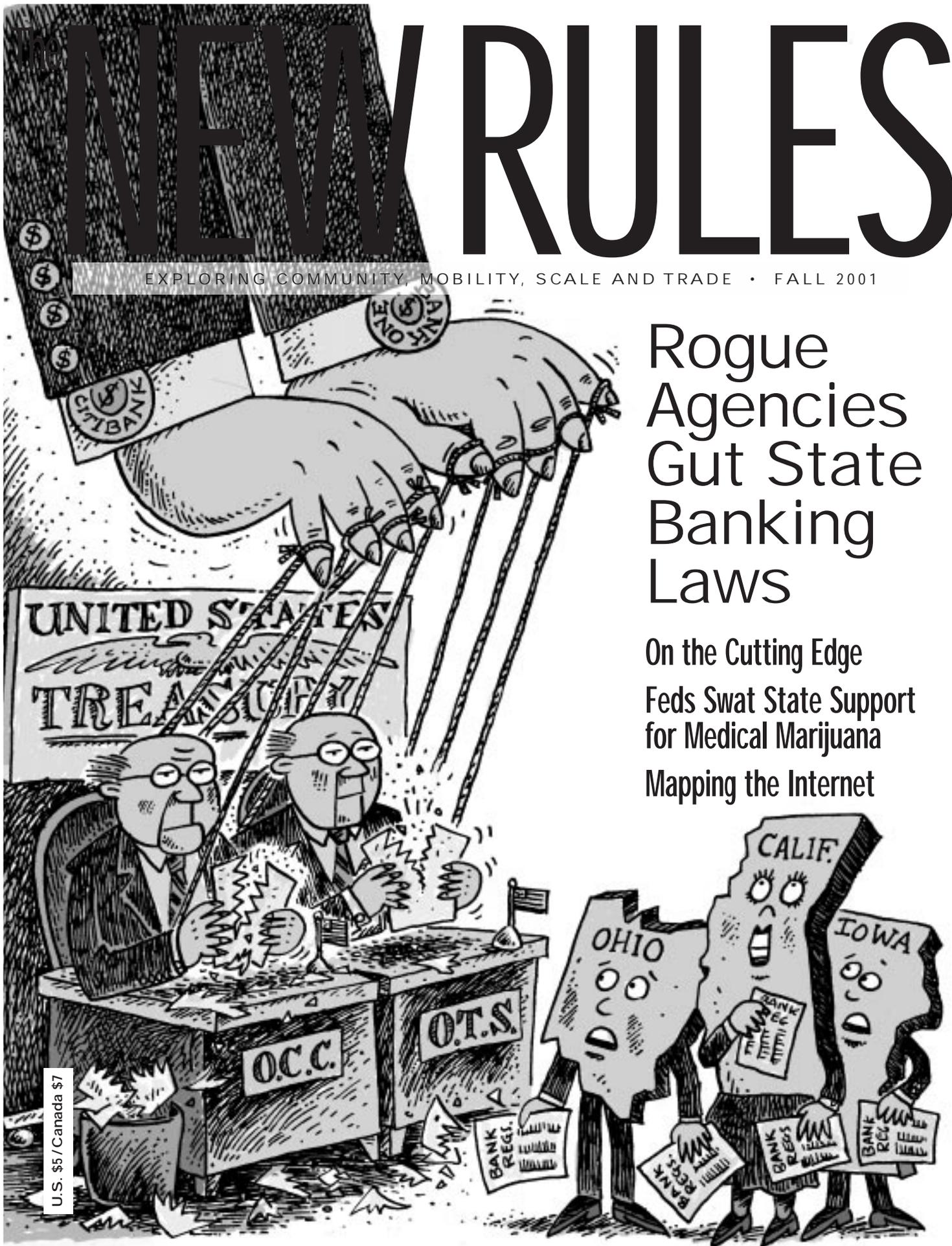


NEW RULES

EXPLORING COMMUNITY, MOBILITY, SCALE AND TRADE • FALL 2001

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On the Cutting Edge
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The New Rules (ISSN 1521-9917) is published quarterly by the Institute for Local Self-Reliance, 1313 5th Street SE, Minneapolis, MN 55414; telephone: 612-379-3815; fax: 612-379-3920; website: www.newrules.org; Washington, DC, office: 2425 18th Street NW, Washington, DC 20009; telephone: 202-232-4108; fax: 202-332-0463; website: www.ilsr.org. Send all subscription requests to the Minneapolis office: 1 year \$15, \$25 foreign (U.S. funds drawn on U.S. bank). For subscriptions of more than a year, multiple subscriptions, bulk copy sales, or for rights and permissions, contact Elizabeth Noll.

The New Rules is printed with vegetable-based inks containing no less than 20 percent vegetable oil on processed chlorine-free recycled paper containing 50 percent post-consumer waste fiber. This publication is printed in the United States by Sexton Printing, a certified environmentally responsible Great Printer.



Cover Illustration

Ken Avidor/Avidor Studios



Designing rules as if community matters



Who Should Make the Rules?

In June, a front page story in *The Washington Post* informed the nation that the White House planned, by executive fiat, to allow federally funded religious organizations to ignore local anti-discrimination laws. A general outcry arose. The President backed down. It was one of the few victories defenders of local control have won in recent years. At this writing, Congress is deciding whether to do through legislation what the executive branch decided not to do through regulation.

Increasingly higher levels of governments are overruling those closer to the citizenry. State legislatures override city councils and county commissions. Federal agencies and Congress override state legislatures. International agencies like the World Trade Organization override congresses and parliaments.

In 1999, the Minnesota legislature stripped Minneapolis and Saint Paul of their authority to require public employees to live inside the city. Earlier this year, after Portland had enacted a living wage ordinance for city contractors, the Oregon legislature prohibited such an ordinance from being extended to all city businesses. A few months later the Pennsylvania legislature dismantled Philadelphia's anti-predatory lending ordinance.

At the national level, as Daniel Kraker discusses in this issue, Presidents Reagan, Bush, Clinton and now Bush junior steadfastly have refused to recognize the right of states to legalize marijuana for medical purposes. George W. Bush's national energy plan would grant federal agencies the right to impose high-voltage electricity transmission lines on reluctant states. The World Trade Organization ruled that European nations have no right to ban the use of hor-

mones in beef cattle, even when the ban applies to domestic as well as imported cattle.

Both liberals and conservatives pay lip service to the idea that government works best when it is closest to the people. But their actions belie their words. Both firmly believe that local authority should be abolished if it hinders national efficiency, even if the economic costs are theoretical and trivial. Liberals affirm the need for collective authority, but want it exercised primarily at the national level because communities are parochial and too often influenced by the passions of the moment. Conservatives abhor authority exercised collectively at any level, echoing the judgment of Edmund Jennings Randolph, who told the Constitutional Convention, "Our chief danger arises from the democratic parts of our constitutions."

The federal courts are the ultimate arbiters of where power rests. Mostly, they favor centralized power, even when the justification for centralization is weak. In the mid 1980s, for example, Michigan required its counties to become responsible for disposing of their own garbage within their own jurisdictions. In return, counties were allowed to prevent the importation of garbage from less responsible communities. The Supreme Court overturned Michigan's law even though Congress had not explicitly denied Michigan that authority.

In our cover story, Stacy Mitchell describes the sordid history of federal courts overturning state and local banking-related laws even after Congress formally criticized federal agencies for invading state authority.

"Who governs?" is becoming one of the fundamental questions of our time, even in the age of the

world wide web. Many viewed the internet as inherently immune from national regulation. But as Sarah Hannigan points out, advances in technology now allow nations to know the geographic location of information receivers. Now nations technically can regulate the flow of information. If the Netherlands allows pornography and Saudi Arabia does not, should Saudi Arabia have the authority to impose its cultural perspective within its borders?

In answering these questions, we should be guided by the principle of subsidiarity: a higher level of government should not override the will of governments closer to the people unless it can make a compelling case for doing so. The burden of proof lies on preemption, not on devolution. The European Union already embraces this principle.

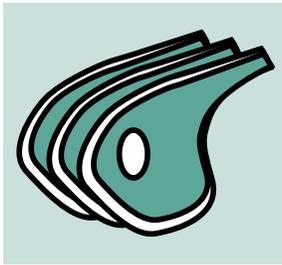
Will local control ensure beneficial outcomes? Of course not. But local control enables the widest possible participation. For example, there has been a considerable amount of local debate about whether residency requirements are useful. Most cities have decided they are not. A few dozen have decided that those who deliver public services paid for by local taxes should live within the community they serve. Why should the state legislature abolish their right to make that decision? Almost 60 percent of Arizonans, by direct popular vote, wanted doctors to be able to prescribe marijuana. Why should a handful of people 2500 miles away deny them the right to make that decision?

"It would be folly to argue that people cannot make political mistakes," Calvin Coolidge observed, "But compared with the mistakes which have been made by every kind of autocracy they're unimportant." [!]

Missouri Law Banning Beef Price Discrimination Upheld in Federal Court

A Missouri law passed in 1999 that requires meatpackers to pay the same prices for cattle of the same quality, regardless of who the sellers are—and to make the prices public—was upheld by the U.S. 8th Circuit Court of Appeals this summer. The law, which was designed to level the playing field for smaller, independent beef producers by eliminating price discrimination, had earlier been struck down by a U.S. District Judge on the grounds that it discriminated against out-of-state beef packers and unfairly burdened interstate commerce. The judge, however, had “little doubt that discrimination exists between the price that packers are willing to pay to a large producer and the price paid to a small producer.”

In reversing the lower court’s decision, the federal appeals court ruled that the Missouri Livestock Price Discrimination Law was constitutional because it



only regulated livestock sold within the state of Missouri, and thus was not an unfair restriction on interstate commerce.

This ruling is especially significant because a similar South Dakota live-

stock “price matching” law was struck down in federal court a year ago. Missouri’s law passed constitutional muster by allowing for different prices for reasons of quality, transportation costs, or special delivery times. The ruling could spur other states into passing similar laws to increase fairness and competition within the livestock industry. The federal Packers & Stockyards Act prohibits price discrimination, but the USDA has not enforced it. Until they do, states will be forced to follow Missouri’s lead and take matters into their own hands.

—DK

Court Upholds Maine Rx Program

A federal appeals court has upheld Maine’s pioneering prescription drug law. The Maine Rx Program authorizes state officials to negotiate with drug companies to obtain lower prices for more than 325,000 uninsured residents. If negotiations fail to lead to substantially lower prices, the law empowers the state to impose price controls starting in 2003.

By acting as an aggregate purchaser for uninsured residents, the state hopes to secure drug prices closer to those paid by HMOs and other bulk purchasers. As

an added impetus to negotiate, uncooperative manufacturers will have their products added to a list of medications that require prior authorization from the state before they may be prescribed to Medicaid patients.

Shortly after the prescription drug law’s passage last year, the Pharmaceutical Research and Manufacturers of America (PhARMA) filed suit in federal court. The trade association contends the law interferes with interstate commerce and is preempted by federal Medicaid law.

In May, an appeals court rejected both arguments, reversing a lower court decision and authorizing state officials to move ahead with the program. “It is one of the happy incidents of the federal system that a single courageous state may, if its citizens choose, serve as a laboratory; and try novel social and economic experiments without risk to the rest of the country,” the court concluded, quoting former Supreme Court Justice Louis Brandeis.

PhARMA has filed an appeal with the U.S. Supreme Court. If the high court endorses the appeals court ruling, the Maine approach is expected to spread rapidly across the country. Similar legislation has already been introduced in more than half the states.

—SM

Halting Predatory Gas Pricing

Last month, Ed Trudeau, co-owner of the Vista Gas Station in Burlington, Wisconsin, drove an 8,500-gallon tanker truck to a competing Citgo Station for a fill-up. Although he managed to pump only 343 gallons before employees cut the flow, Trudeau made his point. The Citgo had been selling gas below cost, a violation of Wisconsin state law. By the time his truck pulled out of the driveway, Citgo employees were raising the price on their sign.

At \$1.69 a gallon, Citgo’s price was below what Trudeau could buy wholesale and well below the \$1.85 his own station charged. State law requires gas stations to charge 6 percent more than their invoice price or 9.18 percent above wholesale, whichever is more.

Twelve states have similar laws, which aim to prevent large corporations from driving smaller businesses out of the market by selling below cost. Over the long term such predatory tactics eliminate competition and lead to higher consumer prices. In California, for example, just six companies control 90 percent of the market. The state has among the highest gas prices in the nation.

This year has seen a burst of renewed interest in laws prohibiting below-cost sales, many of which were adopted decades ago. Lawmakers in a few states

with these laws are pushing for repeal, arguing that they prevent consumers from getting the lowest possible price. As of press time, none of these efforts had succeeded.

Meanwhile, several states without below cost sales laws moved to enact them. Legislation in both Maryland and Minnesota has been signed into law. These new rules derive partly from concerns about the growing power of a few large, vertically integrated companies that own both refineries and gas stations. Another significant concern is the growth of gas stations installed at large retail stores, such as Wal-Mart, Costco and Kroger's. These companies often use gas as a loss leader, making it impossible for nearby independent stations to compete.

—SM

Community Choice On Track in California

Twenty-four states, with well over half the nation's population, have deregulated their electricity systems in the name of "customer choice." We were promised a world where we would choose our supplier from among a host of energy companies competing to bring us low-cost power. Instead, energy companies have competed for large customers and left most residential customers with essentially no choice. After five years of deregulation, less than two percent of residential consumers in restructured states have chosen a different power supplier.

In virtually all states, if a customer chooses not to choose, the existing utility becomes the default supplier. In 1999, Massachusetts became the first state to allow the local government to choose to become the default supplier. Ohio became the second state to embrace community choice. A group of 100 municipalities with 450,000 customers formed the Northeast Ohio Public Energy Council (NOPEC), a public electricity buying group. In February 2001 NOPEC signed a six-year supply contract with Green Mountain Power, switching from 60 percent coal and 40 percent nuclear power to 98 percent natural gas and 2 percent renewable energy, while at the same time lowering their average resident's electricity bill by six to eight percent. Under the terms of the agreement, Green Mountain will also build a 10MW wind turbine in Ohio and install photovoltaic systems on school buildings throughout the NOPEC area.

This summer California enacted AB48x, which authorizes municipalities or groups of cities to negotiate power supply and energy services agreements on behalf of their residents and businesses. As currently written, the bill also gives communities the opportunity to apply to the state for funds paid by their residents into the state's conservation and renewables

funds. Communities would then be able to determine locally how those funds are to be spent, rather than leave them in the hands of private utilities that have an economic incentive to transmit as much power as possible over their wires.

—DK



Six States Preempt Local Living Wage Laws

In June, Oregon became the sixth state in the nation to restrict the power of local governments to enact living wage ordinances. A new state law prohibits cities and counties from setting a minimum wage higher than the state minimum of \$6.50 an hour, except with regard to public agencies and companies that receive government subsidies or contracts.

The law will not affect existing living wage laws in Portland and several other Oregon communities, because they apply only to city contractors and subsidized companies.

Since 1994, more than 60 cities and counties have enacted living wage ordinances, which are designed to bring wages closer to a level capable of meeting basic needs. Portland, for example, mandates that city contractors pay \$8 an hour plus \$1.50 an hour in benefits.

Oregon's new law will prevent cities from taking the next step: mandating a higher minimum wage for all companies operating within their borders. The law was spearheaded by the Oregon Restaurant Association. It is part of a growing national campaign by several industry groups to halt the living wage movement. Five other states have already preempted local authority. Utah prohibits all local living wage laws, even those that apply only to city contractors. [!]

—SM

Rogue Agencies Gut State Banking Laws

The only reason you're not afraid of the Office of the Comptroller of Currency and the Office of Thrift Supervision is because you don't know what they do. Called indentured servants to the national banking industry, they are dismantling the state regulatory system piece by piece, with nothing more than a polite scolding from Congress. *By Stacy Mitchell*

If George W. Bush means what he says about states' rights, then he'll use his new post to rein in two rogue federal agencies that have systematically gutted the ability of state policymakers to protect their citizens from greedy and unscrupulous banks.

Few Americans have heard of the Office of the Comptroller of Currency (OCC), the chief regulator of national banks, or its sister agency, the Office of Thrift Supervision (OTS), which regulates thrifts (savings and loans). Yet these two unelected agencies—they're both part of the Treasury Department and are headed by presidential appointees—have preempted numerous state banking laws designed to prevent anticompetitive practices, ensure fair lending and protect consumers.

"Time after time when states have tried to come up with creative and reasonable solutions to very real consumer problems," observes Santa Monica City Attorney Adam Radinsky, "the OCC has stepped in to tie their hands."

In some cases, the agencies have preempted state authority with the blessing of Congress. But in many

instances they have acted in ways directly at odds with the express intention of federal lawmakers. "The OCC's actions on preemption appear to be more those of an indentured servant of the industry than a regulator concerned with the will of Congress," argues Ed Mierzwinski, consumer program director for the U.S. Public Interest Research Group.

In 1994, Congress formally reprimanded the OCC for "inappropriately aggressive" preemption activities, concluding that the agency had preempted state laws that Congress had no intention of overriding. The OCC ignored the reprimand and has actually accelerated its preemption actions in the years since.

Traditional role of states in overseeing national banks

Historically, banks have been subject to both federal and state oversight. National banks—those chartered at the federal, rather than state, level—have been required not only to comply with federal rules and regulations, but also the laws of the states where they operate. In crafting banking laws, Congress has generally chosen to provide a basic framework of regulation and to establish minimum standards. States have been allowed to enact additional rules and higher standards, particularly with regard to consumer protection, an area Congress has largely viewed as a state responsibility.

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There are multiple benefits to such an approach. States are more nimble than Congress and better able to respond to industry changes. The challenges and needs of rural communities in Maine are often quite different from big cities in California. States can function as a laboratory of ideas; effective policies develop a track record and are copied elsewhere. Unlike federal laws, bad policies adopted in one state will not undermine the entire financial system.

A good example of this principle in action can be found in the Congressional approach to regulating automated teller machines (ATMs). In 1978, Congress enacted legislation “to provide a basic framework establishing the rights, liabilities, and responsibilities” of both purveyors and users of this new technology. The law contains a variety of consumer protections, but expressly authorizes states to establish more stringent standards.

Not surprisingly, state laws governing ATMs evince differing circumstances and priorities. New York lawmakers were concerned about safety and required adequate lighting and surveillance cameras at all ATM locations. Iowa lawmakers felt universal access was necessary in a state with a relatively sparse population of both people and ATMs. They mandated that ATMs be networked in such a way as to enable any resident with a cash card to withdraw money from any machine. Neither safety nor universal access is addressed in the federal ATM law.

Lifeline bank accounts

Ensuring that banks meet the needs of local residents has long been the responsibility of state policymakers. So, in early 1991, as legislation requiring all banks to provide basic, low-cost checking accounts moved through the New Jersey statehouse, no one ques-

tioned whether the state had the authority to act.

Industry deregulation and a wave of mergers in the 1980s had caused the cost of basic banking services to skyrocket. Banks stopped paying interest on deposits and began charging fees for everything from visiting a teller to writing a check. As a result, millions of Americans could no longer afford bank accounts and were forced to operate on a cash-only basis. Check cashing outlets proliferated.

New Jersey legislators responded by requiring all banks operating in the state to offer a no-frills, low-cost checking account. This “lifeline” account must include eight free checks per month, a minimum balance of only \$1 and monthly fees of no more than \$3. All residents without a current checking account are eligible.

The law could hardly be considered burdensome to national banks. It specified that no bank would be required to offer an account below its actual costs and authorized state regulators to grant exemptions. Many national banks already offered accounts that qualified.

But before the law took effect, the OCC determined that New Jersey’s law was preempted by federal law and authorized national banks to ignore its provisions. The agency based its opinion on the Bank Enterprise Act (BEA), in which Congress had given its blessing to low-cost accounts by providing financial incentives to banks that offered them. Nothing in the BEA indicates that Congress had any intention of overriding state efforts to make bank accounts more widely available. Yet the OCC ruled that, because Congress had legislated in this area, it was now off-limits to the states.

At the time, many other states were moving to enact legislation similar to that of New Jersey. The OCC’s action brought these efforts to an abrupt →



halt. Although a handful of states have since enacted some form of low-cost banking legislation, none of these laws apply to national banks, which control nearly 60 percent of all bank deposits. Today, according to a recent estimate by the Federal Reserve, 13 percent of families lack a checking account.

The will of Congress?

The OCC contends that it is merely carrying out the will of Congress when it preempts state laws. "The OCC does not choose 'to preempt,' it is federal law that preempts," insists Comptroller John Hawke, Jr., the agency's head.

Congress itself has reached a different conclusion. In the Conference Report that accompanied the 1994 Riegle-Neal Act on interstate banking, Congress admonished the agency for acting outside the scope of federal law:

[T]he Conferees have been made aware of certain circumstances in which the Federal banking agencies have applied traditional preemption principles in a manner the Conferees believe is inappropriately aggressive, resulting in preemption of State law in situations where the federal interest did not warrant that result. . .

The report singles out two instances of OCC preemption that lawmakers found especially egregious. One was the agency's preemption of New Jersey's lifeline checking account law. "[T]he fact the Congress has acknowledged the benefits of more widespread use of lifeline accounts through the enactment of the Bank Enterprise Act," the conferees wrote, "did not indicate that Congress intended to override State basic banking laws. . ."

With Congressional support in hand, the New Jersey banking department requested that the OCC review its preemption decision. The agency published notice of the review and a request for comment in early 1996. Five years later, however, the OCC has yet to issue a ruling on the matter.

Indeed, in the years since the Congressional reprimand, the OCC's preemption efforts have only accelerated. "The OCC has given national banks the impression that they can do whatever they want," contends Iowa Assistant Attorney General Kathleen Keest. National banks now routinely request cover from the OCC when they encounter a state law with which they'd rather not comply. The agency invariably obliges and has joined banks in several lawsuits aimed at overturning state laws.

The OCC's opinions carry significant weight in the courts. The Supreme Court has held that judges must give deference to the opinions of regulatory agencies. If the meaning of a federal law is ambiguous, as it often is, then the courts decide only whether the OCC's interpretation is reasonable, not whether it is the best or most substantiated reading of Congressional intent. As the OCC consistently favors preempting state authority, the effect of deference has been to undermine federalism.

In 1996, the Supreme Court heard a case brought by California credit card customers against Citibank for charging late fees prohibited by California law. The 1863 National Bank Act authorizes national banks to charge "interest at a rate allowed by the laws of the State. . . where the bank is located."

In 1978, the Court had ruled that the words "where the bank is located" refer to the bank's home state, not the state where the customer resides or where the loan is issued. This enables banks to establish credit card offices in states with lenient lending rules and thereby evade usury laws in other states.

Citibank's credit card headquarters is in South Dakota, which does not cap interest rates.

The question before the Court in the Citibank case was whether late fees qualify as interest. If so, they would be subject to the laws of South Dakota, not California. As the case wound its way through the legal system, the OCC issued a new regulation to extend the meaning of interest in the National Bank Act to cover all manner of credit card

fees, including late fees. As a result, by the time the case reached the Supreme Court, the issue was no longer whether Congress had intended in 1863 to revoke the right of states to restrict credit card fees. Instead, the Court considered only whether the OCC's interpretation of the meaning of "interest" was reasonable. The Court concluded it was.

State ATM laws

Big banks are especially intent these days on evading state laws governing ATMs and other forms of electronic banking. These technologies are not only a rich source of revenue, they're the industry's future. National banks want to operate their ATM networks without regard to local rules and be bound only by the limited consumer protections found in federal law.

In 1998, Bank One, which owns the largest fleet of ATMs in the nation, sued the state of Iowa. It argued that, as a national bank, it was exempt from several provisions of the state's ATM law. Bank One enlisted the support of the OCC, which filed a friend-of-the-court brief on behalf of the bank.

The OCC's argument hinged on what Iowa Attorney General Thomas Miller termed a "minor definitional change" in the 1996 Paperwork Reduction Act. The sentence in question amended the major federal law governing national banks, the National Bank Act (NBA), to indicate that ATMs are not "branches." Since states are allowed to regulate national banks that "branch" into their borders, the OCC contended, if ATMs are not branches, then states cannot regulate them.

Within this bit of legalistic acrobatics, it's hard to divine a clear Congressional intent to override state authority. The amendment offers the only mention of ATMs in the entire NBA. The Paperwork Reduction

Act was designed to reduce unnecessary paperwork. As the heading of the definitional change clearly spells out, its purpose was to eliminate the need for banks to file lengthy branch office applications every time they install a cash machine. Not only is the OCC's interpretation a stretch, it must be weighed against the 1978 federal ATM law's clear language preserving state authority: "This subchapter does not annul, alter, or affect the laws of any State relating to electronic fund transfers, except to the extent that those laws are inconsistent with the provisions of this subchapter, and then only to the extent of the inconsistency. A State law is not inconsistent with this subchapter if the protection such law affords any consumer is greater than the protection afforded by this subchapter."

the laws of any State relating to electronic fund transfers, except to the extent that those laws are inconsistent with the provisions of this subchapter, and then only to the extent of the inconsistency. A State law is not inconsistent with this subchapter if the protection such law affords any consumer is greater than the protection afforded by this subchapter."

Nevertheless, the 8th Circuit Court of Appeals sided with the OCC, overturning a lower court ruling and voiding two provisions of Iowa's law as it applies to national banks. One involved a restriction on advertising on ATMs. The other required a bank to establish a branch office, or partner with a bank already operating in the state, before installing an ATM. The latter rule was designed to ensure that consumers could quickly and easily seek redress for ATM malfunctions.

In a co-signed brief, twenty state attorneys general contend the ruling could "have a chilling effect on state initiatives to protect consumers as national banks have methodically cornered the ATM market in many communities." In Iowa, national banks have not in fact cornered the ATM market—at least not to the degree they have elsewhere. Four banks own fewer than 20 percent of all the ATMs in Iowa. By comparison, in Massachusetts just two banks control more than 65 percent of the machines.

Iowa's more competitive market largely results from the unique structure of its ATM network, as mandated by state law. Unlike networks in other states, banks and credit unions of all sizes have an equal say in network decisions. This has produced one of the most equitable and lowest cost ATM systems in the nation. But if the OCC has its way, innovative state laws like Iowa's will be overturned in favor of a one-size federal regulation that fits no one save a handful of the nation's largest banks. →

ATM surcharges

In 1999, two California cities, San Francisco and Santa Monica, banned surcharges, the fees consumers pay to use an ATM operated by a bank other than their own.

There are two primary reasons for banning surcharges. One is to protect consumers from excessive bank fees. The other is to prevent big banks from using their market power to undermine smaller rivals. By imposing surcharges, banks that own a dominate share of the ATMs in a local market can induce customers of smaller banks to move their accounts to one of the large banks in order to avoid the fees. As David Balto of the Federal Trade Commission has noted, surcharges “present a perverse form of price competition where firms can actually gain customers by raising prices. . .”

Eliminating surcharges does not mean banks must provide ATM service for free. Banks are in fact already compensated for providing ATM service to noncustomers through an inter-network fee paid by the customer’s own bank.

Shortly after San Francisco and Santa Monica prohibited surcharges, Bank of America and Wells Fargo sued the cities in federal court. The two banks own 86 percent of the ATMs in San Francisco and 72 percent in Santa Monica.

The OCC filed a friend-of-the-court brief in support of the banks. The agency argues that the federal ATM law, with its express preservation of state authority, is not the relevant statute under which the case should be decided. Instead, the OCC contends that the controlling statute is the NBA, which authorizes banks to exercise, “subject to law, all such incidental powers as shall be necessary to carry on the business of banking.” Charging fees is an incidental power, according to the agency, and cannot be restricted by state or local laws.

The cities argue that such an expansive reading of the NBA directly contradicts the intent of Congress as spelled out in the federal ATM law. Moreover, the NBA itself does not authorize banks to charge fees and expressly preserves the right of states to regulate national banks.

In fact, among the instances of unwarranted preemption singled out by Congress in 1994 was an OCC regulation that empowered national banks to charge fees without regard to state law. Congress rejected this blanket preemption of state authority and ordered the OCC to revise its rule. The new regulation indicates that questions of preemption will be decided on a case-by-case basis, implicitly acknowledging that in some cases states do have the authority to limit bank fees.

This regulation and its Congressional history are completely inconsistent with the OCC’s argument in

the surcharge case, according to San Francisco Deputy Attorney Owen Martikan. In what can only be seen as an attempt to remove this inconsistency, in January the OCC issued notice that it planned to revise the regulation. “It’s more than suspicious that they would do this two weeks after final briefs were filed, when we can’t respond,” says Martikan.

The case is currently before the 9th Circuit, which is not expected to rule for at least a year. In April, five national banks likewise filed suit, with the support of the OCC, against Iowa’s surcharge ban. Iowa is the only jurisdiction that currently prohibits the fees. Meanwhile, the threat of preemption and litigation have brought consideration of surcharge laws in dozens of cities and states to a standstill.

Predatory lending

“Preemption is the 500-pound gorilla in the closet waiting to pounce on whatever states do,” says North Carolina Assistant Attorney General Phil Lehman. “It’s immensely frustrating.”

North Carolina is one of several states trying to stop predatory lending, a fast-growing practice that targets low-income and elderly borrowers with high-cost home loans. Predatory loans have high interest rates and are loaded with unnecessary fees. They’re often structured to keep the borrower in perpetual debt, by, for example, including one large balloon payment at the end of the loan. Unable to pay, the borrower will be forced to refinance. In the worst cases, the lender will “flip” or refinance the loan repeatedly to earn additional fees.

Many borrowers saddled with predatory loans actually qualify for less expensive mortgages. Those who try to refinance with another lender, however, find that steep prepayment penalties—as much as 5 percent of the principal—make getting out of the loan impossible.

Predatory lending expanded rapidly in the 1990s. Between 1993 and 1998, the number of high interest, sub-prime loans—not all of which are considered predatory—issued each year grew from 80,000 to 790,000. Foreclosures also climbed dramatically, particularly in low-income minority neighborhoods. Many of the nation’s top banks and mortgage companies, including Citibank and First Union, are engaged in predatory lending, either directly or through a subsidiary.

Responding to rising interest rates in the late 1970s, federal lawmakers exempted housing creditors from certain state laws. The goal was to increase the supply of credit and relieve strapped savings and loans, which, at the time, accounted for half of all home lending. Over the years, the OTS and OCC have steadily expanded the scope of these exemptions,



rendering states virtually powerless to protect their citizens from predatory lenders. A 1979 federal law, for example, exempted most residential mortgages from state interest rate caps. Although the legislative history suggests Congress intended the law for home purchases only, in the mid 1980s, the OTS concluded that it applies to other types of loans, provided they are secured by a lien on the borrower's home. This encourages lenders to make loans for cars and other purchases contingent on refinancing the consumer's mortgage. The refinanced mortgage, including the car loan, is thus free from state usury limits. Moreover, the lender can foreclose on the home, rather than repossess the car, should the borrower default. It's a bad deal for consumers and frustrates the original purpose of the 1979 law, which was to expand home ownership.

Unable to cap interest rates, state policymakers have tried to stamp out predatory lending by targeting particular terms and conditions common to predatory loans. Nearly half the states, for example, ban or restrict prepayment penalties, which lock borrowers into unfavorable loans. More than 70 percent of sub-prime loans carry prepayment penalties, compared to only 1 percent of prime loans (those made to borrowers with solid credit histories). Under OCC and OTS regulations, however, state restrictions on prepayment penalties do not apply to national banks and thrifts.

Moreover, in 1996, the OTS concluded that state-licensed housing creditors are also exempt. These nondepository mortgage companies make more than half of all home loans and are responsible for most

predatory lending. The OTS based its decision on the 1982 Alternative Mortgage Transaction Parity Act, which authorized housing creditors to issue adjustable-rate loans regardless of state laws limiting such loans. Following the OTS opinion, lenders challenged prepayment laws in several states, bringing lawsuits against both New Jersey and Virginia. Thus far, the courts have sided with the OTS.

The OTS itself provides only limited consumer protections and has yet to strengthen these rules in response to the growing predatory lending crisis. In a letter last year, 46 state attorneys general accused the OTS of contributing to the crisis and urged it to restore state authority. "We tend to look with disfavor on attempts to preempt state laws designed to protect our citizens, particularly when the federal regulatory scheme offers no similar protections," they wrote.

Payday loans

State policymakers are likewise powerless to protect consumers from a new breed of loan sharks. Known as payday lenders, these companies make small loans based on personal checks held for future deposit. A consumer might, for example, write a check for \$120 and receive \$100 in cash. The lender agrees to cash the check two weeks later, on payday. These loans carry a 300 to 900 percent APR. Many borrowers end up in perpetual debt, rolling the loan over every two weeks for another \$20 fee. Payday lenders made an estimated \$10 billion in loans last year, earning \$2 billion in fees.

Most states have regulated or outlawed payday lending. Nearly twenty states cap interest rates on →

small loans at about 36 percent APR. Others limit the amount of the loan or require certain disclosures to borrowers.

But payday lenders have found a way around these laws by partnering with national banks and thrifts. They claim their affiliation with federally chartered institutions grants them immunity from state laws. Dollar Financial Group, the nation's second largest check-cashing chain, for example, has partnered with Eagle National Bank and is making payday loans in at least four states in defiance of their laws.

National banks and thrifts are essentially renting their federal charters—and all the powers inherent—to payday lenders. Thus far, there's been no penalty. The OCC has even given Eagle a satisfactory evaluation under the Community Reinvestment Act. The agency only considered the bank's activities in the four counties surrounding its Illinois headquarters. The 250 locations where its Dollar affiliates drain money out of low-income neighborhoods were not counted.

Years of overly aggressive, unwarranted federal preemption have had a chilling effect on efforts to challenge these rent-a-charter schemes in court. When California consumers sued Dollar for violating the state's usury law, they took an early settlement offer, explaining, "We were also concerned, frankly, that the OCC would likely weigh in on the defendants' side. . ."

Congressional failure

Congress had an opportunity to curb preemption abuses by the OCC and OTS in 1994, as lawmakers considered the monumental Riegle-Neal Act on interstate banking. In day after day of testimony, consumer advocates and state officials, as well as members of Congress, hammered the agencies' track records on preemption.

In the end, however, Congress did little. Lawmakers reprimanded the OCC for preempting New Jersey's lifeline bank account law, which remains overturned, and ordered the agency to be especially mindful of state authority "regarding community reinvestment, consumer protection, fair lend-

The core of the Riegle-Neal Act, in a nutshell, authorizes banks to establish interstate branches and requires them to comply with state laws, except where those laws are preempted by federal statute. Determining what laws are preempted was left to the OCC and OTS, despite their long history of unwarranted preemption.

ing, or establishment of intrastate branches." State laws in these areas should be overturned only when "the Federal policy interest in preemption is clear" and after a public comment period.

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left to the OCC and OTS, despite their long history of unwarranted preemption.

Financial modernization: banks target state insurance laws

Congress had another significant opportunity in 1999 as lawmakers debated the Gramm-Leach-Bliley Financial Modernization Act (GLBA), which demolished barriers among banks, insurance companies, and securities firms. The legislation allows banks to sell insurance products, exposing a whole new vein of preemption issues. Insurance companies are state-licensed and monitored, and regulation of the industry has always been left in the hands of the states. Now, however, with national banks offering insurance products, the future of state authority is uncertain.

National banks have been working their way into the insurance business for quite some time. In 1916, the OCC successfully lobbied Congress to allow banks in towns of fewer than 5,000 to sell insurance. In 1971, the agency adopted regulations allowing banks to sell insurance in small towns from branch offices, even if their main office was located in a big city. In 1986, the OCC ruled that banks could sell insurance nationwide, provide they had a branch in a small town.

With GLBA, Congress further extended banks' powers with regard to insurance and formally entered the dispute over state authority.

At first blush, the legislation appears to favor maintaining state control over insurance. It gives states the power to regulate all sellers of insurance, including national banks, and establishes thirteen "safe harbors," or specific state law provisions that cannot be preempted. It also requires courts to give equal deference to state officials and federal regula-

tors in cases involving insurance sales by national banks. The deference provision and safe harbors were largely the result of lobbying by insurance companies, who feared that they would be subject to state laws that national banks could evade. For once, consumer advocates and state officials had muscle on their side almost as powerful as banks.

But, ultimately, GLBA is more of the same. Under the law, no state may “prevent or significantly interfere with” the ability of national banks to offer insurance. What constitutes interference is a question left to the OCC. Given the agency’s history, states have serious concerns. Already, with the swaggering confidence of an industry accustomed to having its way with federal regulators, national banks have petitioned the OCC to preempt laws in Massachusetts, Rhode Island and West Virginia.

The laws in question are designed to prevent banks from taking advantage of their loan customers’ vulnerability when selling insurance. West Virginia’s law, for example, bars banks from selling insurance to a customer whose loan application is currently under consideration. It requires that lending and insurance occupy separate sections of the bank office, each with their own staff. More than half the states have similar laws. The OCC has taken public comments, but has not yet issued a decision.

Although insurance companies are currently fighting the battle for state authority, that probably won’t last for long. The industry plans to push for an optional federal charter, enabling individual companies to choose either a state or federal charter, much as banks and thrifts do. Moreover, as banking, insurance and securities firms merge into giant conglomerates, they will pose an even more formidable political force for eroding state authority than banks alone.

Giving power back to the people

Over the last decade, the Federal Reserve has documented sharp increases in the cost of basic banking services. The Fed has also found that those banks and thrifts that have benefited the most from OCC and OTS preemption actions—a handful of giant national banks that now dominate most local markets—are far more expensive than smaller financial institutions. On everything from checking account fees to stop-payment and ATM fees, banks with more than \$1 billion in assets charge substantially more than banks with less than \$100 million in assets.

Banking is costly to those who can afford it, but it is even more costly to those who cannot. Many low-income neighborhoods no longer have local banks and branch offices. They must instead rely on check cashing outlets and fee-laden ATMs. Predatory mort-

gages and payday loans further drain wealth from these communities. The OCC’s failure to account for this in evaluating a bank’s Community Reinvestment Act compliance has skirted the purpose of this important law and enabled banks to escape their obligations to low-income neighborhoods.

The aggressive preemption actions of federal regulators have not only gutted state banking laws, but impeded the passage of an unknown number of new initiatives. Massachusetts recently narrowed a new law limiting the amount banks could charge recipients of bounced checks to apply only to state-chartered banks. The legislature cited fears of OCC preemption.

“Banks are playing the state and national charters against one another to get the lowest possible denominator,” contends consumer advocate Mary Griffin. States are reluctant to require state-chartered banks to comply with rules that national banks may evade. Often these laws are repealed entirely. “The state regulatory system is coming undone,” says Griffin. “It’s an ever-accelerating race to the bottom.”

The OCC has a direct interest in expanding the powers of national banks. The bigger and more powerful they are, the bigger and more powerful it is. By giving national banks a green light to evade state laws and comply only with its own minimal regulations, the OCC can attract more banks to the national (as opposed to state) charter and thereby expand its own turf.

Congress should immediately remove the deference given to federal regulators in the courts. The presumption should be in favor of state authority, not against it. Congress should also redefine the term “location” in the National Bank Act to mean the location of the consumer or the transaction, not the bank’s home state. This would enable states to fulfill their original role in establishing consumer lending protections for their own citizens. Finally, Congress should review the state laws overturned by the OCC and OTS, and reinstate local authority where appropriate.

The OCC and OTS are part of the Treasury Department and are led by presidential appointees. If President Bush fails to demand that these agencies respect state authority, it will provide a clear indication that his states’ rights agenda has little to do with restoring democratic decisionmaking at the local level, and more to do with limiting that authority at the national level. [!]

On the Cutting Edge

A law requiring in-state processing helps keep Idaho's timber industry thriving while harvests decline and sawmills close across the Pacific Northwest.

By Sarah Hannigan

In 1989, raw log exports from the United States peaked at 4.7 billion board feet,¹ enough to build over 313,000 homes. The amount of unprocessed timber exported from the Pacific Northwest alone would have filled 800,000 logging trucks.

Logging communities (or agricultural and mining communities in general) gain little when their principal resource is exported unprocessed. In the case of wood, every million board feet of timber harvested in the United States in 1995 supported about 12 jobs in forestry and wood products manufacturing.² In some areas, more than two-thirds of these jobs are in primary and secondary processing.³ (Lumber and pulp, for example, result from primary processing; secondary processing yields furniture, paper and other finished products).

To strengthen their economies, several states have attempted to inhibit the export of raw logs—and processing jobs—by requiring that timber cut from state-owned forests be processed within the United States. Two states have taken the export ban a step further, requiring the primary processing to occur at mills within the state.

About 12 percent of all timberland in the United States is publicly owned and managed by individual states, counties and local governments. The proportion varies dramatically by state. In Alaska, for example, less than 3 percent of timberland is classified as nonfederal public forest, while in Minnesota the figure jumps to about 37 percent. Nine percent of Idaho's forests fall into this category, as does 12 percent of Washington's timberland.⁴

Idaho was the first state to mandate in-state processing for logs harvested from state forests. Since becoming a state in 1890, Idaho has required all timber sales from state lands to “be manufactured into lumber for timber products with the State of Idaho.”⁵

In 1974 Alaska began requiring primary processing of all raw logs from state lands prior to export.

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Initially the processing had to take place within the United States. In 1982 the processing requirement became a local processing mandate. All primary manufacturing was to take place at mills within the state. Round—or unprocessed—logs were ineligible for export as a marketable commodity.

The axe fell on these state-level initiatives in 1984 when the Supreme Court declared Alaska's law unconstitutional. In *South Central Timber v. Wunnicke*⁶ the Court concluded that requirements for in-state processing interfered with interstate commerce. States lacked the authority to enact such legislation, unless the federal government explicitly granted them that authority, or unless the state directly participates in the timber market. The court found Alaska to be imposing restrictions on a market that it did not directly participate in—Alaska's law unjustly regulated downstream activity by imposing conditions on post-purchase activity of the buyer, rather than just the purchasing activity.⁷

In response to the *South Central* ruling, Idaho's attorney general decided that the state's export restriction was also unconstitutional. The state agencies charged with coordinating timber sales were ordered to cease enforcement of the primary processing requirement.

In the years following the *South Central* ruling, harvest for export stepped up in state forests. By 1989, for example, less than 1 percent of timber harvested in Oregon originated from state-owned lands, yet logs from these forests accounted for about 9 percent of total exports. Along with the raw logs, processing jobs were flowing overseas. Japan boasted over 18,000 sawmills in the late 1980s, almost 100 times the number of mills in the Pacific Northwest.

Idaho's new rule

In 1989 Idaho reestablished its in-state processing requirements for almost all state timber. Under the Timber Supply Stabilization Act (TSSA), 95 percent of Idaho's state timber is offered to qualified bidders

each year. A qualified bidder is essentially an Idaho processor—that is, she has historically processed at least 95 percent of state timber within the state, or has sold at least 95 percent of the timber to other in-state processors. The remaining five percent of state timber sales are open to all bidders. As a result, the Act guarantees about 156 million board feet of timber for local processing each year, enough wood to build about 10,400 houses.

Idaho's new law relies on a state constitutional provision that requires state forests be managed "in such manner as will secure the maximum long-term financial return... to the state."⁸ The TSSA defines "maximum long-term financial return(s)" as those "derived from processing within Idaho timber from state forests because this sustains a healthy forest products industry in Idaho."⁹

Idaho's law also attempts to address the Supreme Court's reasoning. Under the rule, the state is "to act as a market participant in the timber market in a way that helps enhance the long-term maximum value of state forests by ensuring that an adequate proportion of the total sales... is sold to qualified purchasers within Idaho."¹⁰ By defining the state's role as a participant and not a regulator, Idaho's provision may pass constitutional muster where Alaska's provision failed. Under the market participant doctrine, states are allowed "to impose burdens on commerce within the market in which it is a participant,"¹¹ and are considered exempt from commerce clause scrutiny.

Opposition to Idaho's act is strongest in Washington State. Washington's lumber industry claims that Idaho's law unfairly keeps Idaho timber from Washington bidders while all of Washington timber is open to Idaho



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early 1990s, annual harvests from national forests were curtailed in response to environmental and economic concerns. The reduced volume of timber was a major setback to the wood processors across the Pacific Northwest and Alaska. At the same time, technological advances in sawmilling reduced the number of people needed to process timber. Increased import of processed lumber from overseas has also adversely affected the industry.

In Idaho, the total amount of timber harvested has also declined, by about 30 percent over the last decade. Yet employment in Idaho's wood products sector has remained stable since the 1960s. This may be attributed to the fact that very little of the timber har- →

processors. Along the border between the states in early 2000, no mills operated to the west, while several hummed in Idaho's panhandle.

Unfortunately, Washington's constitution, unlike that of Idaho, doesn't require that its natural resources be used to maximize the long-term benefit of the state. Instead it mandates that sales originating from state lands be sold "to the highest bidder."¹² As a result, much of Washington's timber went overseas in the late 1980s, when bids from foreign ports were as much as twice that of domestic mills.

Despite a 1990 federal law banning overseas export of unprocessed timber from state forests, many of Washington's logs are still processed elsewhere. In 1995, Washington's Department of Natural Resources reported that highest bids for 35 percent of its timber sales came from out of state.

Idaho's law may have helped the state's forest products industry flourish despite industrywide pressures that closed sawmills across the Pacific Northwest and Alaska. In the

vested from all forests in Idaho leaves the state unprocessed.

In 1995, 97 percent of the Idaho's total harvest remained in-state. That year every million board feet harvested in Idaho supported approximately 4.5 jobs in the forestry sector, 5.6 jobs in primary products manufacturing (dimensional lumber, plywood, pulp, etc), and 4.4 jobs in secondary products manufacturing (furniture, windows, paper, etc).¹³ At this point, Idaho's forest products industry employment exceeded the national average by nearly two-and-a-half jobs per million board feet.

While total employment remains steady, the sector continues to change. Recently Idaho has experienced a substantial shift in employment from primary products manufacturing to secondary products manufacturing. This shift has also been geographic. Primary processing employment in the timberlands to the north is being replaced by secondary manufacturing jobs in the southern part of the state. And Idaho is not immune to the woes felt by the forest industry nationwide. In February, Boise Cascade announced that by mid-2001 the company will no longer process wood in Idaho.

Idaho's law is not the only one of its type in the nation. In Alaska, legislation has created timber sale programs that assure that a portion of logs from state lands will be sold to local processors. However, only about 3 percent of the timber harvested in Alaska comes from state forests. According to Mike Curran, a forester with the state's Division of Forestry, "state timber sales alone can't keep the industry going."

But in Idaho over the last twenty years, more and more of the state's total timber harvests are comprised of logs from state forests. In 1985, state timber made up 11 percent of the total harvest; almost 14 percent of 1995's harvest came from state lands. With cutbacks on logging in federal forests, state timber is increasingly important in Idaho. In 1989, for every board foot felled in state forests, more than 4 board feet were harvested from federal forests. Today, the volume of state timber harvested and sold exceeds that of federal timber.

Idaho legislation requiring state timber to be sold to in-state processors helps ensure that the value added through processing will remain in-state—and this mandate may be all that stands between a local forest products industry that's thriving and one that's disappearing. [!]

Notes

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2. Wood products industry employment (forestry services, lumber wood products, pulp and paper sectors) per million board feet harvested. Personal communication, April 2001, with Charles Keegan, director of Forest Industry Research at the Bureau of Business and Economic Research, University of Montana.
3. *Ibid*, Idaho statistics for 1995.
4. Rachel Hodgetts and Roseanne Freese, *An Economic Overview of the United States Solid Wood Industry*, Forest and Fishery Products Division, USDA Foreign Agricultural Service, September 2000. <http://www.fas.usda.gov/ffpd/Economic-Overview/ownership.pdf>
5. Idaho Code Sect. 58-403, (1958).
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7. *Ibid*.
8. Idaho Constitution, Article IX, Section 8.
9. Timber Supply Stabilization Act of 1989, Idaho Code Section 58-1002.
10. Timber Supply Stabilization Act of 1989, Idaho Code Section 58-1001.
11. *South Central Timber v. Wunnicke*, 467 US 82, 1984.
12. Washington Constitution, Article XVI, Section 2.
13. Personal communication, Charles Keegan.

Feds Swat State Support for Medical Marijuana



For more than 20 years states have been passing legislation designed to allow their citizens to use marijuana as medicine, and for more than 20 years, federal agencies, Congress and the Supreme Court have stymied these efforts. *By Daniel Kraker*

The Supreme Court decision about medical marijuana and George Bush's nomination of John Walters as the next drug czar offer further evidence that even in a democratic society, the will of people sometimes is not acknowledged—even after years of effort. The struggle to allow marijuana to be used as a medicine has entered its fourth decade.

In 1970, with the Vietnam War still raging, the Beatles still together, and Secretariat yet to run his first race, Congress passed the Federal Controlled Substances Act, which divided narcotics into five categories. Marijuana was assigned Schedule I status, which is reserved for drugs with “a high potential for abuse” and “no currently accepted medical use in treatment in the United States.” In its infinite wisdom, Congress declared marijuana a more dangerous drug than cocaine—which was assigned to Schedule II, allowing doctors to prescribe it.

In 1972, the citizenry tried to change the law by going to the regulatory agency involved, the Bureau of Narcotics and Dangerous Drugs (forerunner of the Drug Enforcement Administration, or DEA). The National Organization for the Reform of Marijuana Laws (NORML) petitioned to move marijuana to Schedule II. For years the DEA refused even to hold hearings. Finally, in 1988, the DEA Chief Administrative Law Judge, Francis L. Young, recommended that doctors be able to prescribe marijuana. “Marijuana, in its natural form,” he noted, “is one of

the safest therapeutically active substances known . . . It would be unreasonable, arbitrary and capricious for DEA to continue to stand between those sufferers and the benefits of this substance.”

Young was overruled by the DEA Administrator. Two appeals later, in 1994, the D.C. Circuit Court of Appeals ruled that the DEA can reject its own judge's ruling and establish its own criteria for deciding whether to reschedule a controlled substance.

Medical marijuana advocates have also tried to petition Congress. U.S. Representative Barney Frank has introduced the “Medical Use of Marijuana Act” every year since 1997. The bill would allow states to determine for themselves whether marijuana should be legal for medicinal use. But it has yet to make it out of committee. Indeed, in September 1998, with no public hearings, the House of Representatives approved 310 to 93 a “sense of the Congress” resolution that it is unequivocally opposed to medical marijuana.

Federal remedies, both regulatory and legislative, have been exhausted.

Early state action

Since the passage of the Federal Controlled Substances Act citizens have also worked tirelessly for change at the state level. In 1978 Illinois passed the first marijuana research law. Eventually 25 other states would follow suit, although only seven ever obtained the necessary federal permissions and actually distributed the drug to patients. Under these programs, patients suffering from glaucoma and cancer could qualify to receive marijuana as part of their treatment. →

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The federal government supplied the marijuana as part of the Compassionate Investigate New Drug (CIND) program, which was created in 1978 as part of a court settlement with a man who was using marijuana for medical purposes.

New York's program was one of the most successful—at one time enrolling 208 patients. Over a four-year period patients received approximately 6,000 government-supplied marijuana cigarettes during more than 500 treatment episodes.

Despite their successes, all state-sponsored therapeutic programs were disbanded in the 1980s. Those involved in the programs say they were red-taped to death. Doctors were discouraged because of the rigorous application requirements for a federal Investigative New Drug (IND) permit; patients were required to complete reams of paperwork; states were forced to follow rigid guidelines set by the FDA and DEA, and thus couldn't streamline the process themselves.

The final deathblow to research programs was the FDA's 1986 decision to approve Marinol, a synthetic THC pill, as a Schedule II drug. Most states believed that further research was pointless after Marinol became available, even though patients and doctors, including the National Institute of Health, concluded that there are medical benefits associated with smoked marijuana that cannot be reproduced in Marinol. Marinol is also prohibitively expensive—as much as \$10,000 per year.

The CIND program was suspended in 1991 after being flooded with applications from AIDS patients. It was permanently disbanded a year later. As a result, only eight surviving patients still receive marijuana from the federal government.

Another more symbolic tack taken by states over the past two decades has been to pass laws allowing doctors to prescribe marijuana. Illinois became the first to do so in 1979, and was quickly followed by Virginia, Connecticut, New Hampshire, Vermont, Wisconsin and Louisiana. Four states—Alaska, Iowa, Montana and Tennessee—have voted to reclassify marijuana as a Schedule II drug, which would also allow it to be prescribed. Washington D.C. went so far as to move it to Schedule V. At least six states have passed nonbinding resolutions urging the federal government to reclassify marijuana.

State action, part II

By 1996, 35 states and the District of Columbia had passed laws favorable to medical marijuana. 30 of those were still on the books. But they were more symbolic than effectual.

In California, the state legislature had twice approved a medical marijuana bill. Both times the bill

was vetoed by Governor Pete Wilson. Finally, in 1996, Californians took power into their own hands. Frustrated by the government's inability to accede to the will of its citizens, they gathered the signatures to place Proposition 215 on the ballot, and overwhelmingly approved it.

California's initiative succeeded where past state efforts failed because it was purposely limited in scope. It only allowed physicians to "recommend" marijuana, thus avoiding the federal ban on its prescription. It didn't create any new bureaucracies or state agencies, which would have required taxpayer dollars. And it didn't try to solve the problem of supplying marijuana to patients, which would also run amok of federal laws. Since 1996 seven additional states, and Washington, D.C., have passed citizen-sponsored initiatives that remove state-level criminal penalties for possession of medical marijuana. Successful initiatives in Arizona, Alaska, Oregon, Washington, Maine, Colorado and Nevada all followed the model established by California.

California officials initially refused to abide by Prop 215's provisions. Attorney General Dan Lundgren raided communities to arrest those who acted on the new state law, even when city councils pleaded with him not to do so. Californians responded by showing Lundgren the door when he ran for governor.

Arizona lawmakers responded similarly that same year when its citizens passed their own medical marijuana initiative. They concluded that their constituents had been duped. Arizona Senator Jon Kyl said he was "embarrassed" by the vote. The state legislature then gutted the initiative and approved a referendum for the 1998 ballot that sought to prohibit doctors from prescribing marijuana until the U.S. Congress authorized its medical use. When that ballot decisively failed, the state legislature, apparently resigned to the will of the voters, allowed the 1996 initiative to stand.

Federal preemption

State governments are now generally supportive of the medical marijuana initiatives overwhelmingly supported by their constituents. But the federal government has unabashedly used all of its powers to stop their implementation.

Soon after Arizona and California's initiatives were passed in 1996, the Clinton administration declared "that a practitioner's action of recommending or prescribing Schedule I controlled substances is not consistent with the public interest." As Eric Sterling of the Drug Policy Foundation points out, if the majority will of the people, as expressed by the ini-

Citizen Struggles: The Long Chronology of Efforts to Make Marijuana Medically Available

1972—NORML petitions the federal government to move marijuana to Schedule II.

1978—Illinois passes the first state-level therapeutic marijuana research program. Eventually 25 states would pass such laws, although only seven would ever distribute the drug.

1978—The federal Compassionate Investigate New Drug (CIND) program is created to supply state research programs with marijuana.

1979—Illinois passes a symbolic law allowing doctors to prescribe marijuana. Ten other states and Washington D.C. would follow suit.

1986—DEA Administrative Judge Francis Young finally rules on NORML's petition, recommending that marijuana should be moved to Schedule II. The DEA ignores the decision.

1992—The federal government disbands the CIND program. Only 8 patients continue to receive marijuana from the program.

1994—A federal Court of Appeals rules that the DEA has the right to reject its administrative judge's ruling and set its own criteria.

1996—California passes its landmark Proposition 215. Arizona also passes an initiative, but it is ineffectual. Seven other states have passed initiatives based on Prop 215.

1997—U.S. Representative Barney Frank introduces the "Medical Use of Marijuana Act," which would allow states to determine for themselves whether marijuana should be legal for medicinal use. Frank has introduced the bill every year, but it has yet to make it out of committee.

2000—Hawaii becomes the first state to pass a medical marijuana bill through the legislature.

2001—Canada adopts rules making it the only country in the world with a government-regulated system for using marijuana as medicine.

2001—The U.S. Supreme Court effectively outlaws marijuana distribution cooperatives, but leaves the door open for states to distribute the drug to patients.

tiative votes, is not the "public interest," then it's very unclear what is.

In 1997 a "Federal Policy" was issued that threatened to arrest physicians and revoke their prescription drug licenses if they recommended marijuana to their patients. Among those pushing for this hard line was John Walters, who worked under President George Bush Sr. and who, four years later, would become Dubya's new drug czar. The policy was eventually thrown out in federal court on First Amendment grounds.

Undeterred, the government turned its attention to the so-called "cannabis clubs" that sprouted in California after the passage of Prop 215. Marijuana distribution cooperatives were created to fill a void in California's

law. Although the initiative allows doctors to recommend marijuana and ill patients to use it, it doesn't legalize the growing and sale of marijuana. In other words, it enables consumption but impedes production.

In 1998 the Department of Justice brought a civil suit under federal law against six northern California cooperatives. Federal judge Charles Breyer agreed that federal drug laws overrode Proposition 215, and ordered the clubs to stop distributing pot to their members.

Of the six clubs, only one—the Oakland Cannabis Buyers Cooperative (OCBC)—appealed. In September 1999, the federal Ninth Circuit appeals court in San Francisco ruled 3-0 that "medical necessity"—the doctrine that a law can be broken when it is the only way to prevent a more serious harm— →

is a valid defense against federal marijuana charges if a distributor can prove that the patients it serves are seriously ill, face “imminent harm” without marijuana and have “no reasonable legal alternative.” The Court then ordered Judge Breyer to rehear the case. Getting no new evidence from the Justice Department, in July 2000 Breyer crafted a new injunction that allowed the OCBC to resume dispensing marijuana to patients who could meet the stiff test of medical necessity—less than 20 of the cooperative’s 4,500 members.

Despite the incredibly limited scope of Breyer’s revised injunction, the federal government immediately asked the U.S. Supreme Court to stay it, arguing that the appellate court ruling was “directly at odds with Congress’ express finding that marijuana has no currently accepted medical use.” The U.S. Supreme Court agreed. It issued an “emergency” order that temporarily barred the Oakland Cannabis Buyers’ Cooperative from distributing medical marijuana, and heard the case in March 2001.

In May 2001 the Supreme Court issued its decision. By an 8-0 vote it concluded that medical necessity was not a valid defense. The Court did not specifically overturn state initiatives. Indeed, it appears that the state itself might be able to distribute the marijuana to patients. But ominously, five justices indicated that they would be open to overturning these state initiatives.

Legitimate medicine

The scientific evidence supporting a medical use for marijuana has been building for decades. Until it was demonized in the late 1930s, marijuana was listed in the U.S. pharmacopoeia as an effective remedy for a variety of ailments, including asthma, migraine headaches and the pain of childbirth.

During the 1980s, researchers in six different state-sponsored clinical studies involving nearly 1,000 patients determined that smoking marijuana is effective in reducing nausea and improving the appetites of cancer patients. A majority of cancer doctors surveyed indicated they would prescribe marijuana for their patients. In 1999, the conservative National Academy of Sciences, in a report commissioned by Barry McCaffrey, said “marijuana’s active components are potentially effective in treating pain, chemotherapy-induced nausea, anorexia from AIDS wasting syndrome, and the involuntary spasticity associated with MS.” Scientific studies in Great Britain and Canada have also validated marijuana’s utility as a medicine.

The public’s endorsement of medical marijuana is nothing short of overwhelming. An April 1999 CNN poll found that 96 percent of respondents supported

the medical use of marijuana. A Gallup poll a month earlier found 73 percent of respondents would vote for making marijuana legally available for doctors to prescribe. At least 25 polls conducted since 1994 show public support for medical marijuana.

In Canada, the will of the people has governed public agencies. There the government convened a task force, which reviewed the evidence and recommended legalization of medical marijuana. In 2001 Canada adopted rules making it the only country in the world with a government-regulated system for using marijuana as medicine. Under the plan, which takes effect July 31, patients must have a recommendation from a physician, who must submit an application to the government. Patients are allowed to grow medical pot for personal use or to designate a grower. “Canada is acting compassionately by allowing people who are suffering from grave and debilitating illnesses to have access to marijuana for medical purposes,” said Health Minister Allan Rock in announcing the plan.

Several other countries are following Canada’s lead.

But in the United States, where politicians of all ideological stripes tout the merits of local control and decry unresponsive government, the struggle continues. One might ask what “devolution” can possibly mean when a government can overrule the right of a community to allow its citizens access to a medicine that will ease their pain.

It’s easy to declare, as Bob Dole did in his 1996 presidential campaign, “power to the people” when you believe the people will do exactly what you want. It is far more challenging to give people authority when they exercise it in ways with which you disagree. “For more than two decades now the federalism movement has been calling for returning power to the states and, even more, to the people,” said Roger Pilon of the libertarian Cato Institute in testimony before Congress. “The medical marijuana referenda movement is a small part of that larger effort, but it brings to the fore the hypocrisy of those who invoke federalism selectively for their own political purposes.”

President Bush has the opportunity to make “devolution” a guiding political principle, not just a campaign buzzword. Fond of rhetorical flourishes such as “Texans can run Texas,” and “local governments make the best decisions for their local communities,” his nomination of John Walters demonstrates his unwillingness to follow his philosophy when it comes to medical marijuana. Only time will tell if he has the courage to embrace the principles of devolution when they don’t serve his own political or ideological ends. [!]

Mapping the Internet

Geo-locators can determine an internet user's geographic location. Online retailers and governments are interested in perfecting this technology, but it might also prove useful to local economies. *By Sarah Hannigan*

Because it is everywhere and nowhere, the internet falls under no one nation's jurisdiction. But new technology is gradually bringing geographical boundaries to the web.

Until recently the primary question concerning the regulation of the world wide web has been: Whose rules apply—those of the country from which the information originates or those of the country where the information is received? Internet activity sanctioned by one nation or state might be unlawful in another. For example, distribution rights for music vary from nation to nation depending on agreements between musicians and their publishers. A digital download of a song may be allowed in Canada but not in the United States. Without a way to discern the location of the end-user, what is an online music retailer to do? Apply U.S. copyright standards to all—and forfeit Canadian customers? Allow access to all—and risk U.S. charges of copyright infringement? And what if the song to be downloaded is banned in certain nations?¹ Should a censorship mandate issued by Singapore affect residents of Spain?

If one country's laws are upheld at the expense of freedoms granted to users of another country, the most stringent rules reflecting the culture of a few would erode the civil liberties of the many.² In 1995 this happened.

A German court ruled that about 200 sex-related newsgroups maintained by CompuServe, a U.S.-

based internet service provider, violated a German law designed to protect minors. CompuServe was ordered to bar German users from these newsgroups. But, because no technical way existed for the company to tailor internet content for its 200,000 German subscribers, the company was forced to apply the rule worldwide. All four million CompuServe subscribers were blocked from the newsgroups.³

In November 2000, a French court ordered U.S.-based Yahoo! Inc. to block French residents from auctions featuring Nazi memorabilia on the Yahoo.com web site. France prohibits the sale or exhibition of Nazi-related items under its anti-racism laws.

Yahoo! maintained that it had upheld France's rule by tailoring its French Yahoo! site (yahoo.fr) to comply with local law.

Yet any internet user in France is able to access the main site Yahoo.com—since the content was available to users in France, the French court ruled that it could assert jurisdiction.⁴

However, before issuing a final ruling, the French judge commissioned an independent panel to determine if it was technologically feasible to protect French residents from Nazi-related content on the Yahoo! site without impeding the rights of others to view the content. The panel found that internet user lookup technologies were available, and though imperfect, could identify internet users from France at least 70 percent of the time.⁵ According to the companies on the leading edge of internet location identification, the technology now offers accuracy for up to 98 percent of users. →



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With geo-locating technologies, users in certain jurisdictions can either be targeted or avoided with particular information and images. The geographic boundaries that define nations and their rules can now be used to govern the world wide web. The timeliness of the emergence of the technology is unquestionable—currently the European Commission is debating

Rome II, European Union law on internet jurisdiction; The Hague Convention is attempting to establish worldwide rules on cross-border disputes; and, in the coming months, a California court will hear an appeal of the French Yahoo! case.

Finding the user

The simplest way to pinpoint a user's location is to request that users provide information about themselves—zip code, telephone area code, country of origin, etc. Based on this information, a web site could determine whether or not the user is located in an area where services provided are legal and grant access accordingly. This method is not reliable as any savvy user could easily cross the border with the "right" answer.

New geo-locating technologies are not as easily deceived. The technologies depend not on the user, but on the user's internet protocol (IP) address. An IP address is a string of numbers assigned to each of the computers connected directly to the internet, that is the servers of the internet service providers (ISPs). Although IP addresses alone say nothing about the location of individual computers, they can be cross-checked against databases that list the name and location of ISP servers. IP lookups or geo-locators are doing just this. And it is no small task—over 1.5 billion IP addresses define the users of the internet today, and up to 4.25 billion possible addresses are available.⁶

Using the resulting map of the internet, content providers can extend and customize operating rules so as to enforce boundaries for content distribution. A primitive form of this technology has been used by Microsoft since the early 1990s to comply with U.S. regulations prohibiting the export of strong-encryption web browsers.⁷

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But the location of an ISP's server doesn't always correspond to the location of the internet users. A large company with offices in many states may have one server that provides internet access for all of its employees. Likewise, the web's largest ISP, AmericaOnline, routes most of its users through its servers in Virginia. Additionally, a local ISP could serve end-users in

neighboring jurisdictions—like Arlington, Virginia and Washington, D.C.

Internet user IP address lookup alone is accurate for about 70 percent of internet users. This may be precise enough for many who plan to use the technology. Geo-location is currently marketed as a tool to improve advertising effectiveness. By honing in on an end-user's location, an online retailer can pitch rain boots to visitors connecting via Seattle-based servers and sandals to those from connecting from Sarasota.

When it comes to upholding the law, the more precise the geo-locator, the better. Technology is under development to allow for greater identification of AmericaOnline's users⁸, and to analyze IP addresses down to the zip code, area code or international phone code⁹. Geo-location technologies are boasting up to 99 percent accuracy in determining a user's country-of-origin¹⁰, and 85 percent accuracy for the user's metropolitan area.¹¹

Such accuracy enables online retailers to cooperate with the censorship and copyright laws of the countries and states in which they do business. But the very qualities that make geo-locators a useful tool for companies also make the technology a potentially serious threat to privacy. Information about physical location is gathered without the end-user's consent and access to content is determined accordingly. Geo-locators claim that the information collected is not about individuals, but about the servers through which individuals connect to the internet. Additionally, the location data is no more refined than a zip code or area code—a letter addressed to your zip code alone will not find its way into your mailbox. But some users believe that even their zip code should be protected from the eyes of the world.

Another use for locators

Although geo-locator technology seems poised to become part of the classic tug of war between proponents of individual privacy and supporters of government regulations, there is a third perspective to consider. Local economies have a stake in the development of geo-locators as well. One example of a case in which this technology could strengthen a community can be found in the issue of internet tax. Currently most online retailers are exempt from collecting state and local sales tax, a situation unpopular with local stores, which are at a 6 to 8 percent price disadvantage. Opponents of an internet tax argue that collection would be nearly impossible, partly because the physical site of an internet transaction would be difficult to determine. But with geo-locator technology, a customer from Montana could be identified as such by an online retailer and charged the appropriate state tax rate for her purchases. States would no longer have to lose sales tax revenue to e-commerce. (For discussions on the local repercussions of a tax-free internet, see "Is Tax Freedom Fair?" *The New Rules*, Winter 2000 and "Think Locally, Tax Globally," *The New Rules*, Summer 2000.)

Even before geo-location became technically feasible, anonymous service providers had begun to offer untraceable connections for those wishing to surf the web without bounds. Circumventing the technology is possible as well—a user in France could dial into a server in the United States and be free to access all that is available to American users. Geo-location technology won't bring an end to illicit internet activity, but that may not be its most important use anyway. More promising is its potential to help implement policies that support healthy local communities.

Four years ago it was thought that "the Internet [was] wholly insensitive to geographic distinctions," (*American Library Association v. Pataki* (969 F.Supp. 160, 170 (S.D.N.Y., 1997))) and therefore the laws, of geographically defined places. Today technology is mapping out boundaries across the internet, raising questions about the nature of the relationship between web and place. [!]

Notes

1. "Censors Pore Over Janet Jackson Album," Reuters, May 9, 2001. Racy lyrics on Janet Jackson's latest album earned her a spot on Singapore's blacklist. The country bans approximately 20 albums a year for illicit content. http://dailynews.yahoo.com/h/nm/20010509/od/jackson_dc_1.html
2. "Sex on the Internet: When Bavaria wrinkles its nose, must the whole world catch a cold?" *The Economist*, January 6, 1996.
3. Stephan Wilske and Teresa Schiller, "International Jurisdiction in Cyberspace: Which States May Regulate the Internet?" *Federal Communications Law Journal*, Vol. 50, No. 1, December 1997.
<http://www.law.indiana.edu/fclj/pubs/v50/no1/wilske.html>
"In the CompuServe case, German law was held applicable to bar access for German users to certain news groups. The consequence was that "German law is dictating what American citizens can read and view." This effect, however, was incidental. It was caused by the inability of CompuServe to tailor its services to the laws of each country in which it operates."
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5. Michael Geist, *Is There a There There? Toward Greater Certainty for Internet Jurisdiction*, April 2001 draft of a paper commissioned by the Uniform Law Conference of Canada. <http://aix1.uottawa.ca/~geist/geistjurisdiction-us.pdf>
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9. Net Geo <http://www.netgeo.com>
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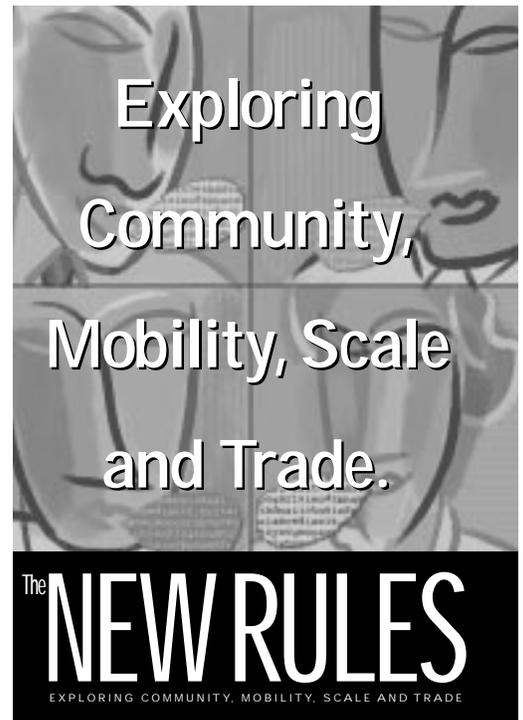
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