, act as the agent for any fire, life or other insurance company . . . by soliciting and selling insurance and collecting premiums on policies issued by such company." 12 U.S.C. § 92 (1988) (omitted since 1952). The United States Code has omitted § 92 since 1952 with a note indicating that Congress repealed it by the Act of April 5, 1918. *See* United States Nat'l Bank v. Independent Ins. Agents of Am., 113 S. Ct. 2173, 2176 (1993). The Supreme Court held that Congress did not repeal § 92. *Id.* at 2176-77.

The circuits disagree over the substantive meaning of 12 U.S.C. § 92. The Second and Fifth Circuits contend that § 92 creates a prohibition on national bank insurance activities in cities with more than 5000 persons. *See* American Land Title Ass'n v. Clarke, 968 F.2d 150, 156 (2d Cir. 1992), *cert. denied*, 113 S. Ct. 2959 (1993); Saxon v. Georgia Ass'n of Indep. Ins. Agents, Inc. 399 F.2d 1010, 1013 (5th Cir. 1968). The Eighth and D.C. Circuits contend that § 92 imposes no limitation on national bank insurance activities. *See* Independent Ins. Agents of Am., Inc. v. Board of Governors of the Fed. Reserve Sys., 736 F.2d 468, 476-77 (8th Cir. 1984); Independent Bankers Ass'n of Am. v. Heimann, 613 F.2d 1164, 1170 (D.C. Cir. 1979), *cert. denied*, 449 U.S. 823 (1980); *infra* note 147.

6. Variable Annuity Life Ins. Co. v. Clarke, 998 F.2d 1295, 1297 (5th Cir. 1993).

7. Variable Annuity Life Ins. Co. v. Clarke, 786 F.Supp. 639, 642 (S.D.Tex. 1991), *rev'd*, 998 F.2d 1295 (5th Cir. 1993).

8. 998 F.2d at 1296. The Fifth Circuit recently denied a petition by the OCC for review of the ruling *en banc*. *Valic Rehearing Rejected in 5th Circuit*, BANKING ATT'Y, Jan. 24, 1994, at 3. Although the OCC was undoubtedly disappointed by the ruling, the decision seems to provide an "engraved invitation to the Comptroller and the banking industry to ask the Supreme Court to review [*VALIC*]." *Id.* The Fifth Circuit rejected the OCC's petition for review because only four of the seven judges necessary voted in favor of rehearing the case. *Id.* Notably, six judges recused, leaving more judges in favor of rehearing than against. *Id.* Furthermore, the four judges favoring a rehearing issued a stinging statement objecting to the *VALIC* decision. *See* Postal, *supra* note 1, at 1. Judge Jerry E. Smith, voting in favor of a rehearing, stated that *VALIC* represents of view of § 92 that is "contrary to the well settled interpretation that has prevailed." *Id.* (quoting Judge Smith, dissenting from the Fifth Circuit's decision not to rehear *VALIC*).

9. *See infra* notes 96-99 and accompanying text.

Furthermore, *VALIC* retreats from a policy of bank deregulation that greatly expanded the financial products and services that commercial banks now market.[10]

This Comment argues that the Fifth Circuit erred in *VALIC*. Part I of the Comment provides a brief overview of the United States commercial banking industry with particular emphasis on the successful efforts of bank agencies to increase securities powers, and the less fruitful attempts to expand insurance powers. Part II discusses *VALIC* and the Fifth Circuit's rationale for prohibiting the sale of annuities in cities with more than 5000 persons. Part III critiques the court's reasoning and concludes that the Fifth Circuit should have deferred to the OCC interpretation that annuities are not insurance under § 92. Notwithstanding the classification of annuities, § 92 imposes no limit on national bank insurance powers. Thus, this Comment proposes that pursuant to OCC approval, national banks may market annuities and other insurance products without limitation.

I. OVERVIEW OF COMMERCIAL BANKING: SECURITIES AND INSURANCE POWERS

A. DUAL CHARTERING

The National Bank Act of 1864 (NBA)[11] created the Office of the Comptroller of the Currency[12] and empowered the OCC to grant federal bank charters.[13] Congress enacted the NBA to

10. *See infra* notes 46-48 and accompanying text (discussing the dismantling of Glass-Steagall securities restrictions by bank agency interpretations).

11. National Bank Act of 1864, ch. 106, 13 Stat. 99 (1864) (codified as amended in scattered sections of 12 U.S.C. (1988)).

12. The OCC, an office within the United States Treasury Department, has the responsibility of chartering and administering national banks. *See* PETER S. ROSE, THE CHANGING STRUCTURE OF AMERICAN BANKING 83-84 (1987). The OCC supervises the activities of federally-chartered banks by conducting periodic examinations. *See* GEORGE G. KAUFMANN & ROGER C. KORMENDI, DEREGULATING FINANCIAL SERVICES: PUBLIC POLICY IN FLUX 23-24 (1986). In general, a federally-chartered national bank must seek approval from the OCC to engage in any activity not expressly permitted by statute. *See* 12 U.S.C. §§ 24(7), 92a (1988).

13. Congress modeled the National Bank Act on various state bank chartering laws, particularly the New York Free Banking Act of 1838. *See* Edward L. Symons, *The "Business of Banking" in Historical Perspective*, 51 GEO. WASH. L. REV. 676, 689-90 (1983). In general, the state chartering laws provided that parties with a prescribed amount of capital could engage in banking activities without limitation. *See id.* at 689; KERRY COOPER & DONALD R. FRASER, BANKING DEREGULATION AND THE NEW COMPETITION IN FINANCIAL SERVICES 46 (1984). The lack of stringent legal barriers to bank entry during this period

help the federal government finance the Civil War[14] and to establish an exclusively federal banking system.[15] Despite the NBA, state-chartered banks flourished due to considerably fewer restrictions than their federally-chartered counterparts.[16]

The dual chartering system[17] led federal regulators to increase national bank powers to match those held by state banks.[18] Following the turn of the century, federal legislation enabled national banks to operate branch banks,[19] to loan on real estate,[20] and to sell insurance.[21] Shortly after World War I,

---

gave rise to the term "free banking era." *See* ROSE, *supra* note 12, at 82; COOPER & FRASER, *supra*, at 46-47. The National Bank Act, however, imposed significant barriers to entry, including higher capitalization requirements than most states required through state chartering laws. *Id.* at 48; *see* ROSE, *supra* note 12, at 83-84.

14. Congress required all national banks to purchase federal bonds and paper currency issued by the Treasury. ROBERT E. LITAN, WHAT SHOULD BANKS DO? 20 (1987).

15. Prior to 1862, the United States had no national paper currency. *Id.* State banks issued their own notes, many of which were worthless. *Id.* To account for multiple and potentially valueless bank notes, noteholders accepted large discounts from face value. *Id.* Advocates of the National Bank Act envisioned that state-chartered banks would convert to federal charters because national banks would offer more security to commercial transactions through the creation and use of a uniform currency. *Id.* at 20-21.

16. Initially, few state banks converted to federal charters. *Id.* Congress accelerated conversions by subsequently imposing a 10% tax on all state bank notes. *Id.* The tax accomplished its immediate purpose, but the number of state-chartered banks soon increased as a result of fewer constraints on banking activities. *Id.* For example, state banks could extend mortgages on real estate, while national banks could only provide commercial credit. *Id.* At the turn of the century, state-chartered banks still outnumbered national banks. *Id.* at 21-22.

17. A commercial bank must obtain a corporate charter from either a federal or state banking agency. Linda B. Matarese, *Has the Chevron Deference Made a Difference When Courts Review Federal Bank Agency Interpretations of the Glass-Steagall Act?*, 33 How. L.J. 195, 214 (1990). A bank can convert from a state to a federal charter, or from a federal to a state charter. *Id.* at 215; *see* 12 U.S.C. §§ 214-214c (1988).

18. *See* LITAN, *supra* note 14, at 22. One commentator notes that a competitive dialectic between state and federal regulators inevitably results in the incremental expansion of bank powers. *See* Kenneth E. Scott, *The Dual Banking System: A Model of Competition in Regulation*, 30 STAN. L. REV. 1, 30-36 (1977); *see also* Matarese, *supra* note 17, at 216-17 (setting forth critics' argument that federal bank regulators are "captured" and act in the private interest of those regulated rather than the public interest).

19. Act of February 25, 1927, ch. 191, § 7, 44 Stat. 1224, 1228 (1927) (codified as amended at 12 U.S.C. § 36 (1988)).

20. The Federal Reserve Act of 1913, ch. 6, § 24, 38 Stat. 251, 273 (1913) (codified as amended at 12 U.S.C § 371 (1988)).

21. Act of September 7, 1916, ch. 461, 39 Stat. 752, 753 (1916) (codified as amended at 12 U.S.C. § 92 (1988) (omitted since 1952)).

Congress permitted national banks to underwrite corporate securities.[22] As a result of these expansive powers, both state and federal commercial banks proliferated.[23]

B. The Banking Crisis of the 1930s and Remedial Legislation

Between 1930 and 1933 approximately one-third of the nation's commercial banks failed.[24] In response to the bank failures, Depression-era legislation created a comprehensive regulatory framework to ensure the solvency and stability of commercial banks and to protect depositors' funds.[25] The De-

22. After the Civil War, state-chartered banks were major participants in the lucrative securities underwriting market that financed the railroad expansion to the West. *See* Litan, *supra* note 14, at 22. National banks, however, could not underwrite corporate securities. *Id.* Underwriting activity intensified after World War I, and Congress attempted to lessen the restraints on national banks by permitting underwriting of those securities approved by the OCC. *Id.* at 23; *see* Act of February 25, 1927, ch. 191, § 2, 44 Stat. 1226 (1927) (codified as amended at 12 U.S.C. § 24(7) (1988)). At first, the Comptroller only approved bank underwriting of corporate bonds. Litan, *supra* note 14, at 22. Later, in response to the proliferation of state-chartered banks, the OCC permitted underwriting of corporate equity. *Id.*

23. In the early 1920s, more than 30,000 commercial banks operated in the United States. Cooper & Fraser, *supra* note 13, at 50. Technological advances in transportation and communications made geographic expansion feasible for commercial banks. Litan, *supra* note 14, at 24-25. The McFadden Act provided national banks with the legal authority to open branch locations according to the laws of their domiciliary state. *Id.* at 24. By 1929, multi-office banks held more than half of all assets in the American banking system. *Id.*

24. Litan, *supra* note 14, at 25; *see also* Cooper & Fraser, *supra* note 13, at 50 (describing impact of the Great Depression on the banking industry).

25. *See* Rose, *supra* note 12, at 352; Emeric Fischer, *Banking and Insurance - Should Ever The Twain Meet?*, 71 Neb. L. Rev. 726, 737-51 (1992). When President Roosevelt took office in 1933 the economy had collapsed, causing a nationwide run on bank deposits. *See* Cooper & Fraser, *supra* note 13, at 50; Litan, *supra* note 14, at 25. Congress and the President quickly enacted The Banking Act of 1933, legislation intended to restore public confidence in the nation's banking system. Rose, *supra* note 12, at 352. Congress targeted commercial banks for more stringent regulatory oversight than other financial institutions because of their public character as the guardians of American savings and private wealth. *See* Joseph J. Norton, *Up Against 'The Wall': Glass-Steagall and the Dilemma of a Deregulated ('Regulated') Banking Environment*, 42 Bus. Law. 327, 329 (1987).

The Banking Act of 1933 created the Federal Deposit Insurance Corporation (FDIC) to insure bank deposits up to a specified amount. The Banking Act of 1933, ch. 89, § 8, 48 Stat. 162, 168 (1933) (codified as amended at 12 U.S.C. §§ 1811-32 (1988)). Congress created deposit insurance to give depositors confidence in using commercial banks. Cooper & Fraser, *supra* note 13, at 145. In addition, the FDIC brought state-chartered banks under federal supervision for the first time. Litan, *supra* note 14, at 26.

Depression-era legislation attempted to prevent future commercial bank

pression-era legislation brought the "free banking era" to an abrupt end,[26] establishing stringent regulatory oversight designed to ensure a sound and stable banking system.[27]

In particular, Congress believed that commercial banks buying, selling, and underwriting securities precipitated bank failures.[28] As a result, Congress enacted the Glass-Steagall provisions of the Banking Act of 1933[29] to end commercial bank underwriting and to severely limit other securities activities.[30]

---

failures by limiting competition among financial institutions. COOPER & FRASER, *supra* note 13, at 54. Thus, legislation increased capitalization requirements and other barriers to entry, restricted permissible activities, and imposed greater regulatory oversight on banks. *Id.* at 54-55.

The Depression-era legislation also sought to diffuse economic power. *See* Fischer, *supra*, at 739. Toward this end, legislation restricted geographic expansion and bank affiliations with other industries. *Id.* at 737. The Glass-Steagall provisions of the 1933 Act separated commercial and investment banking. *See infra* notes 29-31 and accompanying text.

26. Depression-era legislation limited bank entry. *See* ROSE, *supra* note 12, at 86; *see also* COOPER & FRASER, *supra* note 13, at 52 (discussing end of "free banking era"); Fischer, *supra* note 25, at 741-43 (discussing entry restrictions imposed by Depression-era legislation). The chartering laws required that, to win approval, a federal bank charter applicant had to substantively prove that a significant public need existed, and that the new bank would be successful without injuring operating banks. *See* COOPER & FRASER, *supra* note 13, at 52. The FDIC can indirectly limit the entry of state banks by denying deposit insurance to a state bank applicant. *Id.* Because deposit insurance is generally necessary to operate a bank, the FDIC exercises de facto veto power over state bank entry. *Id.*

27. The 1933 Act increased the regulatory oversight role of the Federal Reserve System, prohibited the payment of interest on demand deposits, and raised the minimum capital requirements of national banks. *See* Banking Act of 1933, ch. 89, 48 Stat. 162 (1933). The Depression-era legislation preferred regulation to competition to restore stability in the banking system. *See* ROSE, *supra* note 12, at 353. Considering the economic circumstances of the 1930s in hindsight, regulators may have been justified in promulgating over-reaching regulation. *See id.* The present costs of over-regulation, however, may exceed the benefits derived from safety and soundness in the banking system. *Id.* at 86. In addition, reformers may have overstated the costs attributed to the free banking era. *Id.*

28. *See* Norton, *supra* note 25, at 329. Congress believed that excessive use of bank credit to speculate in the stock market precipitated the 1929 stock market crash and subsequent bank failures. *Id.*; *see* Matarese, *supra* note 17, at 221 (citing S. Rep. No. 77, 73d Cong., 1st Sess. 3-9 (statement of Sen. Glass)). In addition, Congress thought that using customer deposits for investment into corporate securities created unacceptable risks for commercial banks. Norton, *supra* note 25, at 329. Furthermore, Congress believed that commercial banks engaged in investment banking did not allocate credit or provide investment advice impartially. *Id.* at 334.

29. Banking Act of 1933, ch. 89, §§ 16, 20-22, 48 Stat. 162, 184-189 (1933) (codified as amended in scattered sections of 12 U.S.C. (1988)).

30. The Banking Act of 1933 is sometimes referred to as the Glass-Steagall Act. Norton, *supra* note 25, at 327 n.2. The term "Glass-Steagall" applies accu-

Glass-Steagall advanced the Depression-era policy of limiting competition among, and restricting permissible activities of, financial institutions.[31]

C. Judicial Deference to Administrative Agencies

Following the Depression era, federal bank agencies[32] expanded national bank powers by liberally interpreting Glass-Steagall and other banking laws. Courts generally noted that bank agency regulations, opinions, and statutory interpretations warranted judicial deference.[33] Courts did not, however, apply a consistent standard to review bank agency decisions.[34]

In 1984 the Supreme Court defined the relationship between courts and administrative agencies in *Chevron U.S.A.*,

---

rately to only four key provisions of the 1933 Act, §§ 16, 20, 21 and 22. *Id.* Together, these four provisions separated commercial from investment banking. *See id.* at 330-34. Commercial banks could not engage in underwriting or dealing in securities, and investment banks could not accept deposits. *Id.*

31. *See* KAUFMANN & KORMENDI, *supra* note 12, at 29; ROSE, *supra* note 12, at 352-54.

32. The OCC and the Federal Reserve Board are the two principal federal bank agencies that determine permissible banking activities. The OCC administers national banks. *See supra* notes 3, 12 and accompanying text (discussing the responsibilities of the OCC). The Federal Reserve Board supervises bank holding companies (BHC). *See* 12 U.S.C. § 1844 (1988). A BHC controls 25% or more of any class of voting securities of a bank, or if it otherwise exercises a controlling influence on the management, policies, or elections of a bank. 12 U.S.C. § 1841(a) (1988).

33. The Supreme Court articulated a presumption of judicial deference to bank agency interpretations of banking laws in *Investment Co. Inst. v. Camp*, 401 U.S. 617, 626-27 (1971). Matarese, *supra* note 17, at 230. The Court then, however, overturned an OCC regulation that authorized national banks to operate open-end mutual funds because the OCC stated no reasons for its decision. *Camp*, 401 U.S. at 627. Thus, *Camp* illustrates that an unsubstantiated bank agency decision does not warrant judicial deference because a court cannot ascertain whether the decision-maker properly considered the impact of the statute. *See id.* at 628.

Subsequent to *Camp*, courts generally deferred to bank agency interpretations concerning securities activities, but not concerning other areas. *See* Board of Governors of the Fed. Reserve Sys. v. Investment Co. Inst., 450 U.S. 46 (1981) (upholding Federal Reserve Board decision permitting bank holding companies to act as investment advisers to a closed-end investment company); New York Stock Exch., Inc. v. Smith, 404 F. Supp. 1091 (D.C. 1975) (upholding OCC approval of automatic investment service operated by national bank), *vacated on other grounds sub nom.*, New York Stock Exch., Inc. v. Bloom, 562 F.2d 736 (D.C. Cir. 1977), *cert. denied sub nom.*, New York Stock Exch., Inc. v. Heimann, 435 U.S. 942 (1978)); *cf.* Saxon v. Georgia Ass'n of Indep. Ins. Agents, 399 F.2d 1010 (5th Cir. 1968) (overturning OCC opinion allowing national banks to operate insurance agencies); *infra* notes 59-61 and accompanying text (discussing *Saxon*).

34. *See* Matarese, *supra* note 17, at 204-09.

Inc. v. Natural Resources Defense Council, Inc.[35] *Chevron* instructs courts that administrative agencies perform day-to-day law making.[36] Because administrative agencies are politically accountable branches, judicial deference to administrative decisions effectuates the policy objectives of the electorate.[37]

Chevron established a two-step test for review of an agency's interpretation of a statute.[38] If Congress clearly and unambiguously stated its intent, both the agency and the court must effectuate that intent.[39] If, however, Congress did not directly address the question, or addressed the question ambiguously, then the court must determine whether the agency interpretation is a "permissible construction" of the statute.[40] The agency need not adopt the only permissible construction, nor the reading that the court would have reached on its own.[41] The agency's construction controls unless it is "arbitrary, capricious, or manifestly contrary to the statute."[42]

---

35. 467 U.S. 837 (1984). *Chevron* subordinated the judiciary to administrative agencies when determining the meaning of statutes. *Id.* at 843-845; *see* Matarese, *supra* note 17, at 206. D.C. Circuit Judge Abner J. Mikva notes that *Chevron* creates a "hands off" policy that approaches "near abdication" to administrative agencies. *See* Hon. Abner J. Mikva, *How Should The Courts Treat Administrative Agencies?*, 36 AM. U. L. REV. 1, 6-9 (1986).

36. *See* Mikva, *supra* note 35, at 3. In *Chevron* the Court stated that "if Congress has explicitly left a gap for the agency to fill, there is an express delegation of authority to the agency to elucidate a specific provision of the statute by regulation . . . . Sometimes the legislative delegation to an agency on a particular question is implicit rather than explicit." 467 U.S. at 843-44 (footnote omitted).

37. The Court reasoned that "[j]udges . . . are not part of either political branch of the Government. . . . [I]t is entirely appropriate for [administrative agencies] to make such policy choices - resolving the competing interests which Congress itself either inadvertently did not resolve, or intentionally left to be resolved by the agency . . . ." *Id.* at 865-66. Furthermore, "federal judges—who have no constituency—have a duty to respect legitimate policy choices made by those who do." *Id.* at 866; *see* Mikva, *supra* note 35, at 3.

A court cannot circumvent *Chevron* and supersede an agency interpretation with its own policy preference. *See Chevron*, 467 U.S. at 866 (arguing that "the responsibilities for assessing the wisdom of such policy choices and resolving the struggle between competing views of the public interest are not judicial ones . . ."). Independent decision making by inexpert judges precludes utilizing agency expertise to make technical policy choices. *See* Mikva, *supra* note 35, at 3. Some regulatory areas require heavy technical expertise and frequent oversight is efficiently accomplished only by utilizing administrative agencies. *Id.*

38. *Chevron*, 467 U.S. at 842-43.

39. *Id.*

40. *Id.* at 843.

41. *Id.* at 843, n.11.

42. *Id.* at 844.

D. DISMANTLING GLASS-STEAGALL WITH THE HELP OF *CHEVRON*

Chevron enabled bank regulators to "dismantle" Glass-Steagall.[43] Beginning in the 1970s, economic factors and rapid technological advances dramatically changed the landscape of the financial services industry.[44] Depression-era legislation restricted commercial banks from effectively competing with other financial institutions.[45] Bank agencies responded during the 1980s by deregulating commercial banks, particularly the restrictions imposed by Glass-Steagall.[46] Bank agency interpreta-

---

43. *See, e.g.*, Clarke v. Securities Indus. Ass'n, 479 U.S. 388, 403-04 (1987) (upholding an OCC opinion under *Chevron* allowing national banks to market securities through retail discount brokerage subsidiaries located in their branches). *Clarke v. Securities Indus. Ass'n* illustrates the great extent to which courts must defer to interpretations by the OCC. *Id.* at 403-04.

44. Interest rate ceilings imposed on banks proved untenable during the double-digit inflation periods of the 1970s. LITAN, *supra* note 14, at 33. In addition, rapid technological advances and "one-sided" regulation enabled other institutions, such as nonbanks, to effectively exploit market opportunities and to replace commercial banks in many areas. *Id.* at 33-34; *see* Fischer, *supra* note 25, at 771-75 (discussing competition between nonbanks and commercial banks).

A nonbank is an entity that provides either credit or depository functions, but not both. *See* COOPER & FRASER, *supra* note 13, at 198-203. The size and scope of nonbanking firms poses a significant threat to the market share of commercial banks. *See* LITAN, *supra* note 14, at 44. Diversified nonbank financial institutions offer a wide range of depository, lending, and investment services that commercial banks historically provided. *Id.* In addition, non-financial industrial companies have become leading providers of financial services. *Id.*

45. Nonbanks can compete in commercial bank markets, but commercial banks cannot enter many nonbank markets. LITAN, *supra* note 14, at 41. Increasingly, commercial banks did not meet the credit needs of borrowers due to the "one-sided" regulatory constraints. *Id.* Commercial enterprises obtained short and intermediate term financing from the commercial paper markets. *Id.* The booming securities market during the 1980s encouraged raising funds from the capital markets rather than borrowing from banks. *Id.* at 42. Consequently, commercial banks lost market share as providers of credit. *See id.* at 45 (Figure 2-7).

As a result of increased competition in the credit markets, commercial banks assumed riskier loans to boost profitability. *Id.* at 49. Commercial banks lent to higher-risk borrowers because low-risk borrowers utilized alternative sources. *Id.* Thus, one-sided regulation jeopardized the structural soundness of commercial banks. *Id.*

46. The Reagan Administration favored deregulating commercial banks. *Id.* at 49. *See generally* Joseph Jude Norton, *The 1982 Banking Act and the Deregulation Scheme*, 38 BUS. LAW. 1627 (1983) (examing the deregulation scheme after the 1982 legislation). In 1980, Congress removed the interest rate controls the Banking Act of 1933 placed on national banks. *See* Depository Institutions Deregulation and Monetary Control Act of 1980, § 207, 94 Stat. 132, 144 (1980) (codified as amended at 12 U.S.C. §§ 3501-09 (1988)). In 1988, Congress considered repealing certain sections of Glass-Steagall to allow banks to

tions, generously upheld under *Chevron*, substantially displaced prohibitions on dealing and underwriting securities.[47] By 1990, bank holding companies and national banks could operate discount and full service brokerages, as well as engage in limited underwriting and dealing in commercial paper, corporate debt and equity, municipal revenue bonds, and mortgage-backed securities.[48]

E. National Bank Insurance Powers

Increasingly, commercial banks have sought authority to market insurance and other non-traditional financial products.[49] Bank regulators, however, have resisted expanding bank insurance powers due partly to the historical perception that banking and insurance are distinct industries.[50] Congress has

---

underwrite all types of securities except corporate equity. *See* Matarese, *supra* note 17, at 217. Congress did not act, but several Senators and Representatives encouraged banks to expand powers through banking agencies. *Id.* (citing *Proxmire and Garn Urge Greenspan to Let BHCs Underwrite Debt, Equity Securities*, 51 Banking Rep. (BNA) 829 (Nov. 14, 1988)).

47. In 1987 the Board of Governors of the Federal Reserve System (Board) approved the application of several bank holding companies seeking to engage in underwriting of and dealing in certain "ineligible securities," activities expressly prohibited under § 20 of Glass-Steagall. *Citicorp*, 73 Fed. Reserve Bull. 473 (1987). The Board determined that a member bank may underwrite ineligible securities through a subsidiary so long as the subsidiary is not "engaged principally" in underwriting ineligible securities. *Id.* at 475-77. A subsidiary is "engaged principally" in an activity if it derives five percent or more of its average gross revenues over a two-year period from that activity. *Id.* at 483. The Second Circuit upheld the Board's interpretation based on *Chevron*. *See* Securities Indus. Ass'n v. Board of Governors of Fed. Reserve Sys., 839 F.2d 47, 69 (2d Cir. 1988). *Securities Indus. Ass'n v. Board of Governors* precipitated the "dismantling of Glass-Steagall." *See* Fischer, *supra* note 25, at 782. In 1989, the Board expanded the class of securities that banks can underwrite to include all types of corporate debt and equity. *J.P. Morgan & Co., Inc.*, 75 Fed. Reserve Bull. 192, 193 (1989). Later that year, the Board determined that a BHC could earn up to 10% of its gross revenues from underwriting without being "engaged principally" in that activity. *See* 75 Fed. Reserve Bull. 751 (1989).

48. Fischer, *supra* note 25, at 783.

49. *See id.* Commercial banks did not initially engage in broad insurance activities because of the relatively lower returns available when compared to investment banking. Litan, *supra* note 14, at 72. Larger banks, however, seemingly could benefit by selling insurance because they could market insurance more aggressively than existing insurance company agents. *Id.* at 72-73 n.27 (citing Consumer Federation of America, The Potential Costs and Benefits of Allowing Banks to Sell Insurance (1987)). American consumers would benefit most, saving five to seven billion dollars per year as a result of the increased competition. *Id.*

50. *See* Michael G. Capatides, A Guide To The Capital Markets Activities of Banks and Bank Holding Companies 244, 247 (1990).

generally acquiesced to insurance industry lobbying efforts and refused to expand national bank insurance powers.[51] Furthermore, the pre-*Chevron* practice of judicial deference to bank agencies generally did not extend to national bank insurance powers.[52] Even after *Chevron*, some courts narrowly interpreted national bank insurance powers relying on those pre-*Chevron* decisions.[53]

National banks may engage in insurance activities pursuant to 12 U.S.C. § 24(7)[54] and 12 U.S.C. § 92.[55] Neither § 24(7) nor § 92 expressly limits national bank insurance activities.

---

51. *Id.* at 244. For example, the Competitive Equality Banking Act of 1987 created a moratorium on any action by federal banking agencies to increase insurance powers. *See* Competitive Equality Banking Act §§ 201-202, 101 Stat. 581-584 (1987) (codified at 12 U.S.C. § 1841 in a note since expiration of the moratorium). The moratorium expired in March 1988. CAPATIDES, *supra* note 50, at 244. In addition, the insurance industry successfully lobbied Congress to restrict the insurance activities of bank holding company subsidiaries in the Garn-St. Germain Act. *See* Garn-St. Germain Depository Institutions Act of 1982, Pub. L. No. 97-320, 96 Stat. 1469, 1536-1538 (1982) (codified as amended at 12 U.S.C. § 1843(c)(8)(A)-(G) (1988)); Ralph P. DeSanto, Note, *Product Expansion in the Banking Industry: An Analysis and Revision of Section 4(c)(8) of the Bank Holding Company Act*, 53 FORDHAM L. REV. 1127, 1142 (1985).

52. *See* Saxon v. Georgia Ass'n of Indep. Ins. Agents, 399 F.2d 1010, 1013-17 (5th Cir. 1968); *infra* notes 59-61 and accompanying text (discussing *Saxon*).

53. *See* American Land Title Ass'n v. Clarke, 968 F.2d 150 (2d Cir. 1992), *cert. denied*, 113 S. Ct. 2959 (1993); *infra* notes 71-74 and accompanying text (discussing *American Land Title Ass'n v. Clarke*).

54. Section 24(7) states "[a national bank shall have power to] exercise . . . all such *incidental powers* as shall be necessary to carry on the *business of banking*." 12 U.S.C. § 24(7) (1988) (emphasis added). Thereafter, § 24(7) enumerates specific activities in which national banks can engage. Section 24(7) is commonly referred to as the "powers clause." *See* Symons, *supra* note 13, at 698.

Section 24(7) does not expressly grant insurance powers to national banks. Insurance powers derive from the "business of banking" clause and the "incidental powers" clause. *Id.* at 683. Although the OCC has relied on the "incidental powers" clause to approve insurance activities, some commentators contend that the "business of banking" clause grants the authority to engage in many financial activities, including insurance. *Id.* at 680. *See generally* American Ins. Ass'n v. Clarke, 865 F.2d 278 (D.C. Cir. 1988) (stating that the "business of banking" includes activities beyond those enumerated in § 24(7)); Independent Bankers Ass'n of Am. v. Heimann, 613 F.2d 1164 (D.C. Cir. 1979) (upholding national bank authority to broker credit life insurance under § 24(7)), *cert. denied*, 449 U.S. 823 (1980).

55. Section 92 states that "any such [national bank] located and doing business in any place the population of which does not exceed five thousand inhabitants . . . may, under such rules and regulations as may be prescribed by the Comptroller of the Currency, act as the agent for any fire, life or other insurance company . . . by soliciting and selling insurance and collecting premiums on policies issued by such company." 12 U.S.C. § 92 (1988) (omitted since 1952); *see supra* note 5 and accompanying text.

Bank agencies and courts, therefore, have determined permissible commercial bank insurance activities. To date, the Supreme Court has remained silent on the substantive scope of national bank insurance powers under § 92.[56]

In 1963 Comptroller James Saxon, a strong proponent of expanding commercial bank powers,[57] promulgated an OCC ruling that permitted national banks to sell insurance incidental to banking transactions.[58] The Fifth Circuit, however, overturned the OCC ruling in *Saxon v. Georgia Ass'n of Independent Insurance Agents*,[59] holding that § 92 prohibits national banks from operating insurance agencies in cities where the population exceeds 5000 persons.[60] The court concluded that the express grant of insurance powers in § 92 defines the full extent of national bank insurance powers.[61]

Saxon jeopardized all insurance-related activities at most national bank locations, including a long standing practice of

56. *But see* United States Nat'l Bank v. Independent Ins. Agents of Am., 113 S. Ct. 2173, 2176-77 (1993) (holding that Congress did not repeal 12 U.S.C. § 92, but failing to address the substantive meaning of § 92). For a discussion of the Court's decision that 12 U.S.C. § 92 was not repealed, see *supra* note 5 and accompanying text.

57. *See* LITAN, *supra* note 14, at 31.

58. OCC Ruling No. 7110 (1963). The OCC ruling stated that "[i]ncidental to the powers vested in [national banks] under 12 U.S.C. sections 24, 84, and 371, National Banks have the authority to act as agent in the issuance of insurance which is incident to banking transactions." Saxon v. Georgia Ass'n of Indep. Ins. Agents, 399 F.2d 1010, 1012 (1968) (quoting OCC Ruling No. 7110 (1963)). The OCC did not limit its ruling to cities of 5000 persons or fewer. *Id.* Subsequently, the OCC approved the application of Citizens and Southern National Bank to sell broad forms of automobile, home, casualty, and liability insurance in branches located in cities with more than 5000 persons. *Id.*

59. 399 F.2d 1010 (5th Cir. 1968).

60. *Id.* at 1012.

61. *Id.* The Fifth Circuit rejected the claim that insurance powers exist outside of § 92 based on the *expressio unius est exclusio alterius* rule of statutory construction. *Id.* at 1013-14. The *expressio unius* rule of statutory construction means that the mention of one thing in the statute implies the exclusion of another. *Id.* at 1014. Accordingly, the express power to operate insurance agencies in cities with fewer than 5000 persons implies that national banks lack the power to do the same in cities with more than 5000 persons. *Id.* at 1013. The Fifth Circuit supported its construction with the legislative history of § 92. *Id.* The court noted that Congress enacted 12 U.S.C. § 92 in response to a letter by Comptroller John Skelton Williams in 1916. *Id.* (citing 53 CONG. REC. 11,001 (1916)). The Comptroller's letter stated that national banks neither have the express nor the implied authority to act as insurance agents. *Id.* The Comptroller, therefore, recommended that Congress grant insurance powers to national banks located in small towns. *Id.*

selling credit life insurance.[62] Subsequently, in *Independent Bankers Ass'n of America v. Heimann*,[63] the D.C. Circuit held that the sale of credit life insurance did not violate § 92.[64] In *Heimann*, the court determined that national banks have certain insurance powers under § 24(7) not subject to § 92.[65] According to the D.C. Circuit, the *Saxon* construction of § 92 applied only to national banks operating general insurance agencies.[66] The court concluded that selling credit life insurance is incidental to lending, an activity expressly authorized in § 24(7).[67]

The Eighth Circuit also disagrees with the *Saxon* construction of § 92. In *Independent Insurance Agents of America, Inc. v. Board of Governors of the Federal Reserve System*,[68] the Eighth Circuit ignored *Saxon* and held that § 92 does not apply to a

62. *See* Barry A. Abbott et al., *Banks and Insurance: An Update*, 43 BUS. LAW. 1005, 1016 (1988).

63. 613 F.2d 1164 (D.C. Cir. 1979), *cert. denied*, 449 U.S. 823 (1980).

64. *Id.* at 1170. Credit life insurance is a form of security on consumer loans. *Id.* at 1168. A borrower purchases credit life insurance to satisfy the loan in the event of a casualty. *Id.* at 1168 n.9.

65. *Id.* at 1170. The court disagreed with the *Saxon* interpretation that § 92 limits national bank insurance activities. *Id.* According to the court, § 92 creates no limit on national bank insurance activities in cities with more than 5000 persons. *Id.* at 1170 n.18.

66. *Id.* at 1170.

67. *Id.* According to the D.C. Circuit, national banks have incidental powers to pursue all activities related to the "business of banking" activities enumerated in 12 U.S.C. § 24(7). *Id.* Credit life insurance is a commonplace product when ordinary loans on security are involved. *Id.* Thus, a bank has the incidental power to sell credit life insurance under § 24(7) notwithstanding § 92. *Id.*

The D.C. Circuit avoided applying § 92 to a national bank insurance activity in American Ins. Ass'n v. Clarke, 865 F.2d 278 (D.C. Cir. 1988). The court upheld an OCC decision allowing a national bank to sell municipal bond insurance. *Id.* at 281-82. To reach its decision, the court deferred to the OCC's interpretation that municipal bond insurance was the functional equivalent of issuing a standby letter of credit, a service traditionally provided by national banks under 12 U.S.C. § 24(7). *Id.* at 281-82. The court expressed that the term "business of banking" in § 24(7) includes activities beyond those specifically enumerated. *Id.* at 281. Confining bank activities to those specifically enumerated in 12 U.S.C. § 24(7), or those merely incident thereto, reflects "a narrow and artificially rigid view of both the business of banking and the [National Bank Act]." *Id.* (quoting the district court decision in American Ins. Ass'n v. Clarke, 656 F.Supp 404, 408 (D.D.C. 1987), *aff'd* 865 F.2d 278 (D.C. Cir. 1988)). Under *Chevron*, "the Comptroller's expert judgment in this regard should not be overturned." *Id.* at 283 (quoting district court decision in American Ins. Ass'n v. Clarke, 656 F.Supp at 409-10). Thus, the *Saxon* construction of § 92 does not apply to insurance activities within the broad parameters of the "business of banking" powers of § 24(7).

68. 736 F.2d 468 (8th Cir. 1984).

bank holding company's (BHC) national banks when the BHC's insurance agencies are separate subsidiaries.[69]

Responding to the favorable shift toward commercial bank insurance powers, the OCC extended national bank insurance powers into areas less related to traditional bank activities.[70] The Second Circuit, however, recently took a narrow view of national bank insurance powers in *American Land Title Ass'n v.*

---

69. *Id.* at 470. The Board permitted two BHCs, Commerce Bancshares, Inc. (Commerce) and Mercantile Bancorporation, Inc. (Mercantile), to sell certain kinds of insurance through a separate subsidiary to customers of its operating banks. *Id.* For example, the subsidiary may sell car insurance, collision, and liability, to a customer of the bank who borrowed money to buy the car. *Id.* at 471. Mercantile and Commerce operated several national banks in cities with more than 5000 persons. *Id.* at 476. The insurance association plaintiff argued that the sale of insurance violated 12 U.S.C. § 92. *Id.* The court noted that *Saxon* was difficult to distinguish from this situation, yet openly criticized and questioned the validity of the *Saxon* construction of § 92:

> There is a strong argument that *Saxon* was wrongly decided. The legislative history indicates that Congress was concerned only with providing small-town banks with an additional profit source, not with prohibiting city banks from selling insurance. Despite our doubts about *Saxon*'s validity, we prefer not to disagree openly with a sister circuit, and find it unnecessary to do so.

Id. at 477 n.6. The court concluded that *Saxon* did not apply because the operations of the banks and insurance subsidiaries were separate. *Id.* at 477. Thus, a BHC can circumvent "whatever strictures § 92, as interpreted by *Saxon*, impose[s]" by separately incorporating its national bank and insurance agency subsidiaries. *Id.*

After the Garn-St. Germain Act of 1982, a BHC may not engage in certain insurance activities through nonbanking subsidiaries. *See supra* note 51 and accompanying text; 12 U.S.C. § 1843(c)(8) (1988). The nonbanking prohibitions of 12 U.S.C. § 1843(c)(8) do not apply, however, to the direct activities of BHC banks. *See Merchant National Corporation*, 75 FED. RESERVE BULL. 388 (1989); Independent Ins. Agents of Am. v. Board of Governors of Fed. Reserve Sys., 890 F.2d 1275, 1283 (2d Cir. 1989) (holding that § 1843(c) insurance activity prohibitions do not apply to BHC's state-chartered banks), *cert. denied*, 498 U.S. 810 (1990). Thus, while a BHC may not directly engage in certain insurance activities through a nonbanking subsidiary, a BHC may engage in those insurance activities through its bank subsidiaries as long as the chartering authority has approved such activities. *See id.* at 1279-80.

70. The OCC authorized national banks to broker annuity contracts to bank customers. *See* OCC Interpretive Letter No. 331, [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,501 (Apr. 4, 1985); OCC Interpretive Letter No. 499, [1989-1990 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,090 (Feb. 12, 1990). In two interpretive letters, the OCC authorized national banks to sell and underwrite title insurance. OCC Interpretive Letter No. 368, [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,538 (July 11, 1986); OCC Interpretive Letter No. 377, [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,601 (Feb. 6, 1987); *see also* OCC Interpretive Letter No. 366, [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,536 (Aug. 18, 1986) (concluding that § 92 places no geographical limitation on the insurance activities of a national bank in a town of fewer than 5000 persons).

Clarke,[71] holding that § 92 prohibits national banks from selling title insurance in cities with more than 5000 persons.[72] The court based its decision on the *Saxon* construction of § 92.[73] Furthermore, the Second Circuit rejected the D.C. Circuit's holding in *Heimann* that § 24(7) provides insurance powers not subject to limitation by § 92.[74]

Notwithstanding the adverse impact of *American Land Title Ass'n v. Clarke*, national banks discovered a loophole to avoid the *Saxon* limitation on national bank insurance powers. In *Independent Insurance Agents of America, Inc. v. Ludwig*,[75] the D.C. Circuit upheld an OCC opinion and concluded that § 92 imposes no geographical limitation on a national bank insurance agency located in a town of fewer than 5000 persons.[76] *Ludwig* provided a significant victory for national banks because such banks can simply locate branches in towns of fewer than 5000 persons and market insurance products into cities with more than 5000 persons.[77] Unfortunately, commercial banks proba-

71. 968 F.2d 150 (2d Cir. 1992), *cert. denied*, 113 S. Ct. 2959 (1993).

72. *Id.* at 157.

73. *Id.* at 156. The court first recognized that the *Chevron* standard of review was applicable. *Id.* at 154-55. Next, the court followed the *Saxon expressio unius est exclusio alterius* construction of § 92 and concluded that Congress intended to prohibit any general insurance agency activity of a national bank in towns with more than 5000 persons. *Id.* at 155. To support its construction, the court referenced the 1916 letter to Congress by Comptroller John Skelton Williams that proposed giving banks the power to operate insurance agencies in small towns. *Id.* at 155-56 (citing 53 CONG. REC. 11,001 (1916)).

74. The court criticized the *Heimann* position that § 92 imposes no limitation on national bank insurance activities. *Id.* at 156-57. According to the Second Circuit, if Congress wanted all banks to possess insurance powers regardless of location, then the population provision would be superfluous. *Id.* at 155. Notwithstanding § 92, the court distinguished *Heimann* based on the unique nature of credit life insurance. *Id.* at 156. Title insurance differs from credit life insurance because title insurance protects both the borrower's and the lender's interest, whereas credit life insurance only protects the lender's interest. *Id.* at 157. Thus, credit life insurance constitutes a banking activity and title insurance an insurance activity. *Id.*

75. 997 F.2d. 958 (D.C. Cir. 1993).

76. *Id.* at 958. The OCC interpretive letter stated that "a national bank or its branch which is located in a place of 5,000 or under population may sell insurance to existing and potential customers located anywhere." *Id.* at 959 (quoting Letter from Judith A. Walter, Senior Deputy Comptroller for National Operations, to U.S. National Bank of Oregon).

77. Chase Manhattan and other national banks may circumvent the *American Land Title Ass'n* decision and sell title insurance nationwide through a small town branch. *See* Arthur D. Postal, *OCC Chase Stratagem Exploits Insurance Rule*, FDIC WATCH, Oct. 11, 1993, at 1. The *Ludwig* decision prompted intense lobbying efforts by the insurance industry to close the "small-town loop-

bly cannot effectively sell annuities from distant branches.[78] Thus, while liberalizing bank insurance powers dramatically, *Ludwig* does not resolve the dilemma national banks face in marketing annuities.

II. *VALIC*: NATIONAL BANK ANNUITY SALES LIMITED BY 12 U.S.C. § 92

The OCC opined that national banks may market fixed and variable annuities in their branches pursuant to 12 U.S.C. § 24(7) and that 12 U.S.C. § 92 does not apply to the sale of annuity contracts by national banks.[79] Subsequently, the OCC ap-

---

hole." *See* David W. Roderer, *VIEWPOINT: Congress Should Defer Action on Bank Annuity Sales*, AM. BANKER, Nov. 3, 1993, at 12.

78. *See* Postal, *supra* note 77, at 1. Selling annuities by mail and via telemarketing is not feasible. *Id.* Banks will probably exploit *Ludwig* with other forms of insurance more easily sold by mail and telephone solicitations. *Id.*

79. In 1985, the OCC permitted national banks to broker variable annuities through discount brokerage subsidiaries. OCC Interpretive Letter No. 331, [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,501, at 77,773 (Apr. 4, 1985). Variable annuity contracts provide an accumulation unit in a separate investment portfolio in exchange for a lump sum or periodic payment. *Id.* At maturity, the annuitant receives a pro rata share of the portfolio for either a fixed term or life. *Id.* The OCC acknowledged that variable annuities expose issuers to the risk that the annuitant will outlive the expected mortality date. *Id.* at 77,774. In that regard, issuers may structure the payments according to detailed mortality tables. *Id.* A variable annuity, however, does not guarantee any payment at maturity and therefore, the investment risk falls entirely on the annuitant. *Id.* Thus, despite the feature of mortality risk, a variable annuity more closely resembles shares in a mutual fund. *Id.* The OCC cited cases supporting its reasoning. *Id.* (citing SEC v. United Benefit Life Ins. Co., 387 U.S. 202 (1966); Investment Co. Inst. v. Camp, 401 U.S. 617 (1971)). As such, variable annuities are securities that a national bank can buy and sell without recourse under 12 U.S.C. § 24(7). *Id.*

In 1990, the OCC approved the sale of fixed annuity contracts by national banks. OCC Interpretive Letter No. 499, [1989-1990 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,090, at 71,210 (Feb. 12, 1990). A fixed annuity provides a guaranteed payment for a fixed term, or life, in exchange for the premium, or premiums, paid by the annuitant. *Id.* at 71,212. National banks may sell fixed annuities pursuant to their general power to broker financial instruments. *Id.* at 71,213. Although historically a product of insurance companies, the OCC determined that annuities are financial investment products, not insurance. *Id.* The OCC noted that investors purchase annuities to provide tax-sheltered saving for retirement, not to shift financial risk of catastrophic events as in the case of insurance. *Id.* at 71,212 ; *see also* In re Howerton, 21 B.R. 621, 623 (1982) (opining that "life insurance is a promise to pay a certain sum on the death of an insured and an annuity is essentially a form of investment"); APPLEMAN, *supra* note 2, at 295 (arguing that "annuity contracts must . . . be recognized as investments rather than insurance"). Thus, the "risk is essentially an investment risk, not an insurance risk." OCC Interpretive Letter

proved the application of NCNB National Bank of North Carolina to sell fixed and variable annuity contracts through its subsidiary NCNB Securities.[80] On April 16, 1991, the Variable Annuity Life Insurance Company (the Company) filed suit seeking declaratory and injunctive relief against the OCC.[81] The Company claimed that the sale of annuities by national banks violated 12 U.S.C. § 92.[82] On cross motions for summary judgment, the district court granted the OCC's motion and denied the Company's.[83] The district court found that Congress never specifically addressed whether national banks can sell annuity contracts.[84] The court then upheld the OCC opinion because the

---

No. 499, [1989-1990 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,090, at 71,212 (Feb. 12, 1990); *see also* Helvering v. LeGierse, 312 U.S. 531, 542 (1941) (reasoning that "any risk that the [premium] would earn less than the amount paid to respondent as an annuity was an investment risk . . . not an insurance risk"). In addition, annuity contracts resemble debt instruments because an issuer's obligation to make periodic payments resembles that of a debtor. OCC Interpretive Letter No. 499, [1989-1990 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,090, at 71,212-13 (Feb. 12, 1990). Furthermore, the OCC reasoned that a fixed annuity functionally resembles a certificate of deposit (CD). *Id.* at 71,213. A fixed annuity for a fixed term resembles a CD that withdraws a portion of principal to reduce the balance to zero at the end of the term. *Id.* An annuity with a life term operates like a CD with a life interest in the income. *Id.* The OCC concluded that banks sell other financial instruments that entail the two principal features of a fixed annuity, life term and fixed return. *Id.*

The OCC also disagreed with the *Saxon* interpretation of § 92. *Id.* Congress did not define "insurance" in § 92. *Id.* at 71,214. The OCC cited various dictionary definitions and cases to support its decision that annuities are not "insurance" within the meaning of § 92. *Id.* The OCC determined, however, that even under *Saxon*, § 92 does not prohibit the sale of annuities. *Id.* at 71,215. According to the OCC, the *Saxon* limitation applies, if at all, only to broad forms of insurance, such as fire or life insurance, and does not affect specialized products such as annuities. *Id.*

80. OCC Unpublished Interpretive Letter from J. Michael Shepherd, Senior Deputy Comptroller Corporate & Economic Programs, to Robert M. Kurucza, Attorney on behalf of NCNB National Bank of North Carolina (March 20, 1990), *available in LEXIS*, Banking Library, ALLOCC File.

81. Variable Annuity Life Ins. Co. v. Clarke, 786 F. Supp. 639, 640 (S.D. Tex. 1991).

82. *Id.* The Company sells annuities in all fifty states and directly competed with NCNB in the business of selling annuity contracts. *VALIC*, 998 F.2d at 1297.

83. *Variable Annuity Life Ins. Co.*, 786 F. Supp. at 640.

84. *Id.* at 641. According to the district court, Congress did not address whether banks may sell insurance in cities with more than 5000 persons or the meaning of insurance under § 92. *Id.* The court noted that the plain language of § 92 expressly grants national banks the authority to operate insurance agencies in cities with fewer than 5000 persons. *Id.* The language does not expressly prohibit national bank insurance activities and "it is neither arbitrary nor capricious to view 12 U.S.C. § 92 as a supplemental powers provision and not a limitation on national banks[']' incidental powers under § 24(7)." *Id.* at

OCC's interpretation was a "permissible construction" under *Chevron*.[85] On appeal, the Fifth Circuit reversed the district court and concluded that the sale of annuities by national banks violated 12 U.S.C. § 92.[86]

According to the Fifth Circuit, the *Saxon* interpretation of § 92 exhibits Congress's clear intent to limit national bank insurance activities to cities with fewer than 5000 persons; therefore, the district court never should have reached the second step of *Chevron*.[87] The court relied on the *expressio unius est exclusio alterius* construction of § 92 set forth in *Saxon* to reach this conclusion.[88] The court supported its construction by noting that the legislative record of § 92 indicates that national banks should operate insurance agencies only in small communities.[89] Furthermore, the court contended that the OCC cannot invoke *Chevron* to overrule the judicial precedent established by *Saxon*.[90]

---

642. The court also noted that the legislative record indicates that Congress enacted § 92 to provide an additional source of income for national banks located in small towns, not to protect insurance companies from competition. *Id.* at 641.

The district court observed that § 92 does not define "insurance." *Id.* Congressional silence, combined with express rulemaking authority delegated to the OCC, "left a gap for the [Comptroller] to fill." *Id.* (quoting Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837, 843 (1984)). The OCC determined that annuities were financial investment instruments, not insurance products, because they do not indemnify against risk of loss. *Id.*

85. *Id.* at 642 (citing *Chevron*, 467 U.S. at 843).

86. *VALIC*, 998 F.2d at 1296. The Fifth Circuit applies de novo review on an appeal from summary judgment when questions of law control the disposition. *Id.* at 1297.

87. *Id.* The court first observed that 12 U.S.C. § 92 exists after U.S. Nat'l Bank v. Independent Ins. Agents of Am., 113 S. Ct. 2173 (1993). *VALIC*, 998 F.2d at 1297-98; *see supra* note 5 and accompanying text.

88. *Id.* at 1298. In addition, the Second Circuit recently followed *Saxon* in reversing an OCC directive permitting national banks to sell title insurance. *Id.*; *see* American Land Title Ass'n v. Clarke, 968 F.2d 150 (2d Cir. 1992); *supra* notes 71-74 and accompanying text (discussing *American Land Title Ass'n v. Clarke*).

89. *VALIC*, 998 F.2d at 1298-99. The only source of legislative history concerning § 92 is a 1916 letter from Comptroller John Skelton Williams to Congress proposing that national banks should have the authority to act as insurance agents. To support its construction of § 92, the Fifth Circuit cited a portion of that letter that states "from the standpoint of public policy and banking efficiency that this authority should be limited to banks in small communities." *Id.* at 1299 (citing 53 CONG. REC. 11,001 (1916)).

90. *Id.* at 1300 (citing Lechmere, Inc. v. NLRB, 112 S. Ct. 841 (1992); BPS Grand Services, Inc. v. NLRB, 942 F.2d 519, 523 (8th Cir. 1991)). The OCC questioned the precedential weight of *Saxon* because the case was decided sixteen years before *Chevron*. *Id.*

The Fifth Circuit then held that annuities are insurance products, both historically and functionally.[91] All fifty states regulate annuities under their insurance laws.[92] Annuities are insurance products because "functionally they are the mirror image of life insurance."[93] In addition, life insurance and annuities both rely in part on actuarial calculations of mortality risk.[94] The Fifth Circuit concluded that annuities are insurance and therefore, § 92 prohibits the sale of annuities in cities with more than 5000 persons.[95]

The Fifth Circuit rejected the OCC's argument that, under *Heimann*, § 92 only applies to broad insurance activities[96] by stating that this distinction would require courts to create an arbitrary distinction between general and specialized insurance products.[97] According to the Fifth Circuit, giving banks the power to sell insurance under § 24(7) would render § 92 superfluous.[98] Moreover, the court reasoned that *Heimann* did not

---

91. *Id.* at 1300-01

92. *Id.* at 1306.

93. *Id.* at 1301. The court reasoned that "[a]n annuity contract is the *exact inverse* of a life insurance contract." *Id.* (emphasis added). By "exact inverse," the court refers to the typical payment structure of annuities and life insurance policies. *See id.* In exchange for periodic payments, a life insurance contract provides a lump sum upon the death of the insured. *Id.* An annuity provides an annuitant periodic payments in exchange for a lump sum. *Id.* Although accurate, life insurance and annuity contracts offer other payment structures as well. *See* OCC Interpretive Letter No. 499, [1989-1990 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,090 (Feb. 12, 1990).

94. *VALIC*, 998 F.2d at 1301. Both life insurance and annuities transfer the economic risk of death from the policyholder or annuitant to the insurance company. *Id.* Life insurance protects the insured from premature death, and an annuity protects the annuitant from outliving forecasted mortality. *Id.*

95. *Id.*

96. *Id.* The OCC argued that even if annuities are insurance products, the *Saxon* construction of § 92 only applies to "general" types of insurance. *Id. Saxon* reversed an OCC ruling which allowed a national bank to sell "broad forms of automobile, home, casualty and liability insurance." *See* Saxon v. Georgia Ass'n of Indep. Ins. Agents, 399 F.2d 1010, 1012 (5th Cir. 1968); *supra* notes 58-61 and accompanying text (discussing *Saxon*). According to the OCC, annuities are a specialized insurance product to which *Saxon* does not apply. *VALIC*, 998 F.2d at 1301-02. Furthermore, the OCC contended that annuities are analogous to credit life insurance which *Heimann* held national banks were permitted to sell. *Id.* at 1302.

97. *VALIC*, 998 F.2d at 1302. The court also noted that the Second Circuit dismissed the same argument in *American Land Title Ass'n v. Clarke*, 968 F.2d 150, 156-57 (2d Cir. 1992). *VALIC*, 998 F.2d at 1302; *see supra* notes 71-74 and accompanying text (discussing *American Land Title Ass'n v. Clarke*). The court noted that annuities are no less a "general" type of insurance than land title insurance. *VALIC*, 998 F.2d at 1302.

98. *VALIC*, 998 F.2d at 1303. As such, § 92 reflects Congress's understanding that national banks did not have incidental powers to sell insurance under

apply because, unlike credit life insurance, selling annuities is not closely related to the business of banking.[99]

The Fifth Circuit concluded that *Saxon* compelled its decision in *VALIC*.[100] Since 1968 Congress has not modified the *Saxon* construction of § 92.[101] The court admonished national banks for seeking more power than that granted by statute and recommended that banks "look to Congress, not the Comptroller . . . or the courts" to expand insurance powers.[102] Thus, the Fifth Circuit reversed the district court and held that the OCC decision allowing NCNB to sell annuities in towns with more than 5000 persons violated 12 U.S.C. § 92.[103]

III. A NEW VIEW ON ANNUITIES AND NATIONAL BANK INSURANCE POWERS

VALIC represents a major set-back for the banking industry's push into insurance markets. *VALIC* not only restricts certain national banks from participating in the billion dollar annuity market,[104] but also reflects an unduly narrow interpretation of national bank insurance powers.[105] In addition, *VALIC* jeopardizes the relationship established by *Chevron* between federal courts and administrative agencies.[106] Bank agency de-

§ 24(7). *Id.* The Fifth Circuit additionally stated that even if selling annuities is incidental to banking, selling annuities is not "necessary." *Id.* at 1302. Section 24(7) provides, in part, that national banks shall have "all such incidental powers as shall be necessary to carry on the business of banking." 12 U.S.C. § 24(7) (1988).

99. *VALIC*, 998 F.2d at 1302. Both the Fifth and Second Circuits view national banks selling credit life insurance as simply charging a higher price for the loan. *Id.* In addition, the Fifth Circuit noted that notwithstanding the general grant of power in § 24(7), the § 92 limitation controls. *Id.*

100. *Id.*

101. *Id.* at 1303.

102. *Id.* (quoting *Saxon*, 399 F.2d at 1021 (Thornberry, J., concurring)).

103. *Id.*

104. *See supra* note 1 (noting magnitude of the income generated by national banks from sale of annuities). The decision does not presently affect national bank annuity sales outside the Fifth Circuit. Robert M. Garsson, *Courts Slam Lid on Annuity Sales in Texas, Louisiana, Mississippi*, AM. BANKER, Aug. 31, 1993, at 2 (quoting Ronald Glancz).

105. One commentator notes, "[t]he way the decision is written, it seems to me that taking the case to the Supreme Court will be a win or lose all decision." *IBAA Breaks Ranks on Insurance*, AM. BANKER Sept. 6, 1993, at 8 (quoting an unidentified banking industry lawyer). *But see supra* note 8 (discussing likelihood that OCC will seek review by Supreme Court based on manner its petition for rehearing *en banc* was rejected). Michael F. Crotty of the American Bankers Association noted that the court took a "parsimonious view of incidental powers." *See* Garsson, *supra* note 104, at 2.

106. *See supra* notes 35-42 and accompanying text (discussing judicial defer-

cisions now lack finality, and reliance on regulatory approval by banks may be costly.[107]

A. Annuity Contracts Are Not Insurance Under 12 U.S.C. § 92

The Fifth Circuit stated that it "must determine the applicability [*or inapplicability*] of § 92 to the sale of annuities."[108] Section 92 only applies if annuities are insurance. The Fifth Circuit, therefore, should have begun its analysis by asking whether annuities are insurance. Instead, the Fifth Circuit first upheld the *Saxon* construction of § 92 and then addressed whether annuities are insurance.[109] The court's approach requires a finding that annuities are insurance: otherwise the initial analysis of § 92 becomes irrelevant dictum.

Noting the ambiguity in § 92, the district court correctly observed that "[b]ecause § 92 is silent with respect to defining the term 'insurance,' the court must defer to any reasonable interpretation by the Comptroller on that issue."[110] Congress did not define "insurance" in § 92.[111] In addition, the legislative record does not indicate the products or activities to be included by the term "insurance."[112] The OCC determined that annuities are

---

ence to administrative agency statutory interpretations). Although the Fifth Circuit claimed to apply the *Chevron* standard of review in determining the scope of § 92, the court ignored *Chevron* when reviewing the OCC's interpretation that annuities are not "insurance" under § 92. *VALIC*, 998 F.2d at 1300-01.

107. Banks rely on the fee income annuity sales generate. *See* Karen Talley, *NEWS ANALYSIS: Courts Leave Banks in Limbo On Right to Market Annuities*, Am. Banker Sept. 28, 1993, at 12. According to Michael F. Crotty, deputy general counsel with the American Bankers Association, "[w]e wish all this would get straightened out so we know what we are doing." *Id.* Until the legal issues are resolved, some banks will utilize outside marketing firms to sell annuities in their branches. *Id.* National banks may enter percentage leases with insurance agents pursuant to a 1983 OCC opinion. *See* OCC Interpretive Letter No. 274, [1983-1984 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,434 (Dec. 2, 1983). Under this alternative approach, however, banks must share fee income. *See* Talley, *supra*, at 12. Furthermore, many of the outside marketing firms fear that *VALIC* jeopardizes all annuity sales in national banks. *Id.*

108. *VALIC*, 998 F.2d at 1298.

109. *See id.* at 1298-1300.

110. Variable Annuity Life Ins. Co. v. Clarke, 786 F. Supp. 639, 641 (S.D. Tex. 1991).

111. *See* 12 U.S.C. § 92 (1988) (omitted since 1952).

112. *See* 53 Cong. Rec. 11,001 (1916) (Letter of Comptroller Williams proposing legislation). Comptroller Williams stated that Congress should permit national banks " to act as agents for insurance companies in the placing of policies of insurance - fire, life, etc. . . ." in towns with fewer than 3000 persons. *Id.* The letter did not mention the sale of annuities. *See id.*

not "insurance" under § 92.[113] Thus, the Fifth Circuit should have reviewed the OCC interpretation under the second step of *Chevron* to determine whether this is a "permissible construction."[114]

Courts and commentators widely recognize annuities as an investment vehicle clearly different from insurance.[115] Insurance involves a different form of risk than annuities.[116] The issuer of an insurance contract bears an immediate risk of indemnifying a loss.[117] Annuity contracts, however, create no immediate risk for the issuer.[118] Instead, the investor bears the risk of not realizing future income.[119] The Fifth Circuit concluded that annuities are insurance because of this "mirror image" inverse relationship.[120] The court's counter-intuitive conclusion contradicts general authority.[121]

In addition, annuities and life insurance serve different pur-

113. *See supra* note 79 and accompanying text.

114. *See* Chevron U.S.A., Inc. v. Natural Resources Defense Council, 467 U.S. 837, 843 (1984).

115. "Ordinarily, it is recognized, *even by laymen*, that contracts of life insurance and of annuity are *distinctly different*." APPLEMAN, *supra* note 2, at 295 (emphasis added). Apparently, this distinction escaped the Fifth Circuit. *See* Chatham County Hosp. Auth. v. John Hancock Mut. Life Ins. Co., 325 F. Supp. 614, 617 (D. Ga. 1971) (finding that "annuities are 'essentially a form of investment' and that the contingency of continuance of life does 'not bring it within the classification of insurance'") (quoting Wolfe v. Breman, 26 S.E.2d 633, 637 (Ga. 1943)); 3A C.J.S. *Annuities* § 3 (1973) (noting that "an annuity contract differs from an insurance contract, and it comprehends few of the elements of an insurance contract").

116. *See Chatham County Hosp. Auth.*, 325 F. Supp. at 617; APPLEMAN, *supra* note 2, at 295; 3A C.J.S. *Annuities* § 3 (1973); *see also* SEC v. Variable Annuity Life Ins. Co., 359 U.S. 65, 71 (1959) (concluding that annuities offer a different form of risk than insurance).

117. *See* APPLEMAN, *supra* note 2, at 295 (noting "there is an immediate hazard of loss thrown upon the issuer . . ."); 3A C.J.S. *Annuities* § 3 (1973) (stating that "insurance, as generally understood, is an agreement to indemnify against loss . . .").

118. *See* APPLEMAN, *supra* note 2, at 295 (noting that "the hazard of loss is no longer upon the company but upon the recipient . . .").

119. *Id.* In the case of variable annuities, future income is contingent on the investment performance of the underlying portfolio. *See supra* note 79 and accompanying text; *see also* SEC v. Variable Annuity Life Ins. Co., 359 U.S. at 71-72 (referring to variable annuities, the Court stated that "they guarantee nothing to the annuitant except an interest in a portfolio of common stocks or other equities"). Fixed annuities expose investors to the risk of future payments made in depreciated dollars. *See* SEC v. Variable Annuity Life Ins. Co., 359 U.S. at 70; APPLEMAN, *supra* note 2, at 285. Thus, annuities produce an investment risk, not an insurance risk. *See supra* note 79 and accompanying text.

120. *VALIC*, 998 F.2d at 1301.

121. *See supra* notes 79, 115-119 and accompanying text (discussing general authority that annuities are not insurance).

poses.[122] Life insurance distributes proceeds to a designated beneficiary upon the death of the insured.[123] Conversely, an annuity benefits the purchaser by providing contingent future income.[124] As such, annuities are generally regarded as investments rather than insurance.[125]

Furthermore, the annuity contracts that the OCC approved closely resemble other financial investment products that are not considered insurance.[126] Variable annuity contracts are functionally equivalent to shares in a mutual fund because payments to an annuitant depend entirely on the performance of the investment portfolio.[127] Fixed annuity contracts typically offer a guaranteed return, similar to a certificate of deposit (CD), and payments for a life term.[128] Other non-insurance instruments offer life interests in the income of an asset.[129] For example, banks can sell a CD with a life interest in the income,[130] or corporate bonds with annuity features, without violating § 92.[131]

---

122. *See Chatham County Hosp. Auth.*, 325 F. Supp. at 617 (concluding that "generally speaking, life insurance is a provision for death, while an annuity is a provision for life") (quoting Wolfe v. Breman, 26 S.E.2d 633, 638 (Ga. 1943)); APPLEMAN, *supra* note 2, at 295.

123. *See Chatham County Hosp. Auth.*, 325 F. Supp. at 617.

124. *See* APPLEMAN, *supra* note 2, at 285-299. Fixed annuities, introduced in the 1920s as a method of providing for retirement, became less desirable investments because of inflation. *Id.* at 285. Variable annuities allow the offeror to avoid paying annuitants in depreciated dollars when investment returns exceed inflation. *See* SEC v. Variable Annuity Life Ins. Co., 359 U.S. at 70.

125. SEC v. Variable Annuity Life Ins. Co., 359 U.S. at 709; *see* APPLEMAN, *supra* note 2, at 285-299. Insurance contemplates payment as a result of loss, such as loss of life, property, or health. In re New York State Ass'n of Life Underwriters, Inc. v. New York State Banking Dept., 598 N.Y.S.2d 824, 828 (N.Y. App.Div. 1993) [hereinafter *NY Annuity Case*]. Annuities contemplate a long-term income stream based on an initial payment. *Id.* The OCC analogized annuities to several common financial investments in its opinion. *See supra* note 79 and accompanying text.

126. *See supra* note 79 and accompanying text.

127. SEC v. United Benefit Life Ins. Co., 387 U.S. 202, 209-11 (1967); SEC v. Variable Annuity Life Ins. Co., 359 U.S. at 70-73; ROBERT POZEN, FINANCIAL INSTITUTIONS: INVESTMENT MANAGEMENT 550-55 (1978); *see supra* note 79 and accompanying text.

128. *See supra* note 79 and accompanying text.

129. *See supra* note 79 and accompanying text.

130. *See supra* note 79 and accompanying text.

131. National banks can broker securities without recourse under 12 U.S.C. § 24(7). *See* 12 U.S.C. § 24(7) (1988). A newly issued corporate bond paying interest in-kind (PIK) for several years before cash interest and principal becomes due resembles a fixed annuity for a fixed term. Similarly, perpetuity bonds function like fixed annuities. After *VALIC*, a national bank in the Fifth Circuit could sell the bonds, but not annuities.

The Fifth Circuit noted that, historically, annuities have been considered insurance products.[132] This historical perception of annuities results because insurance companies typically issue annuities and all fifty states regulate annuities under their insurance laws.[133] The court, however, ignored that several of these states allow their state-chartered banks to sell annuities.[134] Furthermore, federal law distinguishes annuities from insurance.[135]

Contrary to the Fifth Circuit's conclusion, insurance company products are not necessarily "insurance." Such a conclusion leads to an inappropriately intransigent classification of financial products considering today's dynamically changing financial markets.[136] Moreover, assuming that § 92 limits national bank insurance activities, the plain language applies only to "soliciting and selling *insurance* and collecting premiums on

132. *VALIC*, 998 F.2d at 1300 (quoting the 1990 OCC opinion approving the sale of fixed annuities by national banks).

133. *Id.*

134. *See, e.g., NY Annuity Case*, *supra* note 125, at 828 (holding that New York state-chartered banks may sell annuities as a permissible incident to the business of banking). The New York court concluded that, although the state's Insurance Law defines "annuity," and the Department of Insurance regulates annuity sales, an annuity is not insurance. *Id.* at 828; *see also* CONN. GEN. STAT. ANN. § 36-142 (West 1987 & Supp. 1993) (permitting state-chartered savings banks to establish insurance departments); IND. CODE ANN. § 28-1-11-2 (Burns 1993) (permitting state banks to solicit and write insurance as brokers for insurance companies); MASS. GEN. LAWS ANN. ch. 178, §§ 1-6 (Law. Co-op. 1987 & Supp. 1993) (permitting state-chartered banks to establish an insurance department and grant and sell annuities); Banks and Banking—Activities of State Chartered Banks, 43 Op. Att'y Gen. Mont. 293-95 (1990) (Montana Attorney General opines that state law permits state-chartered banks to directly market fixed annuities); Retirement Annuities, 1985 Op. Att'y Gen. S.D. 16 (1985) (South Dakota Attorney General opines that state law permits state-chartered banks to sell retirement annuities); CAPATIDES, *supra* note 50, at 249 (citing FDIC survey indicating that twenty-four states permit state-chartered banks or their subsidiaries to engage in general insurance agency and brokerage activities).

135. *See* SEC v. Variable Annuity Life Ins. Co., 395 U.S. at 69-73. The Supreme Court held that, under federal law, variable annuities are not insurance. *Id.* at 68-73.

136. The Fifth Circuit failed to recognize the blurring of lines between different segments of the financial services industry. *See NY Annuity Case*, *supra* note 125; *supra* notes 44-45 and accompanying text (discussing changes in the commercial banking industry). In the *NY Annuity Case*, the court correctly observed that "we should not close our minds to the well-known fact that the banking business in this country has developed rapidly during the last few years to meet the ever-growing demands of business. Banks *ex necessitate* have been required to extend their functions and perform services formerly foreign to the banking business." *NY Annuity Case*, *supra* note 125, at 827 (quoting Dyer v. Broadway Cent. Bank, 169 N.E. 635, 636 (N.Y. 1930)).

policies."[137] Thus, for § 92 to apply, the court must make a functional finding that annuities are "insurance," not simply insurance company products.

The Fifth Circuit reasoned that annuities are functionally equivalent to life insurance policies because both use actuarial calculations to price mortality risk.[138] Actuarial calculations of mortality risk are a common characteristic of annuities and life insurance, but not the touchstone of what constitutes insurance. Automobile and property insurance policies set premiums without reference to mortality tables, yet these products are still considered insurance. Actuarial calculations of mortality risk are a matter of form, not substance.[139] An annuity lacks the key substantive element of insurance: indemnification for catastrophic loss.[140]

A court must defer to a regulatory interpretation unless it is "arbitrary, capricious, or manifestly contrary to the statute."[141] The OCC determined that annuities are not "insurance" under § 92 because annuities lack the key element of insurance: indemnification for catastrophic loss.[142] The OCC substantiated its decision by further noting that annuities and life insurance involve different forms of risk.[143] Case law as well as prominent

137. 12 U.S.C. § 92 (1988) (omitted since 1952) (emphasis added).

138. *VALIC*, 998 F.2d at 1301.

139. *See* SEC v. Variable Annuity Life Ins. Co., 359 U.S. at 70-73. The Court noted that issuers of annuities assume mortality risk based on an "actuarial prognostication" of life expectancy. *Id.* at 70. Although mortality risk is an aspect of insurance, the Court noted that the insurance aspect of annuities created by mortality risk is "apparent, not real; superficial, not substantial." *Id.* at 70-71. The Court's reasoning applies equally to fixed annuities.

Other financial investments reflect assumptions of mortality risk, even if not actuarially calculated. Investors indirectly account for the risk of an officer's death (or departure) if the success of the company largely depends on that officer's management. In this situation, as with annuities, mortality risk constitutes a component of the investment price. The investment, however, does not become life insurance simply because mortality risk influenced the price.

140. *See supra* notes 79, 116-117, 122-123 and accompanying text (authority distinguishing annuities from insurance). According to the Supreme Court in *SEC v. Variable Annuity Life Ins. Co.*, insurance involves a "conventional concept of risk-bearing" that requires an issuer to assume an immediate risk of loss. 359 U.S. at 70-71. Neither fixed nor variable annuities create this risk for the issuer.

141. Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837, 844 (1984); *see supra* notes 35-42 and accompanying text (discussing *Chevron*).

142. *See supra* note 79 and accompanying text (discussing characteristics of annuities).

143. *See id.*

insurance law commentators support the OCC construction.[144] As the district court correctly held, *Chevron* requires deference to the OCC.[145] Oblivious to *Chevron*, the Fifth Circuit bluntly responded to the OCC's interpretation: "We disagree."[146] The Fifth Circuit erred by ignoring the *Chevron* standard of review and independently defining annuities.

B. 12 U.S.C. § 92 Creates No Limit on National Bank Insurance Powers

Notwithstanding the classification of annuities, § 92 imposes no limit on national bank insurance powers.[147] Although the Fifth Circuit's analysis of § 92 claims to follow *Chevron*, the court treated *Chevron* disingenuously. The Fifth Circuit implied Congress's "clear intent" under the *expressio unius* rule of statutory interpretation[148] and construed Congress's silence in § 92 as a *prohibition* on national bank insurance powers in cities with more than 5000 persons.[149] Congress, however, can only express its clear and unambiguous intent when it has *"directly spoken* to the *precise question* at issue."[150] Thus, courts should not rely on the *expressio unius* rule of statutory construction to

144. *See supra* notes 115-125 and accompanying text (citing cases and secondary sources distinguishing annuities from insurance).

145. Variable Annuity Life Ins. Co. v. Clarke, 786 F. Supp. 639, 642 (S.D. Tex. 1991), *rev'd*, 998 F.2d 1295 (5th Cir. 1993).

146. *VALIC*, 998 F.2d at 1300.

147. Three positions have evolved concerning national bank insurance powers under § 92. First, § 92 is the full extent of national bank insurance powers. *See* American Land Title Ass'n v. Clarke, 968 F.2d 150, 155 (2d Cir. 1992) (holding that the *expressio unius* rule leads to the conclusion that Congress intended to *prohibit* national banks located and doing business in towns with over 5000 persons from engaging in the insurance agency business); Saxon v. Georgia Ass'n of Indep. Ins. Agents, 399 F.2d 1010, 1014 (5th Cir. 1968) (reasoning that "since Congress dealt specifically with the insurance agency power in Section 92, the *expressio unius* [*est exclusio alterius*] rule negates the existence of any other power to act as an insurance agent under the general provisions of Section 24(7)"). Second, § 92 only restricts national banks from operating general insurance agencies in cities with more than 5000 persons; § 24(7) authorizes insurance activities incidental to commercial bank activities. *See* Independent Bankers Ass'n of Am. v. Heimann, 613 F.2d 1164, 1169-70 (D.C. Cir. 1979), *cert. denied*, 449 U.S. 823 (1980); *supra* notes 63-67 and accompanying text (discussing *Heimann*). Third, § 92 creates no limit on national bank insurance powers. *See* OCC Interpretive Letter No. 499, [1989-1990 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,090 (Feb. 12, 1990); Independent Ins. Agents of Am. v. Board of Governors of Fed. Reserve Sys., 736 F.2d 468, 477 n.6 (8th Cir. 1984); Variable Annuity Life Ins. Co. v. Clarke, 786 F.Supp. 639, 642 (S.D. Tex. 1991).

148. *See VALIC*, 998 F.2d at 1298.

149. *See id.* at 1300.

150. *Chevron*, 467 U.S. at 842 (emphasis added).

determine Congress's intent under the first step of *Chevron*.[151]

The Fifth Circuit asserted that the legislative record supports the *Saxon* § 92 construction.[152] The legislative record, however, consists only of Comptroller Williams' 1916 letter to Congress.[153] The letter cannot evidence Congress's intent because the Comptroller, not Congress, is speaking. Comptroller Williams' statement that insurance powers "should be limited to banks in small communities"[154] does not control when the statute is silent on this point. Had Congress agreed with the Comptroller, the statute itself would expressly limit national bank insurance powers to cities with less than 5000 persons. Furthermore, the Comptroller's letter indicates that the primary purpose of § 92 was to increase the revenue of small town banks which had difficulty meeting the minimum capital requirements under federal chartering laws.[155] Ironically, giving the Comptroller's statements controlling weight over the language Congress used in the statute accomplishes what the Fifth Circuit seeks to prevent: it allows the Comptroller to contravene Congress.[156]

---

151. Applying the *expressio unius* rule, a court reaches a conclusion by negative implication based on the language of the statute. *See supra* note 61 and accompanying text (discussing Fifth Circuit application of *expressio unius* rule). *Chevron*, however, holds that those things not "directly spoken to" by Congress create a delegation of legislative authority to the administrative agency. *Chevron*, 467 U.S. at 843-44; *see supra* notes 35-42 and accompanying text (discussing *Chevron*). When a court invokes the *expressio unius* rule, Congress necessarily has not "directly spoken." Thus, the *expressio unius* rule directly conflicts with the first step of *Chevron*.

152. *See VALIC*, 998 F.2d at 1298-99.

153. *See* 53 CONG. REC. 11,001 (1916); *see supra* note 89 and accompanying text (discussing the Fifth Circuit's use of Comptroller Williams' letter).

154. 53 CONG. REC. 11,001 (1916).

155. *See id.*; Independent Ins. Agents of Am. v. Board of Governors of Fed. Reserve Sys., 736 F.2d 468, 477 n.6 (8th Cir. 1984) (opining that "the legislative history [of § 92] indicates that Congress was concerned only with providing small-town banks with an additional profit source, not with prohibiting city banks from selling insurance"); Variable Annuity Life Ins. Co. v. Clarke, 786 F.Supp. 639, 641 (S.D. Tex. 1991) (opining that "the legislative history of § 92 indicates that it was proposed to provide an additional source of revenue for national banks located in small towns and not to protect the markets from competing insurance agents"); *cf.* American Land Title Ass'n v. Clarke, 968 F.2d 150, 156 (2d Cir. 1992) (quoting parts of the Comptroller's letter indicating that national banks did not have insurance powers before Congress enacted 12 U.S.C. § 92); Saxon v. Georgia Ass'n of Indep. Ins. Agents, Inc., 399 F.2d 1010, 1015 (5th Cir. 1968) (interpreting the Comptroller's letter to mean that national bank insurance powers are limited to cities with less than 5000 persons).

156. *See supra* text accompanying note 102 (noting the Fifth Circuit's assertion that national banks should look to Congress, not the OCC, or the courts, for expanded insurance powers).

The Fifth Circuit further contended that *Chevron* does not entitle the OCC to overrule the judicial precedent established by *Saxon*.[157] In *Lechmere, Inc. v. NLRB*,[158] the Supreme Court noted that *stare decisis* prevents an agency's interpretation from overriding the Court's construction of a statute.[159] The Fifth Circuit misplaces its reliance on *Lechmere* because the Supreme Court has not interpreted the substantive meaning of § 92.[160] Furthermore, *Saxon* is not entitled to precedential weight under the doctrine of *stare decisis*.[161] The Fifth Circuit decided *Saxon* prior to *Chevron*,[162] and subsequently, the Eighth[163] and D.C. Circuits[164] have disagreed with the *Saxon* construction of § 92.

Section 92, by its plain language, creates no limitation on national bank insurance powers.[165] An interpretation consistent with the plain language of the statute is not "arbitrary, capricious, or manifestly contrary to the statute" under the second step of *Chevron*.[166] The OCC construction that § 92 imposes no

157. *VALIC*, 998 F.2d at 1300 (citing Lechmere, Inc. v. NLRB, 112 S. Ct. 841, 847-48 (1992); BPS Guard Services, Inc. v. NLRB, 942 F.2d 519, 523 (8th Cir. 1991)).

158. 112 S. Ct. 841 (1992).

159. *Id.* at 847-48 (citing Maislin Industries, U.S., Inc. v. Primary Steel, Inc., 110 S. Ct. 2759, 2768 (1990)).

160. *See supra* notes 5, 56 and accompanying text (discussing failure of Supreme Court to interpret substantive scope of 12 U.S.C. § 92 in *United States Nat'l Bank v. Independent Ins. Agents of Am.*).

161. The Fifth Circuit decided *Saxon* assuming that a court's interpretation of a statute may supersede an administrative agency's interpretation. *See* 399 F.2d. at 1015. In *Saxon*, the court independently interpreted § 92 without regard to the OCC's construction. *Id.* Under *Chevron*, a court cannot reach an interpretation on its own, or even a better interpretation of the statute. *See Chevron*, 467 U.S. at 843-44; *supra* notes 35-42 and accompanying text (discussing *Chevron*). Thus, *Saxon* does not provide a valid construction of § 92 because the court did not conform to the standard of judicial review *Chevron* established.

162. The Fifth Circuit also relied on BPS Guard Services, Inc. v. NLRB, 942 F.2d 519 (8th Cir. 1991), to support its argument that *Chevron* does not entitle an administrative agency to overrule judicial precedent. *VALIC*, 998 F.2d at 1300. In *BPS Guard Services*, however, the agency's original interpretation was reviewed under *Chevron*. *See* 942 F.2d at 523-24. Conversely, in *Saxon*, the OCC construction of § 92 was not reviewed under *Chevron*. Thus, *Saxon* should not govern the Fifth Circuit's decision or the OCC interpretation.

163. *See* Independent Ins. Agents of Am. v. Board of Governors of Fed. Reserve Sys., 736 F.2d 468, 477 n.6 (8th Cir. 1984).

164. *See* Independent Bankers Ass'n of Am. v. Heimann, 613 F.2d 1164, 1170 (D.C. Cir. 1979).

165. *See supra* notes 5, 55 and accompanying text (quoting language of § 92).

166. *See Chevron*, 467 U.S. at 844; *see also supra* note 38 and accompanying text (describing *Chevron*'s two-step analysis).

limit on national bank insurance powers is a permissible construction and warrants deference under *Chevron*.

C. THE *VALIC* CONSTRUCTION OF 12 U.S.C. § 92 IS INCONSISTENT WITH EXISTING NATIONAL BANK INSURANCE POWERS

The Fifth Circuit erred by relying on *Saxon* because the *Saxon* construction of § 92 conflicts with more recent decisions concerning national bank insurance powers. *Heimann* holds that § 92 does not limit national bank insurance activities incidental to the business of banking.[167] The Fifth Circuit attempted to reconcile *Heimann* with the *Saxon* construction of § 92 by implying that credit life insurance may not be "insurance" under § 92 because it amounts to simply charging a higher price on the underlying loan.[168] Credit life insurance, however, does not differ in form, or substance, from traditional life insurance policies.[169] Credit life insurance provides health, accident, or life insurance coverage to protect a borrower's debt obligation in the event of a casualty.[170] Credit life insurance indemnifies an insured's loss, a principal characteristic of insurance,[171] and entails pricing mortality risk, the court's primary reason for holding that annuities are insurance.[172] Furthermore, the

167. *See supra* notes 63-67 and accompanying text (discussing *Heimann*). In addition, the Eighth Circuit avoided the *Saxon* construction of § 92. *See supra* note 69 and accompanying text. Furthermore, after *Independent Ins. Agents of Am., Inc. v. Ludwig*, § 92 no longer places any practical limitation on national bank insurance powers. *See supra* notes 76-77 and accompanying text (discussing *Ludwig*). Although *Ludwig* provides national banks with the legal authority to market insurance products into larger cities from a small town branch, in practice, this is inconvenient and inefficient. *See supra* notes 75-79 and accompanying text (discussing *Ludwig*).

168. *VALIC*, 998 F.2d at 1302. The Fifth Circuit also relied on the Second Circuit's distinction that credit life insurance only protects the lender's interest. *Id.* (citing American Land Title Ass'n v. Clarke, 968 F.2d 150, 157 (2d Cir. 1992)). The Second Circuit concluded that title insurance protects the lender's *and* the borrower's interest. American Land Title Ass'n v. Clarke, 968 F.2d at 157.

The Second Circuit is incorrect. Credit life insurance protects the borrower's interest. If the borrower dies, or the prescribed event occurs for which the insurance applies, credit life insurance protects the borrower from a claim for repayment of the debt. *See Heimann*, 613 F.2d at 1168. The Second Circuit's reasoning, with which the Fifth Circuit agreed in *VALIC*, unreasonably contends that borrowers will pay for something that provides no benefit.

169. *See Heimann*, 613 F.2d at 1168 n.9.

170. *See id.*

171. *See supra* notes 116-117 and accompanying text (discussing characteristics of insurance).

172. *See supra* note 94 and accompanying text (discussing the Fifth Circuit's

court's rationale that credit life insurance is simply a bank's method of charging a higher price for the loan fails to recognize that federal statutory law prohibits "tying arrangements."[173]

Credit life insurance is "insurance" under § 92. The Fifth Circuit's construction of § 92 therefore directly conflicts with *Heimann*. The court attempted to distinguish *Heimann* on the basis that credit life insurance is "intimately related to the bank's primary business of lending."[174] Similarly, selling annuities is "intimately related" to the bank's primary business of offering financial products to customers. The Fifth Circuit, however, disagreed and stated that "annuities have nothing to do with the primary business of banking."[175] This statement ignores the expansion of commercial bank activities, i.e., the "business of banking," that has transpired over the past twenty years.[176]

Notwithstanding the Fifth Circuit's narrow interpretation of the "business of banking," the court seemingly created an exception to the *Saxon* construction of § 92 by stating that banks may sell insurance products "intimately related to the business of banking" without violating § 92.[177] Earlier in its opinion, however, the court rejected the OCC's argument that *Heimann* limits *Saxon* to only "broad forms" of insurance.[178] Thus, *VALIC* confuses, rather than clarifies, the meaning of § 92.

---

reasoning for holding that annuities are insurance). The Fifth Circuit did not address the fact that credit life insurance transfers a direct economic risk of death to the issuer, whereas an annuity only transfers an indirect risk of death (i.e., risk of living).

173. *See* 12 U.S.C. § 1972 (1988). A tying occurs when the bank directly or indirectly forces borrowers to purchase other bank products as a condition for receiving credit. *See* LITAN, *supra* note 14, at 131. If a national bank required a borrower to purchase credit life insurance as a condition for receiving a loan, then the court's argument would have merit. The court ignores, however, that under federal law, selling the insurance policy must be a distinct transaction from tendering the loan. *See* 12 U.S.C. § 1972 (1988). Thus, credit life insurance does not constitute charging a higher price on the underlying loan.

174. *See VALIC*, 998 F.2d at 1302.

175. *Id.*

176. *See NY Annuity Case*, *supra* note 125, at 828.

> Quite plainly, in order to properly interpret the very amorphous phrase "incidental powers" necessary to carry on the "business of banking", special expertise is required encompassing a comprehensive understanding of the evolvement of banking, the nature and extent of present practices, and the need for and legitimacy of added banking services in light of present day business technology and customer needs.

Id.

177. *VALIC*, 998 F.2d at 1302.

178. *Id.* at 1301-02.

D. Consequences of the OCC Construction of 12 U.S.C. § 92

The OCC construction of § 92 imposes no limitation on national bank insurance activities.[179] The structural soundness of the overall U.S. banking system should benefit from allowing banks to sell insurance.[180] Commercial banks can reduce systemic risk through product line diversification.[181] Diversification allows an institution to smooth earnings fluctuations from deposit taking and lending[182] and derive cost savings through economies of scope.[183]

Assuming OCC approval, American consumers could substantially benefit if commercial banks sold various forms of insurance. Commercial banks could become "financial supermarkets" offering "one-stop" shopping for depository, consumer and commercial credit, capital market, and insurance products and services.[184] In addition to convenience, increased competition in the sale of insurance would result in estimated cost savings to American consumers of five to seven billion dollars.[185]

Permitting national banks to sell insurance does not infringe upon the overriding banking policy objective of maintaining the "safety and soundness" of the banking system.[186] Congress believed that commercial bank securities activities principally caused the banking crisis of the 1930s, and legislation targeted securities as the primary area of product line regulation.[187] By 1990, however, bank agencies, along with judicial acquiescence, eliminated many of the Glass-Steagall investment banking restrictions imposed on commercial banks.[188] Thus, maintaining the separation between insurance and banking is

179. *See supra* note 79 and accompanying text (discussing OCC interpretation of § 92).

180. *See* Litan, *supra* note 14, at 60-118. This assumes that the OCC approves a national bank's application to sell insurance under 12 U.S.C. § 24(7).

181. *Id.*

182. *Id.* at 104-05.

183. *Id.* at 74-81.

184. *See* Capatides, *supra* note 50, at 244.

185. *See supra* note 49 and accompanying text (noting benefits associated with banks' expansion into non-traditional financial products).

186. *See supra* notes 25-27 and accompanying text (discussing safety and soundness rationale for regulating the banking industry).

187. *See supra* notes 28-31 and accompanying text (discussing Depression-era legislation).

188. *See supra* notes 46-48 and accompanying text (discussing deregulation of commercial banks).

inconsistent with, and inappropriate in light of, the expanded securities powers of commercial banks.

CONCLUSION

The Fifth Circuit's decision in *VALIC* defied the framework for judicial review established in *Chevron*. The OCC determined that 12 U.S.C. § 92 does not apply to the sale of annuities because annuities are not insurance, and even if they are, § 92 does not impose a limit on national bank insurance activities. Because Congress did not directly express an intent to limit national bank insurance activities in § 92, the Fifth Circuit should have reviewed the OCC opinion under the second step of *Chevron*. The OCC interpretation that § 92 does not limit national bank insurance activities accords with the plain language of the statute and is therefore a permissible construction under *Chevron*.

The Fifth Circuit did not need to address the substantive scope of § 92 in *VALIC* because annuities are not insurance. Section 92 does not define insurance which, according to *Chevron*, creates a delegation of legislative authority to the OCC to determine which products constitute insurance. Under *Chevron*, the court should have deferred to the OCC interpretation that annuities are not insurance. The Fifth Circuit, however, erroneously ignored *Chevron* and simply asserted its own opinion that annuities are insurance and within § 92.

The Fifth Circuit's narrow view of permissible bank activities is particularly inappropriate in light of today's complex financial markets. Empirically, commercial banks have suffered from rigid product line restrictions. As a result, bank regulators virtually eliminated the Glass-Steagall separation of investment banking and commercial banking during the 1980s. The Fifth Circuit's bright line dividing commercial banks and insurance, without statutory support, is not only ill-advised, but inconsistent with the policy of creating a level playing field for commercial banks.