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# CASE DIGEST

by MICHAEL D. SCOTT\*

The materials in this section are intended to provide a concise overview of the case law which has developed in the electronic funds transfer area. Each case is summarized in a separate digest entry. Each digest entry contains the following information:

- case name
- case citation
- subsequent history (if any)
- summary of salient facts
- legal analysis and holding of the court

The digest entries are arranged alphabetically by case name.

**EFT-1** American Bankers Association v. Connell, FED. BANKING L. REP (CCH), ¶ 97,785, at 83,547 (D.C. Cir. 1979), *cert. denied*, — U.S. — (1979).

This was the consolidation of three different cases. *Connell* involved credit unions and “share drafts”; *Independent Bankers Association of America v. Federal Home Loan Bank Board* concerned savings and loan associations and “remote service units”; while *United States League of Savings and Loan Associations v. Board of Governors, Federal Reserve System* considered commercial banks and “automatic funds transfers.”

The court, in an unpublished opinion, held that regulations issued by the Federal Reserve Board,<sup>1</sup> Federal Home Loan Bank Board,<sup>2</sup> and National Credit Union Administration<sup>3</sup> violated 12 U.S.C. § 371a,<sup>4</sup> Section 5 of the Home Owners’ Loan Act of 1933,<sup>5</sup>

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1. 43 Fed. Reg. 20,001 (1978), *to be codified in* 12 C.F.R. § 217.5(c)(2) & (3).

2. 12 C.F.R. § 545.4-2 (1978).

3. *Id.* § 701.34 (1978).

4. The court also noted that the automated funds transfer system authorized by the Federal Deposit Insurance Corporation in 43 Fed. Reg. 20,222 (1978), *to be codified in* 12 C.F.R. § 329.5(c)(2), violated 12 U.S.C. § 1828(g) (1976). FED. BANKING L. REP. (CCH), ¶ 97,785, at 83,547 n.1.

and provisions of the Federal Credit Union Act,<sup>6</sup> respectively.

While recognizing the impact that its decision would have on the financial community as a whole, the court felt that it had no choice under current statutes, and indicated its expectation "that Congress will speedily review the overall situations and make such policy judgments as in its wisdom it deems necessary . . . ."<sup>7</sup>

**EFT-2 Bloomfield Federal Savings & Loan Association v. American Community Stores Corp., 396 F. Supp. 384 (D. Neb. 1975).**

Plaintiff, a federal savings and loan association, filed suit against defendants American Community Stores Corp., d/b/a/ Hinky Dinky, and the Federal Home Loan Bank Board ("FHLBB"), challenging a regulation that authorized federally chartered savings and loan associations to install and operate electronic funds transfer systems.<sup>8</sup> Under that regulation, First Federal Savings & Loan Association of Lincoln, Nebraska, had opened a remote service unit ("RSU")<sup>9</sup> at an Hinky Dinky supermarket. Plaintiff claimed that the regulation in issue violated Section 5 of the Home Owners' Loan Act of 1933.<sup>10</sup>

Addressing the question of whether Hinky dinky was transacting banking business by using the RSU, the court stated:

Critical to the analysis of these transactions is the judicial recognition that the element of a debtor and creditor essential to any deposit or withdrawal of funds never exists between the store and the customer-depositor. The "customer" is transacting business with First Federal Savings & Loan Association of Lincoln through the use of a computer terminal in the store, and the actions of the store facilitate that transaction. The computer terminal is the conduit for the *relay of information* to a central computer at First Federal. The transactions are electronically effected and perfected by the computer on the records and premises of First Federal. At no time does

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5. 12 U.S.C. § 1464(b)(1) (1976).

6. *Id.* §§ 1751-90 (1976).

7. FED. BANKING L. REP. (CCH), ¶ 97,785, at 83,548.

8. 12 C.F.R. § 545.4-2 (1974).

9. 12 U.S.C. § 1464 (1970).

10. The term "remote service unit" means an *information processing* device, including associated equipment, structures, and systems, by means of which information relating to financial services rendered to the public is stored and transmitted, whether instantaneously or otherwise, to a financial institution and which, for activation and account or deposit access, is dependent upon the use of a machine-readable instrument in the possession and control of the holder of such account or deposit. The term "remote service unit" includes, without limitation, both "on-line" computer terminals and "off-line" cash dispensing machines, but does not include terminals or teller machines using passbooks regardless of whether the passbooks are machine-readable.

396 F. Supp. at 387 n.2; emphasis in original.

First Federal have possession or ownership of any cash or funds physically transferred on the store premises between the store and the customer. The store is the financial and operational medium between the "customer" and First Federal.<sup>11</sup>

Turning then to the basic issue of the FHLBB's authority, the court concluded that:

The Board, in allowing limited experimentation in the field of "electronic funds transfer systems," was neither operating beyond the scope of its authority nor in an arbitrary and capricious manner, but, rather, was adopting new regulations in the area statutorily committed to the exclusive discretion of the Board by "which people may invest their funds and in order to provide for the financing of homes."<sup>12</sup>

The court held that the utilization of the RSU was "not the functional equivalent of a check or negotiable instrument, but rather . . . functionally equivalent to a deposit or withdrawal slip."<sup>13</sup>

On the issue of whether the terminal constituted a "branch," the court reasoned that the National Bank Act<sup>14</sup> applied only to national banks, and that Congress had not defined "branching" in the area of federal savings and loan associations, but had left that task to the FHLBB.<sup>15</sup> The FHLBB had defined a branch to be a "full-time and permanent office at which *any business* of a federal association may be transacted."<sup>16</sup> Noting that the regulation in question prohibited the use of an RSU "for opening savings accounts or deposits, or for the origination, processing or approval of any loans,"<sup>17</sup> the court concluded that the RSU was not a branch.

**EFT-3** Colorado *ex rel.* State Banking Board v. First National Bank of Ft. Collins, 540 F.2d 497 (10th Cir. 1976), *aff'g in part and rev'g in part*, 394 F. Supp. 979 (D. Colo. 1975), *cert. denied*, 429 U.S. 1097 (1977).

The First National Bank of Ft. Collins ("Bank"), a national bank, acting pursuant to a Comptroller of the Currency's interpretive ruling,<sup>18</sup> installed a customer-bank communications terminal ("CBCT") in a shopping center two miles from its offices. In its ruling, the Comptroller declared that "the use of such devices at loca-

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11. *Id.* at 387-88; emphasis in original.

12. *Id.* at 388.

13. *Id.*

14. 12 U.S.C. § 36(c) (1970).

15. 396 F. Supp. at 389.

16. 12 C.F.R. § 545.14 (1974); emphasis in original.

17. 396 F. Supp. at 389.

18. 12 C.F.R. § 7.7491 (1974).

tions other than the main office did not constitute branch banking."<sup>19</sup>

Using these terminals, customers could deposit funds, withdraw pre-packaged currency, debit their checking or savings accounts or charge it to a designated credit card, or transfer funds from savings to checking or vice versa.<sup>20</sup>

The State of Colorado expressly prohibits branch banking.<sup>21</sup> The State therefore filed a complaint against both the Bank and the Comptroller, claiming that the Bank was engaging in branch banking in violation of both state and federal laws. The trial court concluded that the receipt of deposits violated 12 U.S.C. § 36(f), but that the other functions did not. Both sides appealed.

The appellate court, relying on recent decisions in *Independent Bankers Association of America v. Smith*<sup>22</sup> and *Illinois ex rel. Lignoul v. Continental Illinois Bank & Trust Co.*,<sup>23</sup> held that all three functions violated 12 U.S.C. § 36. Citing the "competitive equality" language of Chief Justice Burger in *First National Bank of Logan v. Walker Bank & Trust Co.*,<sup>24</sup> the court concluded that:

Colorado law on branch banking precludes a state bank from maintaining off premises a machine of the type here sought to be used by the Bank. Accordingly, as concerns the use of off-premises CBCT's, we are by this opinion maintaining competitive equality in Colorado.<sup>25</sup>

EFT-4 *First National Bank in Plant City, Florida v. Dickinson*, 396 U.S. 122 (1969).

Petitioner, a national bank, brought a declaratory relief action against the State Comptroller of Florida to determine whether or not its armored car messenger service and off-premises deposit receptacle could be prohibited by state law.

Florida law prohibited all branch banking by state chartered banks.<sup>26</sup> The Comptroller of the Currency issued two letters authorizing the armored car messenger service<sup>27</sup> and the off-premises re-

19. 540 F.2d at 498.

20. COLO. REV. STAT. 11-6-101(1) (1973).

21. 540 F.2d at 498.

22. 534 F.2d 921 (D.C. Cir. 1976), *cert. denied*, 429 U.S. 862 (1976). See Case EFT-8 *infra*.

23. 536 F.2d 176 (7th Cir. 1976), *cert. denied*, 429 U.S. 862 (1976). See Case EFT-6 *infra*.

24. 385 U.S. 252 (1966). See Case EFT-5 *infra*.

25. 540 F.2d at 500.

26. FLA. STAT. § 659.06(1)(a) (1965).

27. The Comptroller relied upon COMPTROLLER'S MANUAL FOR NATIONAL BANKS ¶ 7490, for its authority.

ceptacle. Both letters indicated that all deposits would not become bank liabilities until actually in the hands of a teller at the "banking house," and that any checks cashed by the messenger would be deemed paid at the bank.<sup>28</sup>

The armored car service was arranged by contract between the bank and the customer. The contract specified that the messenger was the agent of the customer. The transmittal slip and a sign at the off-premise receptacle both recited that the messenger who collected the funds acted as the agent for the customer and that the funds would not be deemed deposited until delivered at the bank's premises.

The State Comptroller notified Petitioner that both of these services violated the prohibitions of Florida law against branch banking. The district court granted judgment for Petitioner,<sup>29</sup> and the Court of Appeals reversed.<sup>30</sup> The United States Supreme Court affirmed.

The Court first noted that under Section 7 of the McFadden Act,<sup>31</sup> a national bank may establish a branch "only when, where, and how state law would authorize a state bank to establish and operate such a bank,"<sup>32</sup> and that Florida allowed *no* branching of any kind. The question presented was then stated as "whether the activities of First National authorized by the United States Comptroller are branch banking."<sup>33</sup>

Relying on a broad interpretation of the term "branch" as defined in the McFadden Act,<sup>34</sup> the Court had no difficulty finding that both services constituted branch banking. Rejecting the notion that a state's definition of "branch banking" should be controlling, Chief Justice Burger first noted that the term branch bank, as used in the Act, "at the very least includes *any* place for receiving deposits or paying checks or lending money apart from the chartered premises."<sup>35</sup> Since the definition is in the disjunctive form, the Court found that the offering of any one of these three services is sufficient for branch banking.<sup>36</sup>

The Court focused solely on the question of whether deposits were received by the messenger or at the receptacle. The Court held

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28. 396 U.S. at 126.

29. 274 F. Supp. 449 (N.D. Fla. 1967).

30. 400 F.2d 548 (5th Cir. 1968).

31. 12 U.S.C. § 36.

32. 396 U.S. at 130.

33. *Id.* at 131.

34. 12 U.S.C. § 36(f); emphasis in opinion.

35. *Id.* at 135.

36. *Id.*

that whatever binding effect the terms of the contract between the parties concerning the place of deposit might have on the respective rights of the parties themselves, those terms were irrelevant in determining the meaning of the definition of branch banking in the Act.

Relying on the policy of "competitive equality" recognized in *First National Bank of Logan v. Walker Bank & Trust Co.*<sup>37</sup> the Court found a competitive advantage for "a bank that provides a service of receiving money for deposit at a place away from its main office."<sup>38</sup> Hence, the activities in question violated the McFadden Act and would be enjoined.

EFT-5 *First National Bank of Logan v. Walker Bank & Trust Co.*,  
385 U.S. 252 (1966).

Three actions were consolidated for hearing before the United States Supreme Court. All involved the construction of 12 U.S.C. § 36(c), which authorized a national bank, with the approval of the Comptroller of the Currency, "to establish and operate branches within the limits of the municipality in which the bank is located, if such operation is 'at the time authorized to State Banks by the law of the State in question.'"<sup>39</sup>

The two banks in issue sought to open new branches in municipalities in which their main offices were located. Utah law prohibited Utah state banks generally from establishing branches except by taking over an existing bank which had been in operation for not less than five years.<sup>40</sup>

The Court provided an historical background of the branch banking language in the McFadden Act,<sup>41</sup> and concluded that Congress intended, by the Act, "to place national and state banks on a basis of 'competitive equality' insofar as branch banking was concerned."<sup>42</sup> The Court concluded that the restriction in Utah law which prevented branching except for bank takeovers, was also applicable to national banks situated in Utah.

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37. 385 U.S. 252, 261 (1966). See Case EFT-5 *infra*.

38. 396 U.S. at 137.

39. 385 U.S. at 253.

40. UTAH CODE ANN., tit. 7, c. 3, § 6 (1965 Supp.).

41. 12 U.S.C. § 36(c).

42. 385 U.S. at 261.

EFT-6 *Illinois ex rel. Lignoul v. Continental Illinois National Bank & Trust Co.*, 536 F.2d 176 (7th Cir. 1976), *affg in part and rev'g in part*, 409 F. Supp. 1167 (N.D. Ill. 1975), *cert. denied*, 429 U.S. 862 (1976).

The Illinois bank commissioner brought an action against Continental Illinois Bank & Trust Co. ("Continental"), a national bank, for declaratory relief and an injunction with respect to the defendant's use of customer-bank communications terminals ("CBCTs"). The lower court held that the CBCT facility was a branch bank under 12 U.S.C. § 36(f), "except with regard to the withdrawing of cash by card and payments made on installment loans due the bank."<sup>43</sup>

The appellate court, adopting the opinion in *Independent Bankers Association of America v. Smith*,<sup>44</sup> held that "all of the functions performed by the CBCT constituted branch banking."<sup>45</sup>

EFT-7 *Independent Bankers Association of America v. Federal Home Loan Bank Board*, FED. BANKING L. REP. (CCH), ¶ 97,785, at 83,547 (D.C. Cir. 1979), *cert. denied*, — U.S. — (1979).

See Case EFT-1 *supra*.

EFT-8 *Independent Bankers Association of America v. Smith*, 534 F.2d 921 (D.C. Cir. 1976), *cert. denied*, 429 U.S. 862 (1976).

In December 1974, the Comptroller of the Currency issued an interpretive ruling construing the McFadden Act as permitting national banks to establish off-premise CBCTs.<sup>46</sup> The Independent Bankers Association of America and others filed suit to enjoin the implementation of this ruling. The district court declared the ruling unlawful and issued an injunction.<sup>47</sup> The Comptroller appealed.

The appellate court affirmed. In a lengthy opinion, it held that all CBCTs performed at least one of the banking services of receiving deposits, paying checks or making loans, and were therefore branches within the terms of the McFadden Act. As a result, the

43. 536 F.2d at 177.

44. 534 F.2d 921 (D.C. Cir 1976), *cert. denied*, 429 U.S. 862 (1976). See Case EFT-8 *infra*.

45. 536 F.2d at 177-78.

46. CBCTs are manned or unmanned electronic terminals which, depending on how the machines are programmed, permit an existing bank customer to accomplish various financial transactions, including deposit and withdrawal of funds and the transfer of funds between accounts.

534 F.2d at 924.

47. 402 F.Supp. 207 (D.D.C. 1975).



court held that CBCTs must comply with the branching requirements of both federal and state laws.

EFT-9 *Missouri ex rel. Kostman v. First National Bank in St. Louis*, 538 F.2d 219 (8th Cir. 1976), *cert. denied*, 97 S. Ct. 357 (1976).

The trial court found that the operation of CBCTs by First National Bank ("Bank") violated 12 U.S.C. § 36(f), since the number of branch facilities of the Bank, including the CBCTs, exceeded the maximum permitted by Missouri law.<sup>48</sup> The appellate court affirmed, stating:

Our review of this record discloses that the machines in question are capable of receiving deposits and crediting the amount deposited to the customer's account. The ability of the CBCT machines, when properly operated, to perform this banking transaction at a location "apart from the chartered facility" constitutes branch banking.<sup>49</sup>

EFT-10 *Nebraska EFT System*, 6 CLSR 502 (U.S. Dep't of Justice 1977).

The Nebraska Electronic Terminal System ("NETS") was a proposed joint venture to establish an EFT system. Membership in NETS was restricted to federal and state chartered banks, pursuant to the State's EFT statute. In an opinion letter dated March 7, 1977, Donald I. Baker, assistant attorney general, antitrust division, Justice Department, indicated that "the degree of risk, the amount of capital required and the economies of scale involved in constructing EFT systems—all of which are often cited as justification for joint ventures—do not necessarily suggest the need for a joint venture of the dimensions of NETS."<sup>50</sup>

Mr. Baker noted the Justice Department's general opposition to mandatory sharing legislation since it undercuts the incentive to innovate, and may violate the antitrust laws.<sup>51</sup>

EFT-11 *Nebraska ex rel. Meyer v. American Community Stores Corp.*, 193 Neb. 634, 228 N.W.2d 229 (1975).

In 1974, the Federal Home Loan Bank Board ("FHLBB"), authorized First Federal Savings & Loan Association ("First Federal"), a federally chartered savings and loan association, to install CBCTs in two American Community Stores ("American") "Hinky Dinky"

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48. MO. ANN. STAT. § 362.107 (Vernon).

49. 538 F.2d at 220.

50. 6 CLSR at 503.

51. *Id.* at 504.

supermarkets. Using a CBCT, a depositor at First Federal could deposit or withdraw sums of money. The State filed suit against American, claiming that these services constituted unlawful banking. The district court dismissed the action, and the State appealed.

The State contended on appeal that American was itself receiving deposits and paying withdrawals, and that this amounted to carrying on the business of banking in violation of Nebraska law.<sup>52</sup> The court found that American was simply acting as an intermediary, assisting in the transfer of funds between First Federal and its depositors, and that those acts did not amount to engaging in the banking business. The court noted:

The undisputed evidence here establishes that the element of a debtor and creditor relationship essential to any bank deposit or withdrawal of funds never existed between the store and the customer. The customer is transacting business with First Federal through the use of a computer terminal in the store, and the actions of the store facilitate that transaction. . . . The computer terminal is analogous to communications equipment of other kinds in that it simply transmits information to the central computer of First Federal. The deposit and withdrawal transactions are electronically effected and perfected by the computer on the records and premises of First Federal.<sup>53</sup>

EFT-12 Oklahoma *ex rel.* State Banking Board v. Bank of Oklahoma, 409 F. Supp. 71 (N.D. Okla. 1975).

The Defendant had variously installed CBCTs in retail stores (point-of-sale terminals), and freestanding off-line ATMs (automated teller machines) in numerous off-premises locations. These terminals could perform limited functions, including withdrawals of cash, and deposits of cash and checks, and the transfer of funds from one account to another. The state brought suit for declaratory and injunctive relief against the use of these terminals.

The district court, in a lengthy opinion, found that a "branch," as conceived at the time Congress enacted the McFadden Act, was a complete banking establishment, staffed by people, where general banking business took place.<sup>54</sup> As such, a CBCT was not a "branch" as defined in the Act or in Oklahoma law, and that even if it was a "branch," the functions performed did not constitute branch banking.

The court appeared to be heavily influenced in its decision by the savings and efficiency that would occur with the displacement of

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52. NEB. REV. STAT. 1943, § 8-114.

53. 193 Neb. at 639, 228 N.W.2d at 303.

54. 409 F. Supp. at 90.

paper checks by electronic transactions, and the pro-competitive effects EFTS will have on the American financial industry.<sup>55</sup>

EFT-13 State Bank of Fargo v. Merchants National Bank & Trust Co., 593 F.2d 341 (8th Cir. 1979).

Plaintiff, State Bank of Fargo, sued the Comptroller of the Currency and Merchants National Bank ("Merchants"), a national bank, to prohibit Merchants from operating two CBCTs pursuant to authority of the Comptroller. The trial court entered summary judgment for the defendants<sup>56</sup> and plaintiff appealed.

The question before the court was not whether CBCTs were branch banks, as had been considered in previous cases,<sup>57</sup> but merely whether, under North Dakota law, a state bank could lawfully operate CBCTs. North Dakota law<sup>58</sup> provides that

state banks may provide services to its customers involving electronic transfers of funds to the same extent that other financial institutions chartered and regulated by any agency of the federal government are permitted to provide such services within the state.<sup>59</sup>

The law further provides that CBCTs are not to be considered branches, and that mandatory sharing of terminals is required on request of other banks.<sup>60</sup>

The court affirmed the trial judge's finding that under North Dakota law, a state bank can lawfully use a CBCT, since both federal savings and loans and federal credit unions are permitted to use remote service units, and therefore, Merchants' was authorized under federal law to maintain CBCTs as branch banks.<sup>61</sup>

EFT-14 United States v. Rocky Mountain Automated Clearing House Association, FED. BANKING L. REP. (CCH), ¶ 97,124, at 82,404 (D. Colo. 1977).

The United States Department of Justice challenged the membership and access restrictions of the Rocky Mountain Automated Clearing House Association as violating the Sherman Act, since it

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55. *Id.* at 85, 89-90.

56. 451 F. Supp. 775 (D.N.D. 1978).

57. Independent Bankers Association of America v. Smith, 534 F.2d 921 (D.C. Cir. 1976), *cert. denied*, 429 U.S. 862 (1976) (*see* Case EFT-8 *supra*); Missouri *ex rel.* Kostman v. First National Bank in St. Louis, 538 F.2d 219 (8th Cir. 1976), *cert. denied*, 97 S. Ct. 357 (1976) (*see* Case EFT-9 *supra*).

58. N.D. CENT. CODE § 6-03-02(8).

59. 593 F.2d at 345.

60. *Id.*

61. *Id.* at 345-46.

restricted access to its computer facilities and prevented thrift institutions from becoming members or gaining direct access to its facilities. The case was later dismissed by the Government after the Association amended its rules to permit membership by financial institutions other than banks.

**EFT-15** United States League of Savings and Loan Associations v. Board of Governors, Federal Reserve System, *FED. BANKING L. REP. (CCH)*, ¶ 97,785, at 83,547 (D.C. Cir. 1979), *cert. denied*, — U.S. — (1979).

*See* Case EFT-1 *supra*.

