Local Power to Regulate Payday Lenders in Light of California State Preemption

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Issue

What powers does San Mateo County have to control payday lending?

Facts

Payday lending takes advantage of the poor and the unbanked. Members of the community in San Mateo are interested in confronting problems related to payday lending in their County. They are looking to ways to regulate and control the practice. The cities and county of San Mateo governments may consider adopting legislation to regulate payday lenders in their jurisdiction. However, they may be limited in their ability to enact certain laws due to state preemption. The State of California has usury laws and Deferred Transactions laws, which address and regulate the operation of payday lending establishments.

This memorandum explores the limits placed on San Mateo County and its cities' governments.

Analysis

State Preemption

California’s doctrine of state preemption makes the state’s laws superior to local laws. Local governments are permitted to make laws when they do not conflict with

State preemption of local law can be expressed or implied. “Express preemption” requires the legislature make an explicit statement that it intends a state law to fully occupy the area. *Valley Vista* at 887. “Implied preemption” is less defined and can come in many forms when the legislature has not expressed its intent to permit local regulation. *Mendocino* at 476. There can be no implied preemption when a state law expressly allows supplementary local legislation. *Personal Watercraft Coalition v. Board of Supervisors*, 100 Cal. App. 4th 129 (1st Dist. 2002). For a local law to be struck down on the basis of implied preemption, a court must establish that the state has occupied the field. *Id.* at 487.

In order to establish if the state occupies the field, courts must look to the purpose and scope of the legislative scheme. In general, preemption by state law exists if one of three tests is met:

1. the subject matter has been so fully and completely covered by general law as to clearly indicate that it has become exclusively a matter of state concern;
2. the subject matter has been partially covered by general law couched in such terms as to indicate clearly that a paramount state concern will not tolerate further or additional local action; or
3. the subject matter has been partially covered by general law, and the subject is of such a nature that the adverse effect of a local ordinance on the transient citizens of the state outweighs the possible benefit to the municipality.

In certain, limited situations the courts will assume that local rules standup against state laws. When local governments regulate an area over which they typically have control, like local land use, courts will presume that this regulation is not preempted by state statute, unless there is an indication of preemptive intent from the state legislature. O’Connell v. City of Stockton, 41 Cal. 4th 1061, 1069 (2007). The power over local governments to regulate land use is a police power granted in Article XI, Section 7 of the California Constitution to cities and counties. Big Creek Lumber Co. v. County of Santa Cruz, 38 Cal. 4th 1139, 1151 (2006). It is not a power delegated by the authority of the state. DeVita v. County of Napa, 9 Cal. 4th 763, 782 (1995). Also, when there is a significant local interest to be served, presumption favors the validity of the local ordinance. Big Creek Lumber at 1149.

**State Laws on Payday Lending**

In light of the practice of state preemption, it is important for those wishing to regulate payday lending in San Mateo County to understand what state laws govern the field of payday lending. The State of California currently has laws regarding interest rates and deferred transactions. The usury rate is capped at 10 % by Article XV of the California Constitution. Sections 23000-23106 of the California Financial Code, also known as the California Deferred Deposit Transaction Law, govern the conduct of check cashers and payday lenders. Cal. Fin. Code §§ 23000-23106. The law requires payday lenders to register with the state, submit reports to the state and it allows the state to
issue penalties to those that violate the law. In addition, Section 1789 of the California Civil Code sets a limit on interest and fees for check cashers. Local regulation would have to be respectful of these state laws in order to avoid state preemption issues.

**San Mateo County Power**

Counties have the authority to govern, subject only to the limitation that they exercise this power within their territorial limits and subordinate to state law. *San Diego County Veterinary Medical Ass’n. v. County of San Diego*, 116 Cal. App. 4th 1129 (4th Dist. 2004).

San Mateo county and the cities within may be able to gain control of their payday lending problem through zoning ordinances that restrict land use, rather than trying to regulate the business practices of payday lenders. As stated above, local land use is a police power granted to local governments rather than the state. *Big Creek Lumber* at 1149; *DeVita* at 782.

The powers of a county can only be exercised by the County Board of Supervisors or through authorized agents. In order for Board actions to be valid, the Board must follow procedural requirements as mandated by state statute. Where the state law does not specify a method of accomplishing something, the county can adopt any means it chooses.¹

**How State Preemption Stopped Predatory Lending Ordinances**

If San Mateo county or the cities within the county choose to pass ordinances to regulate payday lending, they may be confronted by opposition not only in the legislative realm, but also through legal challenges raised in court. This was true with recent

legislation passed to control predatory lenders in cities across the country. Lawsuits were filed by lenders in order to validate local ordinances on the basis of state preemption doctrine.

The California State Supreme Court in American Financial Services Ass’n v. City of Oakland, invalidated an Oakland predatory lending ordinance. 34 Cal. 4th 1239 (2005). Oakland’s ordinance was stricter than California’s statute. The court held that the state’s laws controlled the field, although this was not express. The court reasoned that statewide regulation of mortgage lenders was essential as the housing market was critical to the state economy. The court feared that local regulations would upset the “centralized and uniform” rules necessary for the economic wellbeing of California. American Financial at 1258. There was disagreement between the parties on the evidence that the legislature had implicitly preempted local initiatives and on whether the state’s regulatory interest was sufficiently powerful to trump Oakland’s interest in dealing with the negative social and economic consequences of payday lending within its borders. Oakland argued that there was no state preemption because at the time when state legislation (California Financial Code Section 4970-4978) was passed mortgage lenders had lobbied for express preemption measures and were unsuccessful. The state bill said nothing about preemption. Oakland argued its ordinance only supplemented the state’s approach to predatory lending. Yet, these arguments did not persuade the court. The court held that the state legislation fully occupied the field. The ordinance was not supplementary, but rather it invaded the state’s control.