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Office of the Comptroller of the Currency  
250 E Street, S.W., Public Information Room, Mailstop 1-5  
Washington, DC 20219

Re: Docket No. 03-16, 12 CFR Parts 7 and 34.

Dear Sir or Madam:

We, the undersigned Attorneys General of 50 States and the Virgin Islands and the District of Columbia Office of Corporation Counsel, submit the following Comments on the rules proposed by the Office of the Comptroller of the Currency in Docket No. 03-16. As the chief law enforcement officials of our respective jurisdictions, we strongly oppose these preemption rules and urge the OCC to defer further action on them.

The OCC's current proposal, coupled with other recent OCC pronouncements on preemption, represents a radical restructuring of federal-state relationships in the area of banking. In recent years, the OCC has embarked on an aggressive campaign to declare that state laws and enforcement efforts are preempted if they have any impact on a national bank's activities. The OCC has zealously pushed its preemption agenda into areas where the States have exercised enforcement and regulatory authority without controversy for years.

The OCC's preemption analysis is one-sided and self-serving. The OCC has paid little deference to well-established history and precedent that has allowed the States and the OCC to coexist in a dual regulatory role for over 130 years. That precedent has upheld this nation's policy that national banks are subject to state laws unless the state laws significantly impair the national bank's powers created under federal law. The OCC is destroying that careful balance by finding "significant interference" or "undue burden" whenever state law has any effect on a national bank.

The States acknowledge that the National Bank Act preempts some state laws, such as regulation of credit card interest rates charged by out-of-state national banks.<sup>1</sup> Particularly in the area of consumer protection, however, there are state laws that affect virtually all commercial entities doing business with the public, including banking institutions. These laws do not impose significant burdens on national bank activities and are applied evenhandedly throughout the marketplace. As a general rule, state consumer protection laws prohibit businesses from engaging in unfair or deceptive practices. These laws are consistent with Section 5 of the Federal Trade Commission Act, and the States traditionally have enforced them in a wide range of financial activities involving consumers. A national bank's compliance with these laws should be expected and welcomed by the OCC, not regarded as a "significant impairment" of the bank's federal rights. It would be unprecedented and unfair to grant national banks (including, in the OCC's view, affiliated nonbank institutions) total immunity from all state consumer protection regulation and enforcement.

In the area of predatory mortgage lending, the OCC's actions are particularly disappointing. The States have taken a leadership role in devising legislation to restrict abusive practices in home equity lending. These state laws were carefully crafted to avoid preemption issues, to create safe harbors for mortgage lenders, and to add consumer protections to high cost subprime loans. In the States' experience, these laws have worked. Instead of commending the States' efforts, the OCC has gone to great lengths to attack them and to declare that they are inapplicable to national banks and their operating subsidiaries. In their place, the OCC has recommended minimal protections that fail to address many of the worst predatory lending abuses.

The States would prefer to cooperate and partner with the OCC, especially when enforcement resources are limited. The States and the OCC share similar goals of protecting the public and providing for a fair credit marketplace. But instead of seeking cooperation and joint enforcement, the OCC is insisting on an exclusive regulatory regime that would eliminate the role of the States, particularly with respect to such important consumer protection issues as predatory mortgage lending and telemarketing abuses. There is much work to be done by all regulatory and enforcement agencies on real and pressing problems. The States submit that this is not the time to devote energies to turf battles and empire building.

**A. National Banks Historically Have Been Subject to State Laws and a Dual System of Enforcement.**

The OCC's recent campaign to obtain exclusive enforcement authority over its constituent national banks, and to shield the banks from virtually all state laws, ignores a longstanding tradition of federal and state enforcement. Under this dual system, federal authorities have overseen the business activities of national banks to ensure the "safety and soundness" of banking institutions. The States, for their part, have enforced state laws of general application against all persons and businesses within their borders, including national banks. This complementary system of state and federal enforcement has worked well, both to maintain safe and sound banking practices, and to protect the consuming public from deleterious business practices. The dual system has roots not only in actual enforcement experience, but also in U.S. Supreme Court and other judicial precedents as

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<sup>1</sup> Marquette National Bank v. First of Omaha Service Corp., 439 U.S. 299 (1978).

well as Congressional pronouncements recognizing the vital role of the States in monitoring business activities within their borders.

**1. Under Supreme Court Precedent, National Banks Are Subject to State Laws that Do Not Conflict With, or Substantially Impair, Bank Rights under Federal Law.**

The National Bank Act ("NBA"), on which the OCC heavily relies to augment its powers, is a Civil War-era statute that was intended to finance the war and restore control of the monetary system to the federal government.<sup>2</sup> Contrary to the OCC's current assertions, the NBA was not intended to divest all state authority over national banks. Indeed, from its earliest decisions involving the NBA, the U.S. Supreme Court has recognized and upheld the applicability of state laws to national banks. In 1870, the Supreme Court rejected a preemption challenge to a state's collection of a bank shares tax, declaring that national banks "are subject to the laws of the State, and are governed in their daily course of business far more by the laws of the State than of the nation. It is only when the State law incapacitates the banks from discharging their duties to the government that it becomes unconstitutional."<sup>3</sup> In McClellan v. Chipman,<sup>4</sup> the Court rejected a bank's "assertion that national banks in virtue of the [NBA] are entirely removed, as to all their contracts, from any and every control by the state law," holding instead that state laws govern the business transactions of national banks except in areas where Congress expressly preempts state law or state law would impair the banks' efficiency in carrying out their duties imposed by federal law. Other Supreme Court decisions affirm the principle that national banks remain subject to many state laws.<sup>5</sup>

In general, the Supreme Court has upheld state laws that 1) did not expressly conflict with the statutory powers of national banks; 2) did not discriminate against national banks; or 3) did not impose undue burdens on the performance of bank functions mandated or permitted under national banking laws. Where the Court has found preemption, it usually has been in instances where the state law either prohibited or significantly impaired an express statutory power of a national bank.

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<sup>2</sup> Act June 3, 1864, ch. 106, 13 Stat. 99.

<sup>3</sup> National Bank v. Commonwealth, 76 U.S. (9 Wall.) 353, 361-62 (1870).

<sup>4</sup> 164 U.S. 347, 359 (1896).

<sup>5</sup> See, e.g., Davis v. Elmira Savings Bank, 161 U.S. 245, 290 (1896) ("Nothing, of course, in this opinion is intended to deny the operation of general and undiscriminating state laws on the contracts of national banks, so long as such laws do not conflict with the letter or the general objects and purpose of Congressional legislation."); First National Bank in St. Louis v. Missouri, 263 U.S. 640, 656 (1924) (National banks "are subject to the laws of a State in respect of their affairs unless such laws interfere with the purposes of their creation, tend to impair or destroy their efficiency as federal agencies or conflict with the paramount law of the United States."); Anderson National Bank v. Lockett, 321 U.S. 233, 244-52 (1944) ("National banks are subject to state laws, unless those laws infringe the national banking laws or impose an undue burden on the performance of the banks' functions," holding that a state statute administering abandoned deposit accounts did not "unlawful[ly] encroac[h] on the rights and privileges of national banks."); Franklin National Bank v. New York, 347 U.S. 373, 378 n.7 (1954) ("National banks may be subject to some state laws in the normal course of business if there is no conflict with federal law."). More recently, in the 1997 case, Atherton v. FDIC, 519 U.S. 213, 222-23, the Supreme Court reaffirmed the principle that "federally chartered banks are subject to state law," based on its earlier decisions.

The Supreme Court's 1996 decision in Barnett Bank of Marion County, N.A. v. Nelson<sup>6</sup> is consistent with these principles. In Barnett, the Court struck down a Florida law restricting the sale of insurance by national banks because a federal statute granted national banks the right to sell insurance in towns of 5,000 or fewer. The Court stated that preemption would be found if there was a direct conflict with express federal statutory authority because "normally Congress would not want States to forbid, or to impair significantly, the exercise of a power that Congress explicitly granted."<sup>7</sup> However, the Court went on to stress that the preemption test was not intended "to deprive States of the power to regulate national banks, where (unlike here) doing so does not prevent or significantly interfere with the national bank's exercise of its powers."<sup>8</sup>

Therefore, the test to determine whether a state law is preempted when applied to a national bank focuses on whether there is a "significant impairment" of a bank's express rights under federal law or a "significant interference" with the legitimate functions of a bank. This test reflects the traditional standard for conflict preemption in that only those state laws significantly interfering with a bank's exercise of its powers are preempted.

Lower court decisions also have recognized and affirmed the general applicability of state laws to national banks. For example, in Video Trax, Inc. v. NationsBank, N.A.,<sup>9</sup> the U.S. District Court for the Southern District Court of Florida observed: "Banking is not an area in which Congress has evidenced an intent to occupy the entire field to the exclusion of the states, and thus, state legislatures may legislate in all areas not expressly or impliedly preempted by federal legislation."

The OCC's current approach to conflict preemption flies in the face of these judicial precedents; it is so sweeping that, in reality, the OCC is establishing a regime of field preemption. The OCC presupposes that any state law that can arguably "impair the efficiency" of national bank lending operations compels a finding of preemption. Under this theory, most state consumer protection laws would be preempted, since such laws are unlikely to provide any protection without having some incidental impact on a bank's "efficiency." The OCC should not, by expansively interpreting the terms "impair significantly" and "significant interference," undertake to overturn over 130 years of precedent establishing that national banks are not entitled to immunity from all state laws and regulation.

## **2. Congressional Intent Supports the Applicability of State Law to National Banks and the Presumption against Preemption.**

In 1994, Congress enacted the Riegle-Neal Interstate Banking and Branching Efficiency Act to permit national banks to operate interstate branches to better serve consumers. In enacting the legislation, Congress made a clear pronouncement of its intent that state law would continue to apply to the interstate operations of national banks, particularly in the area of consumer

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<sup>6</sup> 517 U.S. 25 (1996).

<sup>7</sup> Id. at 33.

<sup>8</sup> Id.

<sup>9</sup> 33 F. Supp. 2d 1041, 1048 (S.D. Fla. 1998), aff'd per curiam, 205 F.3d 1358 (11th Cir.), cert. denied, 531 U.S. 822 (2000).

protection. The report of the House-Senate conference committee on the Riegle-Neal Act noted that “[u]nder well established judicial principles, national banks are subject to state law in many significant respects.”<sup>10</sup> The report emphasized:

States have a strong interest in the activities and operations of depository institutions doing business within their jurisdictions, regardless of the type of charter an institution holds. In particular, States have a legitimate interest in protecting the rights of their consumers, businesses and communities. Congress does not intend that the Interstate Banking and Branching Efficiency Act of 1994 alter this balance and thereby weaken States’ authority to protect the interests of their consumers, businesses, or communities.<sup>11</sup>

On the question of whether state laws may be preempted by federal banking law, the Conference Report noted that courts generally have applied “a rule of construction that avoids finding a conflict between Federal and State law where possible.”

The OCC appears tone deaf to the Congressional message sent by Riegle-Neal. The OCC discounts Riegle-Neal’s legislative history by noting that the Act excluded from its coverage those state laws that were preempted by federal law. While this statement is correct, the OCC ignores the fact that in 1994, when Riegle-Neal was enacted, it was generally accepted that most state consumer protection laws (outside of usury regulation) were not subject to preemption. Now that the OCC is taking the position that essentially all state consumer protection laws are preempted as to national banks, it contends that the Riegle-Neal mandate on the continued applicability of such state laws has no import. Surely, Congress did not anticipate that its stated intent could be displaced by the OCC pushing the boundaries of preemption off the map.

#### **B. The OCC Has Established an Aggressive Pattern of Advocating Preemption of State Laws.**

The OCC has, of late, undermined Congressional intent and the historic federal-state balance by promoting preemption and exclusive OCC control at every opportunity. In recent court appearances, policy statements, opinion letters and proposed rules, the OCC has articulated an intent to exempt its bank clientele from any duty to comply with state law or state consumer protection enforcement. The OCC’s efforts have included reducing the traditional “significant interference” test to one of “impairing the efficiency” of a national bank; construing the “visitorial powers” of the OCC<sup>12</sup> to exclude any state enforcement of state laws; and using the “incidental powers” granted national banks under the NBA<sup>13</sup> as a catch-all preemption provision.

The OCC has been candid about its desire, for the benefit of its constituent national banks, to sweep aside the nuisance of state laws: “The ability of a national bank to conduct a multistate business subject to a single uniform set of federal laws, under the supervision of a

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<sup>10</sup> H.R. Rep. No. 103-651, reprinted in 1994 U.S. Code Cong. & Ad. News 2068, 2074 (emphasis added).

<sup>11</sup> *Id.*

<sup>12</sup> 12 U.S.C. § 484.

<sup>13</sup> 12 U.S.C. § 24 (Seventh)

single regulator, free from the visitorial powers of various state authorities, is a major advantage of the national charter....”<sup>14</sup> The Comptroller has stated that the power to override state law “is one of the advantages of a national charter and I’m not the least bit ashamed to promote it.”<sup>15</sup>

The OCC has been an assertive advocate in persuading most federal courts to ratify its aggressively expansive preemption policy.<sup>16</sup> In all of the recent decisions cited by the OCC as background for the proposed rule, federal courts found in favor of the OCC’s position on preemption. This is hardly surprising, given the OCC’s aggressive advocacy role in the federal courts.

Under the Chevron doctrine,<sup>17</sup> federal courts give substantial deference to federal regulatory agencies when interpreting laws enforced by those agencies. Pursuant to the Supreme Court’s directive in Chevron, federal courts must exercise restraint in substituting their own construction of a statute for a “reasonable” interpretation by the appropriate agency administrator. The OCC has taken full advantage in exploiting this judicial deference, as have its regulated entities. In banking regulatory cases raising preemption issues, the OCC has repeatedly filed amicus briefs that uniformly promote the interests of the major national banks and oppose state consumer protection interests. Although some courts have questioned the OCC’s motives,<sup>18</sup> most courts have felt bound to follow the OCC’s preemption interpretations under the Chevron doctrine.

For example, in Bank One, Utah v. Gutttau,<sup>19</sup> the OCC sided with a national bank and against the State of Iowa in opposing a state statute requiring that ATM owners maintain an Iowa office and that ATMs display the name, address and phone number of the owner. This latter requirement, intended to give consumers access to information that could help them resolve ATM operational problems, was characterized by the dissent as “a straightforward consumer protection measure.”<sup>20</sup> Although the District Court found that the OCC’s interpretation of the NBA was “unreasonable,”<sup>21</sup> the Eighth Circuit adopted the OCC’s preemption position. In Metrobank v. Foster,<sup>22</sup> the OCC supported another national bank in opposing Iowa’s prohibition against charging ATM fees that exceed the “interchange fees” paid to financial institutions by non-account holders.

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<sup>14</sup> OCC News Release 2002-10.

<sup>15</sup> “Dependent on Lender’s Fees, the OCC takes Banks’ Side Against Local Laws,” Wall Street Journal, 1/28/02.

<sup>16</sup> One exception is the case of Bowler v. Hawke, 320 F.3d 59, 62-63 (1<sup>st</sup> Cir. 2003). The First Circuit found that an opinion issued by the OCC, which purported to declare certain Massachusetts insurance laws as preempted by the Gramm-Leach-Bliley Act, was “no more than informal agency guidance to banks and other interested parties,” and did not “create a ‘regulatory conflict’ giving rise to a case or controversy . . .”

<sup>17</sup> Chevron, U.S.A., Inc., v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984)

<sup>18</sup> Wells Fargo Bank of Texas, N.A. v. James, 321 F.3d 488, 494 (5<sup>th</sup> Cir. 2003)

<sup>19</sup> 190 F.3d 844 (8<sup>th</sup> Cir. 1999), cert. denied sub nom. Foster v. Bank One, Utah, 529 U.S. 1087 (2000).

<sup>20</sup> Id. at 851

<sup>21</sup> Bank One, Utah v. Gutttau, 1998 U.S. Dist. Lexis 14830 (S.D. Iowa, 1998).

<sup>22</sup> 193 F. Supp. 2d 1156 (S.D. Iowa 2002).

This year, in the case of Wells Fargo v. James,<sup>23</sup> the OCC again argued in support of a group of national banks opposed to a Texas consumer protection law. At issue in that case was a “par value” statute that prohibited any Texas bank from charging fees to cash checks drawn on that bank (known as “on us” checks). Texas contended that such check cashing charges fell disproportionately on the working poor, who often did not have their own bank at which to cash paychecks. Although the Fifth Circuit found in favor of the OCC’s preemption position, it expressed concerns about the OCC’s role:

Here, the constituency positively affected by the OCC’s position is concentrated, organized and well-funded, and also happens to be the regulated industry. In contrast, the constituency which is adversely affected by the decision, though vast, is diffuse, unorganized, and definitionally ill-funded. It may be that these competing interests could better be balanced, as Appellant suggests, by a national Congress whose commitments are diverse and universal, or even by the people as they are represented in the state legislatures, than by a solitary institution whose focus is a single industry.<sup>24</sup>

The breadth of the OCC’s preemption position is revealed in recent interpretative letters issued by the Comptroller. In May 2001, the OCC issued opinions overriding Ohio and Michigan motor vehicle regulatory laws. In the Ohio opinion, the OCC authorized national banks to conduct sales of returned lease vehicles without complying with Ohio sales licensing laws.<sup>25</sup> Ohio law was preempted, according to the OCC, because the bank was authorized to sell the vehicles “in the manner most economically beneficial.” In the Michigan opinion, the OCC found that a car dealer is not subject to the State’s motor vehicle sales financing laws if a national bank is financing the sale.<sup>26</sup>

### **C. The OCC’s Preemption Actions Interfere with State Consumer Protection Enforcement.**

In addition to claiming that most state laws are inapplicable to national banks, the OCC essentially contends that the States do not have any consumer protection enforcement jurisdiction over national banks. The OCC does have explicit “visitorial powers” over national banks pursuant to the NBA.<sup>27</sup> The States therefore may not conduct bank examinations or engage in the direct supervision of a national bank. The OCC, however, is seeking to stretch the meaning of visitorial jurisdiction to block all investigations and enforcement actions directed at national banks.

The OCC has recently advised national banks to notify it if any bank is contacted by a state official, even if the state official is simply seeking information.<sup>28</sup> And although the visitorial powers provision in the NBA contains an express exemption for litigation (“except as . . . vested in the courts of justice”), the OCC, in a recent proposed rule on visitorial powers,<sup>29</sup> dismisses the States’ right to

<sup>23</sup> 321 F.3d 488 (5<sup>th</sup> Cir. 2003).

<sup>24</sup> Id. at 494.

<sup>25</sup> 66 Fed. Reg. 23977 (5/10/01).

<sup>26</sup> 66 Fed. Reg. 28593 (5/23/01).

<sup>27</sup> 12 U.S.C. § 484.

<sup>28</sup> OCC Advisory Letter 2002-9, 11/25/02.

<sup>29</sup> 68 Fed. Reg. 6366 (2/17/03).

seek legal remedies against national banks. The OCC would limit state enforcement actions to the filing of declaratory judgment actions aimed at determining whether or not the state law in question is preempted. If, then, the court finds against preemption, the OCC maintains that enforcement of a bank's compliance with the state law "is within the OCC's exclusive purview."<sup>30</sup>

In the past, state Attorneys General have brought consumer law enforcement actions against national banks with little controversy, just as attorneys representing private individuals have filed suit to obtain legal redress against national banks.<sup>31</sup> The States have routinely investigated consumer complaints against national banks and have reached formal and informal settlements with national banks. Until recently, most national banks cooperated in the resolution of these actions, and the OCC voiced no disapproval of state enforcement efforts.

In some of these actions, the States were targeting fraudulent or deceptive practices by a local retail seller. To obtain adequate relief for victimized consumers, the States have included as defendants the banking institutions that provided the financing for the questionable transactions. As the West Virginia Supreme Court noted in allowing the state Attorney General to maintain an action against a national bank that financed the allegedly unlawful sale of motor vehicle extended warranties:

Logic and experience dictate that if the types of lawsuits which the Attorney General could bring under the CCPA did not include lawsuits against financial institutions such as defendants, these institutions could, if unsavory, run in effect a "laundry" for "fly-by-night" retailers that seek to excessively charge their consumers. Consequently, the real meaning of consumer protection would be stripped of its efficacy.<sup>32</sup>

The OCC has increasingly hardened its position against state enforcement rights in the past three years. In 2001, the Minnesota Attorney General brought a federal court case against Fleet Mortgage Corporation under the FTC's Telemarketing Sales Rule<sup>33</sup> and the Minnesota Consumer Fraud Act. Minnesota alleged that Fleet Mortgage had engaged in a deceptive marketing scheme by providing customers' private account information to third party telemarketers selling memberships in buying clubs. Fleet also added the charges for the buying club sales to customers' mortgage loan accounts.<sup>34</sup>

Fleet Mortgage argued that only the OCC could enforce state consumer protection laws against it. The District Court rejected Fleet's motion to dismiss, holding that "[f]ederal law does not require that the OCC have exclusive enforcement over such actions. The OCC has no direct responsibility for enforcing non-banking state laws such as the [Minnesota consumer protection

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<sup>30</sup> Id. at 6370.

<sup>31</sup> See, e.g., State of Alaska v. First National Bank of Anchorage, 660 P.2d 406 (Alaska 1982); State of Arizona v. Sgrillo, 176 Ariz. 148, 859 P.2d 771 (1993); State of Wisconsin v. Ameritech Corp., 185 Wis. 2d 686, 517 N.W.2d 705 (1994); State of West Virginia v. Scott Runyan Pontiac-Buick, Inc., 194 W.Va. 770, 461 S.E.2d 516 (1995).

<sup>32</sup> State v. Scott Runyan Pontiac-Buick, Inc., *supra*, 461 S.E.2d at 526.

<sup>33</sup> 16 C.F.R. § 310 (promulgated pursuant to the federal Telemarketing and Consumer Fraud and Abuse Prevention Act, 15 U.S.C. § 6101).

<sup>34</sup> State of Minnesota v. Fleet Mortgage Corp., 158 F. Supp. 2d 962 (D. Minn. 2001).

laws].”<sup>35</sup> Fleet, with the support of the OCC, brought a second motion to dismiss. The OCC, in its amicus brief, contended that neither Minnesota nor the FTC had any authority to enforce the Telemarketing Sales Rule against Fleet Mortgage because national banks are exempt from the Rule and the exempt status extended to non-bank subsidiaries like Fleet Mortgage. The District Court rejected the OCC’s position: “The OCC’s contention that it must have exclusive jurisdiction over subsidiaries in order to avoid having its authority ‘restricted’ is unpersuasive.”<sup>36</sup>

There are other recent examples of States’ consumer protection enforcement efforts against national banks, all of which the OCC would eliminate under its current preemption and visitorial powers stance. In some of these cases, the OCC has actively attempted to interfere with the state actions by advising banks that the States had no jurisdiction over them.

Beginning in 2001, a group of states, including California, Illinois, New York, and Florida, conducted an investigation into telemarketing operations by several major national banks. The banks had contracted with third-party telemarketers to share, for a fee, personal information about the banks’ credit card customers and to provide access to bank customer billing information. The bank’s name was then used in the telemarketer’s sales pitch. The products sold were unrelated to the bank or to any banking services. The investigating states reached settlement agreements with Citibank and First USA despite the OCC’s efforts to dissuade the banks from concluding such agreements. The OCC’s view was that state Attorneys General had no enforcement authority over national banks.

In other recent examples, the Kentucky and Indiana Attorneys General have settled alleged violations of state “Do Not Call” telemarketing law violations with a national bank. The State of Arizona brought a case against an air conditioning company and Household Bank for alleged deceptive sales and financing practices targeting Spanish-speaking customers. In 2002, the States of Illinois, Maryland, and Missouri investigated an unlicensed trade school for deceptive advertising. The States questioned a national bank’s role in financing tuition payments but were advised by the bank that they were preempted. The OCC confirmed the bank’s view, and informed the States that the OCC alone would determine if there had been any violation of state consumer protection laws by the bank.

The proposed rule, when coupled with the OCC’s pending proposed rule on visitorial powers and other OCC pronouncements, demonstrates that the OCC intends to divest the States of their traditional consumer protection enforcement jurisdiction over national banks.

**D. The OCC’s Proposed Rule and Other Recent Actions Undermine State Efforts to Attack Predatory Lending Abuses.**

The OCC’s recent preemption activity, including its order preempting Georgia’s Fair Lending Law, is an unfortunate and unnecessary response to efforts by the States to control the problem of predatory mortgage lending. The States have taken a leadership role in addressing predatory lending, both in regulation and enforcement, and these state actions have been effective. The OCC should

<sup>35</sup> *Id.* at 966 (D. Minn. 2001).

<sup>36</sup> *State of Minnesota v. Fleet Mortgage Corp.*, 181 F. Supp. 2d 995, 1001 (D. Minn. 2001).

recognize and support these efforts and seek to cooperate in achieving a shared goal of a fair lending marketplace.

Instead, as demonstrated by its order on the Georgia law, the OCC has found conflicts with the National Bank Act in virtually every statutory anti-predatory lending consumer protection adopted by the States. The OCC has also gone beyond assessing the impact of these laws on national banks, and has attacked the usefulness of these laws even as they apply to non-depository institutions.<sup>37</sup> If national banks are not subject to state laws, and if national banks are not the problem, as the OCC repeatedly asserts, then the OCC should have no reason to undermine the States' predatory lending initiatives.

The OCC's efforts to deal with the very substantial problem of predatory lending, while a step in the right direction, fall short of the actions taken by many states. In the proposed rule, the OCC takes a token and minimalist approach. The OCC's proposal addresses only asset-based lending, which is just one of the many abusive practices present in predatory lending. If the OCC intends to supplant all state laws governing predatory lending as to national banks, it should substitute a regulatory regime that more comprehensively addresses the unfair practices that are well-documented in this area. The OCC did begin to adopt a more broad based approach in Advisory Letter 2003-2, in which it recommended that banks adopt guidelines to prevent predatory lending practices. However, the OCC's general guidelines were merely advisory, intended to "encourage" national banks to adopt appropriate policies and do not carry the force of formal rules. The OCC should continue to build on the standards identified in AL 2003-2 and promulgate meaningful and specific predatory lending controls.

In every recent pronouncement the OCC has made on predatory lending, it has pointed out that a group of state Attorneys General are on record saying that most predatory lending problems have come from non-depository subprime mortgage lenders, not national banks. These statements by a group of Attorneys General were made in comments supporting a rulemaking proceeding by the Office of Thrift Supervision under the Alternative Mortgage Transaction Parity Act (AMTPA) and in an amicus brief filed in related litigation.<sup>38</sup> The Attorneys General supported the rational basis for OTS' distinction, in its revised AMTPA preemption rules, between "state housing creditors" and federally supervised banking institutions. The Attorneys General encouraged the OTS to revisit a prior preemption determination, and to require state housing creditors to comply with state laws regulating prepayment penalties and late fees.

It is true that most complaints and state enforcement actions involving mortgage lending practices have not been directed at banks. However, most major subprime mortgage lenders are now subsidiaries of bank holding companies (although not direct bank operating subsidiaries). Recent major settlements by state Attorneys General and the FTC related to alleged unfair lending practices by Household Finance and the Associates, both of which have now been acquired by bank holding companies. A national bank was a defendant in the only court case alleging class-wide

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<sup>37</sup> See OCC News Release 2003-57 (7/24/03); OCC Working Paper, "Economic Issues in Predatory Lending," 7/30/03, available at: <http://www.occ.treas.gov/workingpaper.pdf>.

<sup>38</sup> National Home Equity Mortgage Association v. OTS, No. 02-2506 (GK) (D.D.C. 2003).

violations of North Carolina's Predatory Lending Act.<sup>39</sup> Several national banks have partnered with payday lenders for the sole purpose of claiming preemption authority to make very high rate, short-term consumer loans in violation of state laws. (The OCC took effective action to curtail this latter practice, known as "charter renting.") Based on these actions and other state consumer protection enforcement actions detailed above, it is clear that a national charter does not prevent a bank from engaging in unfair or deceptive practices.

State predatory lending laws have clearly identified unfair and deceptive lending practices and have imposed specific, appropriate requirements to protect consumers. The States that have enacted legislation have been sensitive to federalism concerns and have been careful not to impose direct restrictions on the rates and fees that nationally chartered lenders (or any lender) may charge. The objective in all states has been to narrowly target abusive practices and to cover only the more problematic reaches of the subprime marketplace, where borrowers are unsophisticated and where most of the problems have occurred.

Responsible lenders do not engage in the practices targeted by state predatory lending laws. These laws impose minimal burdens on legitimate lending institutions and do not impair any reasonable lending activity on the part of banks. The laws, by controlling the most abusive actors, serve to clean up the mortgage lending marketplace and restore consumer confidence, which benefits consumers and lenders alike.

In fact, many state predatory lending controls have now been voluntarily adopted by national subprime lenders. The prohibition on financing single premium credit insurance, which was considered controversial when it was included in North Carolina's 1999 law, has been accepted and implemented nationally by all of the major finance company mortgage lenders. The prohibition against flipping and the related "net tangible benefit" test, which was questioned by some lenders when it was introduced in North Carolina, also has been voluntarily adopted as a useful standard. Leading subprime lenders also have imposed restrictions on exorbitant points and origination fees, which were among the primary abuses identified in state predatory lending laws. Far from restricting the flow of credit, the predatory lending controls initially adopted by several states have become useful as bright line industry standards on a nationwide basis.

Despite the success and acceptance of state predatory lending laws, the OCC has declared every significant component of such laws to be impermissible burdens on national banks. In its order preempting the Georgia law, the OCC finds even the most non-controversial and widely accepted provisions to interfere with banks' ability to lend and therefore to be in conflict with the National Bank Act. As an example, no reasonable person would contend that encouraging a borrower to default on an existing loan is an acceptable lending practice. But just such a practice has been used by unscrupulous lenders or brokers to lead borrowers into a desperate delinquency situation, so that the borrowers then fall prey to whatever terms the lender dictates. Widely recognized as an unfair trade practice, encouraging default is prohibited by state predatory lending laws. Yet the OCC found this prohibition in the Georgia law to be preempted because it imposed

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<sup>39</sup> Baxter v. Guaranty National Bank of Tallahassee, 01 CV 9168 (Wake County, NC Superior Court). The bank contended that the North Carolina law was preempted as to a national bank but the case was settled before this issue was judicially resolved.

impermissible restrictions on, and interfered with, “the exercise of the Federal power of national banks to make real estate loans.”<sup>40</sup> The OCC also declared restrictions on other practices, such as negative amortization and financing of prepaid credit insurance premiums, and the requirement for high cost loan borrowers to receive credit counseling, to be similarly preempted.

If national banks do not routinely engage in practices such as encouraging default or using negative loan amortization, it is difficult to see how these consumer protections impede any bank’s ability to lend. Yet under the proposed rule, any state law provision is preempted if it, among other things, 1) restricts a lender’s ability to require insurance; 2) regulates anything relating to the terms of credit, including loan amortization or loan acceleration; 3) requires any disclosures; or 4) regulates advertising.

The OCC recognizes that national banks are subject to Section 5 of the Federal Trade Commission Act, which prohibits unfair or deceptive trade practices.<sup>41</sup> Most states have similarly worded consumer protection statutes, many modeled on the FTC Act. If national banks are prohibited from engaging in unfair and deceptive practices under federal law, then it should be no impediment for them to comply with state laws proscribing the same unlawful practices. State predatory lending acts apply the States’ unfair and deceptive practices regulatory authority to the field of mortgage lending. These statutes give further definition and more precise guidelines for lenders on fair conduct in making mortgage loans to consumers.

In the experience of the States, lenders welcome bright line tests more than general proscriptions against unfair conduct. However, in adopting its own very limited restrictions on predatory lending, the OCC falls back on compliance with the FTC Act as a standard for lenders to follow. The OCC would be better advised to fall back on the numerous state laws and regulations in this area and to develop more useful rules for the benefit of the banking industry and consumers alike. The OCC also should insist that national banks comply with state predatory lending laws unless there is compelling evidence that such compliance substantially interferes with a bank’s ability to make real estate loans.

#### **E. The OCC Has Exceeded its Authority in Extending Preemption Rights to the Operating Subsidiaries of National Banks.**

The OCC’s proposal to apply its overly broad preemption rules to operating subsidiaries of national banks clearly exceeds its authority under the National Bank Act. The proposal would do great damage to the state-federal dual banking system, and should be withdrawn.

Operating subsidiaries are not national banks subject to a national charter; they are state-created entities incorporated under state law and have been licensed and regulated by the States for years without controversy. Nothing in the NBA grants the OCC power to bar states from licensing, examining and otherwise regulating state-created non-bank entities that happen to be subsidiaries of national banks. Nevertheless, the OCC now proposes that operating subsidiaries of national banks should have the same legal and regulatory status as the national banks themselves, contending

<sup>40</sup> 68 Fed. Reg. 46278 (8/5/03).

<sup>41</sup> 15 U.S.C. § 45(a)(1).

that these subsidiaries are effectively departments, divisions or equivalent parts of the banks.

The OCC proposes to federalize state-chartered subsidiaries by placing them within the exclusive supervisory control of the OCC. Under the OCC's proposal, the States would be deprived of all authority to regulate these state-chartered corporations, which include mortgage companies that have long been licensed by States. The OCC proposal intrudes upon the States' sovereign powers and exceeds the boundaries of federal authority under the Tenth Amendment. It attempts to convert state-chartered corporations into creatures of federal law without permission of the chartering states.<sup>42</sup>

According to the OCC, a state law is exempted from preemption only if it is expressly incorporated into the federal banking laws or has no more than an "incidental" effect on banking activities. The OCC, however, considers mere inconvenience to a subsidiary of a national bank to be a conflict between federal and state law. As indicated by amicus curiae briefs filed by the OCC across the country, this overreaching standard would lead to the preemption of nearly all state licensing and regulatory laws. The preemption of state licensing laws, including the ability to license and examine mortgage lending entities, is not sound public policy. It would encourage financial institutions to give up their state charters, and to instead, seek either to obtain a federal charter or to merge with a national bank, effectively destroying the dual banking system that is valued by both Congress and the States.

Operating subsidiaries historically have been regulated by States under their respective laws and relevant regulatory regimes and are in no manner considered "national banks" by the NBA. Moreover, the NBA provides absolutely no basis for ignoring the corporate distinctions between a parent national bank and its subsidiary. In an area where, as here, state law traditionally has applied, Congressional intent to preempt state law must be clearly manifested.<sup>43</sup> There is no such intent expressed anywhere in the NBA, and the OCC's proposal is, in fact, contrary to Congressional intent, expressed most recently in the legislative history of the Riegle-Neal Interstate Banking Act.<sup>44</sup>

Additionally, the NBA provides stringent requirements for banks to qualify as national banks. None of these requirements apply to their state-chartered and state-regulated operating subsidiaries. Instead, as creatures of state law, operating subsidiaries should comply with applicable state law requirements.

Moreover, the States have long held an unquestioned primacy in regulating state-chartered corporations, particularly including companies that engage in consumer financial services. Courts have repeatedly upheld States' authority to exercise comprehensive supervision over the corporations they charter and to license and regulate corporations chartered by other states that transact business within their borders. As affirmed by the Supreme Court, "No principle of corporation law and practice is more firmly established than a State's authority to regulate domestic corporations."<sup>45</sup> The

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<sup>42</sup> Hopkins Federal Savings & Loan Ass'n v. Cleary, 296 U.S. 315 (1935).

<sup>43</sup> English v. General Electric Co., 496 U.S. 72, 74 (1990); California v. ARC American Corp., 490 U.S. 93, 101 (1989); Jones v. Rath Packing Co., 430 U.S. 519, 525 (1977).

<sup>44</sup> See discussion in Section II.B. at pp. 4-5 above.

<sup>45</sup> CTS Corp. v. Dynamics Corp. of America, 481 U.S. 69, 89 (1987).

fact that a state-chartered corporation is an affiliate of a national bank does not alter the principles of federalism that grant States the right to regulate corporations chartered under their laws. Indeed, in a case where the OCC similarly engaged in an overly aggressive interpretation by the OCC of the NBA, a federal circuit court of appeals concluded that “to defer to the OCC in this case would flout Congressional intent – something we remain unwilling to do.”<sup>46</sup>

The OCC’s claim of exclusive supervisory powers over operating subsidiaries is contrary to both this nation’s dual system of banking and the historic primacy of the States in matters of corporate governance. The OCC’s broad assertion of field preemption has no basis in any of the federal legislation that provide that agency with its regulatory authority. Like the OCC’s claims of complete preemption with respect to national banks, the OCC’s proposal to extend its hegemony to banks’ operating subsidiaries wholly exceeds any reasonable interpretation of the regulatory powers given to the OCC by national banking laws. The OCC’s proposal to create such a sweeping standard of preemption and to bar the States from regulating subsidiaries of national banks created under state laws directly violates Congressional intent, federal law and the Tenth Amendment to the Constitution.

In conclusion, the OCC’s proposed rules represent a significant expansion of preemption standards and a restructuring of the federal-state balance that has existed for many years, particularly in the area of consumer protection. For the reasons expressed above, we urge the OCC to withdraw the proposed rules.

We thank you for the opportunity to submit these Comments. If you have questions or comments, please do not hesitate to contact Sarah Reznick, NAAG’s Consumer Protection Project Director, at (202) 326-6016 or Blair Tinkle, NAAG’s Legislative Director, at (202) 326-6258.

Respectfully,



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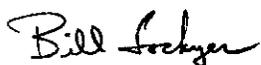
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<sup>46</sup> American Land Title Association v. Clarke, 968 F.2d 150, 157 (2d Cir. 1992).



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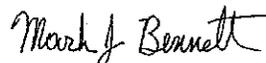
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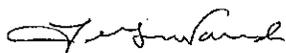
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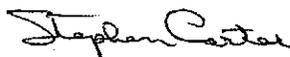
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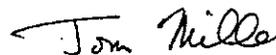
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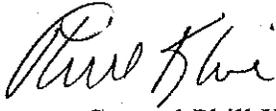
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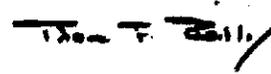
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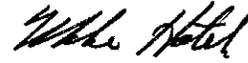
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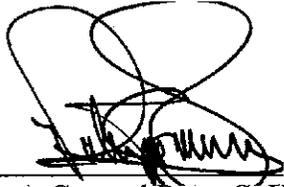
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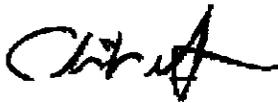
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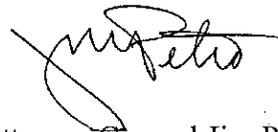
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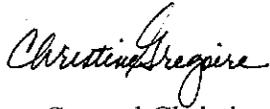
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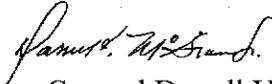
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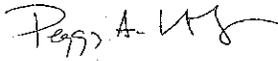
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