

Why the Bank Examination Privilege Doesn't Work as Intended

Eric B. Epstein[†]

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Introduction

Bank examinations are one of the key tools used by federal regulators to supervise the banking and financial services industry. A bank examination is a dialogue between a regulator and a bank about the bank's policies and practices. Confidentiality is crucial to making this dialogue work. As such, publicizing examination records could inhibit candid communication between banks and regulators, and, in some cases, harm the subject institution.¹ But preserving secrecy is difficult when a bank is involved in a lawsuit against a nongovernmental party. In many cases, a bank's adversary will attempt to obtain the bank's examination records in order to use them as evidence against the bank. Surprisingly, however, no federal statute or regulation fully addresses this problem.

To plug this gap, federal courts developed a common law rule: the bank examination privilege. The modern incarnation of the privilege originated in a series of cases in the 1990s. Each of these cases involved examinations conducted by federal regulators, including the Office of the Comptroller of the Currency (OCC), the Federal Reserve Board, and the Federal Deposit Insurance

[†] Mr. Epstein is a partner in the New York Office of Dorsey & Whitney LLP. He is the lead author of a new legal treatise, *THE BANK EXAMINATION PRIVILEGE*, which was published in January by the American Bar Association. He also is a lecturer in law at Columbia Law School.

1. *In re Subpoena Served upon Comptroller of the Currency*, 967 F.2d 630, 633-4 (D.C. Cir. 1992).

Corporation (FDIC).² Courts wanted to give these regulators, and banks, a reasonable assurance of confidentiality while acknowledging litigants' legitimate need for examination records. The privilege strikes a balance: it shields examiners' opinions, recommendations and deliberations, unless a party has a sufficiently strong need, known as good cause, to obtain that information.³

Today, the bank examination privilege is recognized in every federal circuit.⁴ Within the landscape of federal law, the privilege is the primary rule for resolving privilege disputes related to bank examinations. But rifts are growing between how one would expect the privilege to work and how the privilege actually works in practice.

I. The Nature of the Problem

The problem revolves around the interplay between the bank examination privilege and state privilege law. State privilege law does not uniformly mirror the bank examination privilege. Instead, the state law on this issue reflects a spectrum of approaches. Some state laws track the federal approach, while others depart from it significantly.

For example, the rule in the state of Washington functions similarly to the bank examination privilege. A Washington statute provides that bank examination reports are generally, but not always, off-limits: "The court may permit discovery and introduction of only those portions of the report which are relevant and otherwise unobtainable by the requesting party."⁵ The question of whether information is "relevant" and "otherwise unobtainable" is essentially a variation on the good cause exception to the bank examination privilege.

But some other states do not treat bank examination records as privileged, or have not adopted a clear rule on point. For instance, the Supreme Court of Michigan has held that a Michigan law "requiring information obtained by examiners to be kept secret is not intended to prevent testimony of State officers in the courts of the State under oath and upon due process."⁶ At the opposite end

2. *In re Bankers Trust Co.*, 61 F.3d 465 (6th Cir. 1995); *In re Subpoena Served Upon Comptroller of the Currency*, 967 F.2d 630; *Principe v. Crossland Sav., FSB*, 149 F.R.D. 444 (E.D.N.Y. 1993).

3. *In re Subpoena Served upon Comptroller of the Currency*, 967 F.2d at 634.

4. *See, e.g.*, *Martinez v. Rocky Mountain Bank*, 540 Fed. App'x 846, 854 (10th Cir. 2013); *In re Bankers Trust Co.*, 61 F.3d at 471-72; *Rockwood Bank v. Gaia*, 170 F.3d 833, 839 n. 4 (8th Cir. 1999); *Redland Soccer Club, Inc. v. Dep't of Army*, 55 F.3d 827, 853 n.18 (3d Cir. 1995); *In re Subpoena Served upon Comptroller of the Currency*, 967 F.2d at 633-35; *Overby v. U.S. Fidelity & Guar. Co.*, 224 F.2d 158, 163 (5th Cir. 1955); *F.D.I.C. v. Jones*, No. 2:13-cv-00168, 2015 WL 4275961, at *1 (D. Nev. Jul. 14, 2015); *Gradeless v. Am. Mut. Share Ins. Corp.*, No. 1:10-CV-00086, 2011 WL 221895, at *6 (S.D. Ind., Jan. 19, 2011); *In re JPMorgan Chase Mortg. Modification Litig.*, No. 11-MD-02290, 2012 WL 5947757, at *2 (D. Mass. Nov. 27, 2012); *Raffa v. Wachovia Corp.*, 242 F. Supp. 2d 1223, 1225 (M.D. Fla. 2002); *Fed. Hous. Fin. Agency v. JPMorgan Chase & Co.*, 978 F. Supp. 2d 267, 273 (S.D.N.Y. 2013); *Marriott Emps.' Fed. Credit Union v. Nat'l Credit Union Admin.*, No. CIV.A. 96-478-A, 1996 WL 33497625, at *6 (E.D. Va. Dec. 24, 1996).

5. *See, e.g.*, WASH. REV. CODE § 32.04.220 (2016).

6. *In re Culhane's Estate*, 256 N.W. 807 (Mich. 1934) (discussing Michigan state law).

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of the spectrum, some states go even further than the bank examination privilege by strictly shielding examination records. Notably, Delaware has codified a “[f]inancial institution supervisory privilege,” which provides, in relevant part: “All confidential supervisory information shall be the property of the [State Banking] Commissioner and shall be privileged and protected from disclosure to any other person and shall not be discoverable or admissible into evidence in any civil action.”⁷

Thus, state privilege law in this area can differ on a state-to-state basis and often clashes with the federal approach. Based on this author’s review of all published judicial decisions regarding the bank examination privilege, there do not appear to be any published judicial decisions finding that bank examination privilege preempts these state laws.⁸ Thus, in each state, the bank examination privilege coexists with the state law on protecting examination records. As a result, when the two differ, a choice of law question can arise. That is, in order to determine whether bank examination records are privileged, a court first has to decide whether to apply federal or state privilege law.

This choice of law question is the crux of a major problem. One would expect that, in determining the applicable law, courts would simply distinguish between federal and state regulators. As previously mentioned, the privilege is a federal rule. It sprung from cases involving bank examinations conducted by federal regulators, such as the OCC. As such, one would expect courts to look to the privilege whenever a litigant seeks to probe a federal bank examination, but would not expect the privilege to govern bank examinations conducted by state agencies. One would expect that those examinations would be subject to the privilege law of the state that conducted the examination.

To date, however, the federal courts that have grappled with this choice of law question have arrived at a very different solution. Instead of focusing on the nature of the regulator, federal courts have focused on the nature of the lawsuit. Specifically, federal courts have held that the relevant distinction is between federal-question cases (*i.e.*, cases that involve federal law claims or defenses) and diversity-jurisdiction cases (*i.e.*, cases that involve state law claims and defenses). In federal-question cases, the bank examination privilege governs, even if the records being sought belong to a state regulator.⁹ However, in diversity-jurisdiction cases, federal courts have held that it is appropriate to look

7. See, e.g., DEL. CODE ANN. tit. 5, § 145 (2017).

8. U.S. CONST. art. VI, § 2.

9. Fisher v. Ocwen Loan Servicing, LLC, No. 4:12-CV-543, 2016 U.S. Dist. LEXIS 73759 (E.D. Tex. Jun. 7, 2015) (applying the privilege to examination records belonging to the New York State Department of Financial Services in a False Claims Act case); Rouson *ex rel.* Estate of Rouson v. Eicoff, No. 04-CV-2734, 2006 WL 2927161 (E.D.N.Y. Oct. 11, 2006) (applying the privilege to examination records belonging to the New York State Banking Department in a Racketeer Influenced and Corrupt Organizations case).

to state privilege law, even if the examination records being sought belong to a federal regulator.¹⁰

Generally, in diversity-jurisdiction cases, that entails looking to the privilege law of the state in which the federal court is situated. For example, a Michigan federal court would apply Michigan state privilege law. If the examination at issue was conducted or otherwise centered in a different state, such as Washington, the Michigan federal court would follow Michigan's choice of law rules in deciding which state's privilege law to apply.¹¹

II. Why It Matters

This nuance of the bank examination privilege has significant, real-world impact. As a practical matter, federal regulators and banks cannot rely on the privilege as a predictable or dependable rule, eroding confidence in the confidentiality of bank examinations. Despite the existence of the privilege, federal examination records are often at the mercy of the policies of individual states, some of which favor disclosure. In addition, in states that strictly protect examination records, the privilege can be a source of frustration for state regulators and financial institutions. In these states, when an institution is involved in a federal-question case, the privilege can potentially replace the state's strict confidentiality rule, thereby lowering the bar for obtaining information about state-level examinations.

Two recent decisions help to illustrate this problem. *SBAV v. Porter Bancorp* was a diversity-jurisdiction case litigated in the U.S. District Court for the Western District of Kentucky.¹² During discovery, the plaintiff sought records of bank examinations conducted by the FDIC and Federal Reserve. The Court held that because the case involved diversity jurisdiction, the bank examination privilege was inapplicable, notwithstanding the fact that the FDIC and Federal Reserve are federal regulators. Instead, the Court looked to the privilege law of the state, Kentucky, in which the Court was situated. The Court found that Kentucky does not consider bank examination records to be

10. See *Mich. First Credit Union v. Cumis Ins. Soc'y*, No. 05-CV-74423, 2007 U.S. Dist. LEXIS 17582 (E.D. Mich. Mar. 14, 2017) (applying Michigan privilege law to Michigan Office of Financial and Insurance Services examination records in diversity-jurisdiction case); *SBAV LP v. Porter Bancorp, Inc.*, No. 3:13-CV-00710-TBR, 2015 WL 1471020 (E.D. Ky. Mar. 31, 2015) (applying Kentucky privilege law to FDIC and Federal Reserve examination records in diversity-jurisdiction case), *vacated as moot*, 3:13-CV-00710, 2015 WL 8004502 (W.D. Ky. Dec. 1, 2015); *In re Powell*, 227 B.R. 61 (Bankr. D. Vt. 1998) (applying Vermont privilege law to FDIC examination records in diversity-jurisdiction case).

11. *Klaxon Co. v. Stentor Elec. Mfg. Co.*, 313 U.S. 487, 496-97 ("Subject only to review by this Court on any federal question that may arise, Delaware is free to determine whether a given matter is to be governed by the law of the forum or some other law.").

12. *SBAV LP*, 2015 WL 1471020, at *1.

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privileged.¹³ Therefore, the Court concluded, the FDIC and Federal Reserve's bank examination records were unprotected.¹⁴

By contrast, *United States ex rel. Fisher v. Ocwen Loan Servicing* was a federal-question False Claims Act ("FCA") case litigated in the U.S. District Court for the Eastern District of Texas.¹⁵ During discovery, the plaintiff sought records of bank examinations conducted by the West Virginia Department of Financial Institutions ("WVDFI"). The Court found that, under West Virginia law, the documents would be non-discoverable. As the Court noted: "Clearly, these communications originated with an understanding that they would not be disclosed under state law."¹⁶ But, the Court held, "there is no reason for WVDFI to assume that these documents would be protected in an FCA action based on a federal question, especially given the broad range of permissible discovery."¹⁷ Thus, the Court applied the bank examination privilege instead of West Virginia privilege law. It further held that the records were discoverable based on the good cause exception to the bank examination privilege.

In the *SBAV* case, the bank examination privilege failed to protect examination records belonging to federal regulators. In the *Fisher* case, the bank examination privilege governed, but it only served to undermine state privilege law. In both cases, the outcome arguably was a far cry from the original intent of the bank examination privilege, which was to protect sensitive, confidential federal examination records.

Why does the privilege work this way? To answer that question, it is helpful to bear in mind five points about the nature and history of the privilege.

III. Five Points about the Privilege

1. *The Impact of Federal Rule of Evidence 501*

The primary reason the bank examination privilege does not work as expected is because although the privilege is important to banks and federal regulators, Congress has not codified it as a statute. Thus, it is considered to be a common law rule. The fact that it is uncodified is not just a technicality: under Federal Rule of Evidence 501, the common law nature of the privilege changes the way that the privilege functions.

Federal Rule of Evidence 501 governs how federal courts choose between federal privilege law and state privilege law. Rule 501 begins by distinguishing between, on the one hand, federal common law privileges, and, on the other

13. *Id.* at *5.

14. The FDIC and Federal Reserve subsequently moved for reconsideration of this decision. Shortly thereafter, the case was settled. Thus, the Court did not decide the motion for reconsideration.

15. No. 4:12-CV-543, 2015 WL 3942900, at *2 (E.D. Tex. June 26, 2015).

16. *Id.* at *5.

17. *Id.*

hand, federal privileges that stem from the U.S. Constitution, federal statutory law, or rules prescribed by the U.S. Supreme Court.¹⁸ Federal common law privileges apply in federal-question cases. But federal common law privileges do not apply in diversity-jurisdiction cases. In diversity-jurisdiction cases, state privilege law supersedes federal common law privileges.¹⁹

However, when a privilege stems from the U.S. Constitution, federal statutory law or U.S. Supreme Court rules, the equation changes. Rule 501 does not bar federal courts from applying such privileges in diversity-jurisdiction cases.²⁰

In the field of banking law, an example of a federal statutory privilege is the privilege that shields Suspicious Activity Reports (SARs). The SAR privilege is derived from the Federal Bank Secrecy Act (BSA).²¹ When a financial institution submits a SAR, the BSA prohibits the institution from notifying “any person involved in the transaction that the transaction has been reported.”²² Federal regulations broaden that prohibition: Federal regulations categorically provide that “[a] SAR, and any information that would reveal the existence of a SAR, are confidential,” and in general “shall not be disclosed.”²³

These rules create “an unqualified discovery and evidentiary privilege” with respect to SARs.²⁴ Because the SAR privilege is grounded in a statute, Rule 501 does not restrict it to federal-question cases. Federal courts apply the SAR privilege in diversity-jurisdiction cases as well.²⁵ State courts similarly defer to the SAR privilege.²⁶

By contrast, there is no such statute underpinning the bank examination privilege. If such a statute existed, the bank examination privilege and SAR privilege likely would work in a similar fashion. But because there is no such statute, courts channel the bank examination privilege through Rule 501. Rule 501 shuts the privilege down in diversity-jurisdiction cases, even when federal examination records are at issue. Conversely, Rule 501 activates the privilege in federal-question cases, even when state examination reports are at issue.

18. See FED. R. EVID. 501.

19. *Id.*

20. See 23 CHARLES ALAN WRIGHT & KENNETH W. GRAHAM, FEDERAL PRACTICE AND PROCEDURE § 5436 (1980); see also *Pierce Cty. v. Guillen*, 537 U.S. 129, 147-48 (2003) (holding that Congress had the authority under the Commerce Clause to pass a statute restricting the discovery and admissibility of evidence in state and federal court).

21. 31 U.S.C. § 5318(g)(2) (2012).

22. *Id.*

23. 12 C.F.R. § 21.11(k) (2017).

24. *Whitney Nat'l Bank v. Karam*, 306 F. Supp. 2d 678, 682 (S.D. Tex. 2004).

25. See, e.g., *Lee v. Bankers Trust Co.*, 166 F.3d 540, 543-45 (2d Cir. 1999) (applying SAR privilege in diversity-jurisdiction case).

26. See *Union Bank of Cal. v. Super. Ct.*, 29 Cal. Rptr. 3d 894 (2005) (applying SAR privilege).

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2. Relationship to 12 U.S.C. § 1828(x)

There are occasional misconceptions that a federal statutory provision, 12 U.S.C. § 1828(x), codifies the bank examination privilege. As explained below, § 1828(x) does not codify the privilege. Thus, courts treat the bank examination privilege as a common law rule. That is why Federal Rule of Evidence 501 skews the effects of the privilege.

Section 1828(x) is entitled “Privileges not affected by disclosure to banking agency or supervisor.” Section 1828(x) and the bank examination privilege share a similar purpose: to build a barrier between bank examinations and private litigation. But § 1828(x) and the privilege address different aspects of this issue.

Section 1828(x) allows banks to share privileged information with bank examiners without waiving any applicable privileges.²⁷ For example, perhaps a bank receives privileged legal advice from outside counsel in the form of an email. During a subsequent bank examination, perhaps the bank shares the email with the examiner. Under § 1828(x), sharing the email with the examiner does not waive the attorney-client privilege. In a future lawsuit, if the bank’s adversary asks for the email, the bank can withhold it.

The difference between the bank examination privilege and § 1828(x) is that the former is a privilege, while the latter is an anti-waiver rule. The bank examination privilege attaches a privilege to the opinions, recommendations and deliberations of bank examiners. Section 1828(x) cannot do that. It can protect an already-privileged document. But the privilege itself has to come from somewhere outside § 1828(x).

In short, § 1828(x) and the privilege are separate and distinct rules. They serve a similar policy goal, but they do so in different ways.

3. The Role of Regulatory Policy

Many federal regulators take the position that bank examination records are privileged. Some of these regulators have even issued formal regulations to that effect.²⁸ These regulatory policies play a vital role when the bank examination privilege is litigated. Only regulators have the standing to assert the privilege. As such, a bank cannot defend the privilege without a regulator’s support.²⁹ If federal regulators did not consider examination records to be privileged, the privilege likely would be a dead letter.

But these regulations are not the legal authority for the bank examination privilege. That is, the privilege is not an application of these regulations. The

27. 12 U.S.C. § 1828(x) (2012).

28. *See, e.g.*, 12 C.F.R. § 4.36(b) (2016) (“It is the OCC’s policy regarding non-public OCC information that such information is confidential and privileged. Accordingly, the OCC will not normally disclose this information to third parties.”).

29. *Merchants Bank v. Vescio*, 205 B.R. 37, 42 (D. Vt. 1997).

privilege is a common-law rule. Nor do these regulations carry the force of a privilege.³⁰

Why? No federal statute empowers federal financial regulators to declare bank examination records to be privileged in federal litigation.³¹ In that sense, these regulations are unlike the SAR regulation. The SAR regulation is a valid privilege because it is grounded in a statute, but these regulations are not. Without an anchor in a statute, they do not transform the bank examination privilege into a statutory or regulatory privilege. As a result, they do not exempt the privilege from Rule 501.

4. Proposed Federal Rule of Evidence 509

Congress has considered several legislative proposals to shield bank examination reports from private litigants. However, Congress has not enacted any of these proposals. As a result, the bank examination privilege remains a common law rule.

One notable attempt to codify the privilege came about during the development of the Federal Rules of Evidence in the early 1970s. In 1972, the U.S. Supreme Court submitted draft rules of evidence to Congress. Among other things, these rules would have codified nine specific evidentiary privileges.³² These rules also would have prohibited courts from recognizing any other privileges under federal common law.³³

One of these privilege rules, Proposed Federal Rule of Evidence 509, was entitled “Secrets of State and Other Official Information.”³⁴ Proposed Rule 509 would have given the government “a privilege to refuse to give evidence and to prevent any person from giving evidence upon a showing of reasonable likelihood of danger that the evidence will disclose a secret of state or official information as defined in this rule.”³⁵

Under Proposed Rule 509, the definition of “Official Information” would have included governmental information that is unavailable to the public under the Freedom of Information Act, or FOIA.³⁶ FOIA is the federal statute that allows journalists and other members of the public to seek records from federal agencies outside of the litigation context. FOIA contains a variety of exemptions. Each exemption allows agencies to withhold a particular category of sensitive information when responding to FOIA requests.

30. See, e.g., *In re Bankers Trust Co.*, 61 F.3d 465, 470 (6th Cir. 1995).

31. *Id.*

32. *Jaffe v. Redmond*, 518 U.S. 1, 8 n.7 (1996).

33. See FED. R. EVID. 501 (unenacted), http://www.law.harvard.edu/publications/evidenceiii/rules/501_proposed.htm.

34. See FED. R. EVID. 509 (unenacted), http://www.law.harvard.edu/publications/evidenceiii/rules/509_proposed.htm.

35. *Id.*

36. *Id.*

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One of these exemptions, FOIA Exemption 8, specifically concerns federal bank examinations. FOIA Exemption 8 shields information “contained in or related to examination, operating, or condition reports prepared by, on behalf of, or for the use of an agency responsible for the regulation or supervision of financial institutions.”³⁷

In effect, Proposed Rule 509 would have imported FOIA Exemption 8 into private civil litigation. By doing so, Proposed Rule 509 would have indirectly codified a bank examination privilege. In fact, in two ways, this rule would have been stricter than the common law privilege that exists today. First, Exemption 8 does not contain a good cause exception. Second, Exemption 8 is not limited to bank examiners’ opinions, recommendations and deliberations. It encompasses the entire bank examination process.

Proposed Rule 509, by incorporating FOIA Exemption 8, likely would have also reshaped how the privilege applies to federal and state examinations. In particular, it likely would have protected federal examination records in both diversity-jurisdiction and federal-question cases. At the same time, in federal-question cases, it likely would not have undercut state laws that strictly shield examination records.

However, ultimately, Congress chose not to codify any specific evidentiary privileges in the Federal Rules of Evidence. As such, Congress did not pass Proposed Rule 509 into law. The rejection of these privilege rules was not a disapproval of any common law privilege.³⁸ Rather, Congress did not want to “freeze the law governing the privileges of witnesses in federal trials at a particular point in our history[.]”³⁹ Congress intended courts to continue developing the law of privilege “in the light of reason and experience.”⁴⁰

5. The Bank Examination Report Protection Act

In the late 1990s, Congress considered another proposal to legislatively protect bank examination reports: a bill entitled the Bank Examination Report Protection Act (BERPA).⁴¹ BERPA would have added a “Bank Supervisory Privilege” to federal statutory law. In particular, BERPA would have provided: “All confidential supervisory information shall be the property of the Federal banking agency that created or requested the information and shall be privileged

37. 5 U.S.C. § 552(b)(8) (2012).

38. See S. Rep. No. 93-1277, at 7059 (1974) (noting that “the action of Congress should not be understood as disapproving any recognition of a psychiatrist-patient, or husband-wife, or any other of the enumerated privileges contained in the Supreme Court rules”).

39. *Jaffee v. Redmond*, 518 U.S. 1, 9 (1996).

40. See S. Rep. No. 93-1227.

41. See H.R. 174, 106th Cong. (1999).

from disclosure to any other person.”⁴² BERPA would have protected state examinations to the same extent in federal litigation.⁴³

Procedurally, BERPA also would have prohibited litigants from requesting bank examination reports from banks. Instead, BERPA would have required litigants to seek such documents from the regulator that conducted the examination. If the regulator declined to produce the requested documents, BERPA would have allowed the litigant to ask the court to override the regulator’s decision. However, in most cases, the court’s role likely would have been limited to simply confirming that the documents being withheld were, in fact, confidential supervisory information, and therefore privileged.⁴⁴

BERPA had support from federal⁴⁵ and state⁴⁶ regulators. Like Proposed Federal Rule of Evidence 509, BERPA would have fixed two of the anomalies in the common-law bank examination privilege. First, BERPA would have extended the privilege to diversity-jurisdiction cases. Second, by strengthening the privilege, BERPA would have prevented it from diluting state privilege laws. However, for reasons that are unclear from available legislative history, the bill stalled, and was never made into law.

IV. Potential Solutions

As noted earlier, the main purpose of the bank examination privilege is to create clear expectations regarding the confidentiality of federal bank examinations. However, currently, the privilege does not fully achieve that goal. With respect to federal bank examinations, the privilege is not a reliable rule. With respect to state bank examinations, it interferes with state laws that give bank examinations broader and more rigorous protection.

There are two ways to solve this problem. The first would involve legislative change. Congress could pass a bank examination privilege statute. It would have to apply consistently across all types of civil cases, whenever litigants seek federal bank examination records. It also would have to specify the role, if any, of state privilege law when litigants seek information about examinations conducted by state regulators.

The second solution would be to rethink how the existing, common-law bank examination privilege should work. In general, federal common law rules do not supersede state law. But federal common law rules can supersede state

42. *Id.* at § 45(b)(1)(A).

43. *Id.* at § 45(c).

44. *Id.* at § 45(e).

45. *See Regulatory Burden Relief, Hearing Before the Subcomm. on Fin. Insts. & Consumer Credit of the S. Comm. on Banking and Fin. Servs.*, 105th Cong. 158 (1998) (statement of Julie L. Williams, Acting Comptroller of the Currency).

46. *See* Press Release, Conference of State Bank Supervisors, State Bank Regulators Back Burden Relief (Jul. 16, 1998), <http://www.csbs.org/news/press-releases/pr1998/Pages/Statebankregulatorsbackburdenrelief.aspx>.

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law “where there are uniquely federal interests at stake.”⁴⁷ For example, “[o]ne such exception applies to litigation that implicates the nation’s foreign relations.”⁴⁸ In such cases, “[b]ecause our foreign relations could be impaired by the application of state laws, which do not necessarily reflect national interests, federal law applies . . . even where the court has diversity jurisdiction.”⁴⁹

Arguably, the bank examination privilege implicates another uniquely federal interest: specifically, the interest in effective federal regulation of the banking industry. Like foreign relations, this uniquely federal interest could be impaired if “left to divergent and perhaps parochial state interpretations.”⁵⁰ Therefore, when litigants seek to uncover confidential federal examination records, the privilege arguably should supersede state law, even if a literal reading of Rule 501 might suggest that state privilege law should apply.

In addition, in federal-question cases, when litigants seek state examination records, federal courts could give greater weight to state statutes that strictly protect those records. Technically, federal privilege law governs in federal-question cases. But federal privilege law has the flexibility to import state statutory privileges. To determine whether federal privilege law should import a state statutory privilege, a federal court will “balanc[e] the policies behind the privilege against the policies favoring disclosure.”⁵¹ The court will explore:

(1) whether the fact that the . . . [state] would recognize the privilege itself creates good reason for respecting the privilege in federal court, regardless of our independent judgment of its intrinsic desirability; and (2) whether the privilege is intrinsically meritorious in our independent judgment.⁵²

Thus far, only one decision – *Fisher*, which was touched upon earlier – has applied this test to bank examinations. In *Fisher*, the Eastern District of Texas concluded that this standard for the application of state privilege law was not met. The court reached this conclusion because “[t]here is a strong federal interest in FCA cases for seeking the truth, and in this case, federal law plays a predominant role in the litigation.”⁵³ However, this precedent has not yet been analyzed by other federal district courts, or by any federal appellate court.

In sum, there are several potential pathways for fixing the bank examination privilege. For the time being, however, banks should be aware that the privilege does not offer ironclad protection, or even a predictable level of protection, with respect to bank examination records. As a result, during a bank examination, it

47. *Ungaro-Benages v. Dresdner Bank AG*, 379 F.3d 1227, 1232 (11th Cir. 2004).

48. *Id.*

49. *Id.* at 1232-33.

50. *Banco Nacional De Cuba v. Sabbatino*, 376 U.S. 398, 425 (1964).

51. *Am. Civil Liberties Union v. Finch*, 638 F.2d 1336, 1343 (5th Cir. Unit A Mar. 1981).

52. *Id.*

53. *Id.* at 4.

can be difficult for a bank to know with certainty if the examination results will be revealed in future litigation.

Currently, the best way for a bank to reduce this uncertainty is to be mindful of both federal and state privilege law. During a bank examination, a bank should consider the federal rule: the bank examination privilege. But a bank also should consider the relevant state laws that may apply in a future case. In particular, a bank should consider the privilege laws of the states in which the bank is subject to regulatory oversight, as well as the privilege laws of the states in which the bank tends to face civil litigation. By creating a blended picture of these federal and state rules, a bank can assess the risk that its confidential communications with federal and state bank examiners may be exploited by an adversary in a lawsuit.