**Testimony of**

**Joe Belew**

**President, Consumer Bankers Association**

**on**

**OCC Final Rules on National Bank Preemption and Visitorial Powers**

**before the**

**Senate Banking, Housing and Urban Affairs Committee**

**of the**

**United States of America**

**On**

**April 7, 2004**

Mr. Chairman and members of the Committee, my name is Joe Belew. I am President of the Consumer Bankers Association, which represents banks nationwide. CBA's members include most of the nation's largest bank holding companies as well as regional and super community banks that collectively hold two-thirds of the industry's total assets. The vast majority of our members are national banks.

In my role as President of the Association, I interact daily with the heads of the retail banking operations—the men and women who are responsible for many of the lending and deposit taking activities that are subject to the OCC's actions. I am very pleased to have the opportunity to share with you CBA's views on this subject—a subject that is very important to our member institutions. For the record, I am also attaching CBA's comment letter to the OCC in response to the preemption proposal that resulted in the regulation that is the subject of this hearing.

We strongly support the OCC's regulations that define the applicability of state laws to the activity of national banks and their operating subsidiaries. Increasingly, in recent years, national banks have been facing the intrusion of state and local statutes and regulations on their federally created powers. The courts and the OCC have uniformly and consistently resolved each such instance when contested by reaffirming the supremacy of the national bank powers and the Constitutionally based preemptive effect of the National Bank Act. But there has remained a need for greater uniformity and

predictability for national banks operating in multiple jurisdictions nationwide, and these regulations will provide that helpful guidance.

The final preemption rule, which the OCC issued only after it published a Notice of Proposed Rulemaking and reviewed approximately 2,600 public comments, clarifies the extent to which national banks are subject to state laws. The rule identifies the types of state laws that are preempted by the National Bank Act and, importantly, also identifies the types of state laws that are not preempted. Reflecting the history of judicial rulings, the types of laws that are preempted include those laws regulating loan terms, imposing conditions on lending and deposit relationships, and requiring state licenses. These are types of laws that create impediments to the ability of national banks to exercise powers that are granted under federal law. For the record, they are very similar to the types of laws preempted for federally chartered thrifts and credit unions by the regulations of the Office of Thrift Supervision and National Credit Union Administration. The OTS and NCUA rules have been in place for many years and have provided federal thrifts and credit unions with a set of predictable, uniform laws of operation.

The OCC regulation is clear that there are many types of state laws that are not preempted by the National Bank Act. These are laws that do not regulate the manner or content of the business of banking authorized for national banks, but rather establish what the OCC calls the "legal infrastructure" of that business. These generally include laws on contracts, rights to collect debts, acquisition and transfer of property, taxation, zoning, crimes and torts. The agency has also made it clear that the National Bank Act does not

preempt any other law that only incidentally affects national banks' lending, deposit-taking, or other operations.

We believe it is important to recognize that the OCC is not breaking new ground by issuing this rule. The regulation is based on Supreme Court precedent dating back to 1869—135 years—consistently holding that national banks were designed to operate under uniform, federal standards of banking operations nationwide. By codifying over a century of court decisions and OCC interpretations, the agency is clarifying the law and responding to numerous questions about the extent to which various types of state laws apply to national banks and their operating subsidiaries. By a separate rulemaking, the OCC is also clarifying its exclusive visitorial authority over national banks and their operating subsidiaries. These two rules will give national banks the uniform and predictable standards that permit them to serve their customers in diverse markets nationwide.

These rules pose no threat to the dual banking system. States can and do adopt different rules for the institutions they regulate and supervise. On the other hand, many states, including Georgia—which was the subject of the OCC's recent preemption determination—have "parity" or "wild card" laws that give state chartered institutions the same coverage as national banks and federally chartered thrifts. Therefore, as the Comptroller has pointed out, it is up to the states to determine whether they believe a separate state code is appropriate or to employ the same rules as national banks or federal thrifts for state-chartered institutions.

Because so much attention has been directed at the important area of predatory lending and the recent enactment of state laws to address the problem, a charge has inevitably been leveled at the OCC that its actions will leave consumers vulnerable, by sweeping away these state protections and leaving nothing in their place. On the contrary, the OCC is second to none in its regulation and enforcement of consumer protection laws. National banks are subject to the whole array of federal consumer protection laws, from the Truth in Lending Act and the protections accorded by the Home Ownership and Equity Protection Act to the anti-discrimination provisions of the Equal Credit Opportunity Act and the Fair Housing Act. In addition, the OCC has tough guidelines in place that are unique to national banks, spelling out in detail what rules the banks and their operating subsidiaries must follow in order to ensure that all national bank lending, deposit taking, and other activity remain above reproach. We have attached a list of the many consumer protection standards to which national banks must stringently adhere.

As part of the preemption regulation, the agency has also added two additional provisions applicable to national banks, designed to provide an additional layer of protection for consumers. One provision provides that a national bank may not make consumer loans based predominantly on the foreclosure or liquidation value of the borrower's collateral. This places a total ban on any lending by a national bank that does not take into consideration the borrower's ability to repay, a ban on loans made with the expectation of profiting from foreclosure. The second provision added to the new rules states that a

violation of section 5 of the FTC Act, which protects consumers against unfair or deceptive acts or practices, is a violation of the National Bank Act. This ensures that the OCC can employ its enforcement authority against banks that engage in any unfair or deceptive practices as defined by that act, and maintain its vigilant oversight to prevent predatory lending practices of any kind.

Indeed, it is predatory lending that has been the focus of much of the debate surrounding the OCC's recent actions. Yet the overwhelming evidence suggests that national banks and their subsidiaries are not a principal source of concern when it comes to any abusive or predatory practices. For example, an *amicus* brief filed last year by 22 state Attorneys General in the U.S. District Court for the District of Columbia stated, "Based on consumer complaints received, as well as investigations and enforcement actions undertaken by the Attorneys General, predatory lending abuses are largely confined to the subprime mortgage lending market and to non-depository institutions. Almost all the leading subprime lenders are mortgage companies and finance companies, not banks or direct bank subsidiaries."[1] The object of the OCC's comprehensive rules and guidelines—along with the additional standards being adopted as part of this regulation--is to ensure that national banks remain the gold standard of responsible lending.

Our experience at CBA supports the assertion that national banks also take proactive steps to protect consumers from abusive practices of others. One universally recognized

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[1] National Home Equity Mortgage Association v. Office of Thrift Supervision, Brief of Amicus Curiae State Attorneys General in Opposition to Plaintiff's Motion to Summary Judgment and in Support of Defendant's Motion for Summary Judgment, Civ. Act. No. 1:02CV02506 (GK), US Dist. Ct, D.C., March 21, 2003 (Emphasis added)

way to shield consumers is to give them the education in financial services that permits them to recognize and avoid bad practices. As Federal Reserve Board Chairman Alan Greenspan said before this Committee, "In the quest to stem the occurrence of abusive, and at times illegal, lending practices, regulators, consumer advocates, and policymakers all agree that consumer education is essential to combating predatory lending. An informed borrower is simply less vulnerable to fraud and abuse."[2] National banks have demonstrated an ongoing commitment to educating customers as a means of protecting them from predatory practices.

For three years, we have surveyed our member banks to determine how involved they are in financial literacy efforts, as a measure of their sense of responsibility to the communities they serve. The most recent published survey showed that 98% of the respondents--with the majority being national banks--sponsor financial literacy programs or partner on financial education initiatives.

CBA's 2003 *Survey of Bank-Sponsored Financial Literacy Programs* shows a significant increase from the previous year, from 60% to 72%, in bank programs aimed at helping consumers avoid abusive or predatory lending practices. Over 70% of the respondents stated that their banks offered programs targeting issues such as flipping, avoiding unscrupulous lenders, excessive interest rates or payday loans.

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[2] Testimony of Alan Greenspan, Chairman, Board of Governors of the Federal Reserve System, before the Committee on Banking, Housing, and Urban Affairs, U.S. Senate, February 5, 2002.

Additionally, 96% of these banks offer mortgage and home ownership counseling, typically in connection with an affordable mortgage program, which in turn is offered by 93% of responding banks. With 73%, credit counseling is mandatory to qualify for such programs. In addition, 37% of the 2003 respondents indicated that the institution had a foreclosure prevention program in place. The 2004 survey is not yet final, but the preliminary findings suggest that banks may be significantly increasing their involvement in programs that educate school children, both K-12 and college. This may reflect a growing awareness that the complexity of the financial products like mortgages call for a broad based understanding of finance that needs to be learned as part of the educational system.

This commitment to financial literacy is actively encouraged by the OCC as a means of combating predatory practices. Comptroller of the Currency John D. Hawke, Jr., in a speech to CBA members in which he advocated bank involvement in financial education efforts, put it this way: "Studies ... tell us that financial education is an indispensable element of any strategy to combat the rise of predatory lending. Although those who engage in predatory practices are relatively few in number -- and only rarely include regulated depository institutions -- they've done real harm to the reputation of all financial institutions. It's therefore very much in the industry's interests to assist in efforts to oust the bad actors."[3] Obviously, educating consumers is not the *only* solution to the problem of predatory lending practices, but national banks have found that they can use their resources and expertise, often in partnerships with communities and governments, to

[3] Remarks by John D. Hawke, Jr. Comptroller of the Currency, before the Consumer Bankers Association, Arlington, Virginia, April 8, 2002.

make a more financially educated population, who will be less vulnerable to abusive sales practices.

Although, as I have noted, national banks are not known to be involved in abusive lending practices, the OCC has the means to ensure that they remain above reproach. Because of the comprehensive examination oversight to which national banks are subject, the OCC can find and stop problems before they occur. If anything slips through the net, the agency can and will take enforcement action—everything from cease and desist orders to restitution—and it has a strong track record of taking action on the rare occasion it discovers national banks which may be engaged in abusive practices. In several recent cases, for example, the agency has imposed substantial monetary penalties on institutions. But the OCC's scrutiny in this area goes back for a number of years. At a CBA conference four years ago, for instance, OCC Senior Deputy Comptroller and Chief Counsel Julie Williams warned national banks: "We plan to use our supervisory powers -- through our safety and soundness, fair lending, and consumer compliance examinations; our licensing and chartering process; and individual enforcement actions -- to address any potential predatory lending concerns that might arise in national banks and their subsidiaries." [4] Thus, national banks have long been on notice that the OCC's examination and enforcement in this area is rigorous.

The agency employs nearly 1,700 examiners in its 48 field offices and 23 satellite offices, with over 100 working exclusively on compliance supervision. Over 300 examiners are

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[4] Remarks by Julie Williams, OCC Senior Deputy Comptroller and Chief Counsel, before the Consumer Bankers Association, Arlington, Virginia, June 5, 2000.

in the 24 largest national banking companies (many of whom are CBA members) as on-site examiners, engaged in the continuous supervision of those institutions. The OCC also maintains a Customer Assistance Group (CAG), which handles consumer complaints. The CAG, an efficient system the agency employs to address and resolve consumer complaints, is a supplement to the examination function, which efficiently and directly monitors the banks for compliance and safety and soundness matters. The level of oversight and staffing at the OCC is flexible enough to deal with increased compliance and enforcement needs. Since the OCC is funded directly from assessments and fees, it can adjust its overall budget annually to accommodate any increased needs that may follow from changes in the scope of its oversight. By contrast, state attorneys general are often operating under budget constraints, and must enforce a vast array of state laws against many different persons and businesses. Thus, the OCC's oversight of national banks and operating subsidiaries is not only a better means of enforcing compliance, but it frees up the resources of the states to tackle the other many issues they must face.

The OCC has also sought cooperation from the states where there may be allegations of wrongdoing by national banks or their operating subsidiaries. It has established special procedures for expedited referrals of consumer complaints from State Attorneys General and banking departments. In this way, the state law enforcement officers can pass on complaints to the OCC for follow up, and preserve their resources to enforce the state laws against predatory lenders and other bad actors. The agency recently issued a further clarification of the appropriate response by national banks to consumer complaints—regardless of their source. In a recent advisory letter, the OCC has told its banks that

ordinarily they should deal directly with states that have referred consumer complaints and resolve the problems promptly, rather than referring the states or the complainant to the OCC.[5]

National banks benefit from being subject to a uniform set of rules that do not vary from state to state. Banks today operate across many state lines, permitting them to serve the needs of an increasingly mobile society. Some of our members operate in over half the states. A single set of rules permits them to provide economies of scale and streamlined services in a cost-effective way. Subject to comprehensive oversight, they are able to provide the quality products and services that can, through competition in the marketplace, help to drive out the bad actors that we all are trying to eliminate. But their ability to do so is severely hampered by the laws, regulations, and ordinances adopted in each jurisdiction. Since states do not have the kind of on-going scrutiny of unsupervised lenders and brokers that the OCC has over national banks, the laws are often overbroad—driving out the good with the bad. Forcing national banks to comply with all these myriad, often conflicting, state laws, would make it difficult if not impossible for national banks to operate in the uniform and efficient manner envisioned in the National Bank Act.

In conclusion, we strongly support the OCC's regulations clarifying the applicability of state laws to the activity of national banks and their operating subsidiaries. Its actions are in accord with the letter and spirit of the National Bank Act, as it has been consistently interpreted by over a century of court opinions; permitting national banks and their

[5] AL 2004-2 (Feb. 26, 2004).

operating subsidiaries efficiently to serve the needs of their customers nationwide without being hobbled by a hodge-podge of well-intentioned but disruptive laws in every locality. The extensive consumer protection laws to which national banks and their operating subsidiaries are subject, together with strong leadership and rigorous oversight by the OCC and its examination force, will ensure that national banks continue to serve consumers well in the future.

Once again, thank you for this opportunity to share our views.

CBA | CONSUMER BANKERS ASSOCIATION

**Attachment A**

October 3, 2003

John D. Hawke, Jr.
Comptroller of the Currency
Office of the Comptroller of the Currency
250 E St., S.W.
Public Information Room, Mailstop 1-5
Washington, D.C. 20219

**Re: Docket No. 03-16: Notice of Proposed Rulemaking on preemption of state laws.**

Dear Mr. Hawke:

The Consumer Bankers Association[1] (CBA) is pleased to have the opportunity to submit these comments in connection with the proposed rulemaking concerning preemption of state laws, involving amendments to Parts 7 and 34 of the OCC Regulations.

CBA supports wholeheartedly the thrust and direction of the proposal. Over more than a century, and especially in recent decades, it has become abundantly clear that the constitutionally preemptive effect of the National Bank Act and other federal laws relating to the powers of national banks cannot be undercut by state law that interferes with the exercise of those powers. A virtually unbroken line of judicial decisions and OCC interpretations has solidified the notion that national banks must be able to exercise the full range of federally established banking functions, without interference or burden from state regulatory and visitorial regimes.

With legislative and regulatory activity in the states increasing in recent years, it has been necessary for the courts and the OCC to address a series of instances in which state law arguably crosses the federalism line and intrudes on the protected powers of national banks. The proliferation of these challenges, arising not only from regulatory activity in fifty states, but from countless municipal and other local government activities as well, underscores the need for uniform ground rules and oversight for national banks. While the courts and the OCC have regularly reaffirmed the supremacy and independence of national bank powers, the pattern has been one of *ad hoc* determinations, with uncertainty on all sides until the particular state-federal friction has been resolved. And since the preemptive effect of federal law is constitutionally

[1] The Consumer Bankers Association is the recognized voice on retail banking issues in the nation's capital. Member institutions are the leaders in consumer financial services, including auto finance, home equity lending, card products, education loans, small business services, community development, investments, deposits and delivery. CBA was founded in 1919 and provides leadership, education, research and federal representation on retail banking issues such as privacy, fair lending, and consumer protection legislation/regulation. CBA members include most of the nation's largest bank holding companies as well as regional and super community banks that collectively hold two-thirds of the industry's total assets.

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based, in a sense none of these determinations makes new law, but rather each is simply declaratory of the supremacy clause mandate.

Against this background, we understand that the OCC's intent in the proposed rulemaking is to provide clearer and more comprehensive guidance as to the range and scope of federal preemption regarding national bank powers. CBA strongly supports that objective. OCC guidance in this respect will provide helpful reassurance, uniformity, and predictability to bankers, regulators, and the public at large, on the impact of national bank powers and the boundaries for state-law applicability to those banks. In the process, this rulemaking would help equalize and balance the positions of federal thrift institutions under OTS and NCUA oversight, and national banks under OCC supervision.

The underlying issue is not whether state regulation is better or stronger than federal, or vice versa. It is, rather, whether national banks are able to operate and compete in national markets in accordance with federal law and federal supervision, without also being subjected to a flood of differing state and local laws and regulations that create redundancies, inefficiencies, compliance costs, and competitive disadvantages for those national banks. State chartered financial institutions must of course comply with state law, but those state institutions are not subject to the overlay of federal law and supervision that applies specifically to national banks. National banks, in turn, cannot effectively implement their federal charter powers under a blanket of additional, duplicative – and stifling – state and local regulation. In fact, for national banks conducting business across state lines, it is not a single blanket of state law, but potentially fifty – and many more when local jurisdictions are considered.

This is hardly to say that national banks are, or are asking to be, unregulated or free to engage in unscrupulous practices. The body of federal law that empowers national banks also orders and restrains bank operations for the protection of bank customers, investors, and the public at large. All of the federal consumer financial services laws, such as TILA, ECOA, and TISA, apply fully to national banks, as does the general proscription on unfair or deceptive practices under the FTC Act. The OCC has articulated substantial regulatory guidance on permissible and proscribed practices for national banks in all areas of their operations. No example is more current than the OCC guidelines relating to predatory lending, and incorporated in this rulemaking.

Most importantly, every national bank (and its subsidiaries) is subject to close scrutiny of its activities through the bank examination process, and the OCC has clearly indicated its ability and willingness to act against banks that exceed the bounds of appropriate conduct. There is no vacuum of federal law or oversight relating to the protection of national bank customers that needs state law to fill it.

We do not understand the current proposal to be an effort by the OCC to raise the bar of federal preemption, or to displace state law more broadly than precedents and tradition dictate. Rather it provides more bright-line guidance, in advance, as to the scope of the federal preemption. The result will be more certainty and consistency in the application of preemption

principles, and less need for ad hoc challenges that are wasteful, time consuming, and inefficient.

**"Field" vs. "conflict" preemption.**

CBA concurs with the OCC suggestion that mortgage lending powers under Part 34 of the regulations should be treated as a matter of "field" preemption. The real estate lending authority for national banks and their subsidiaries derives from a separate and discrete statutory source (NBA § 371), and the legal framework for such lending has been extensively developed through federal statutes and agency regulations, including extensive guidance from the Federal Reserve Board, HUD, and the OCC itself. There is no need or justification to retain any significant state regulatory or visitorial role with respect to that aspect of national bank operations.[2]

For the proposed revisions in Part 7, which cover a wide waterfront of national bank operations from credit cards to deposit accounts to investment services, it is extremely helpful that the proposal lists the types of state laws that would be subject to preemption in each of the categories addressed (deposit taking, lending, other activities). It is justifiable, we believe, to state the preemptive effect of federal law in terms of general categories of state law, without the need to examine the details of each state initiative and to assess the degree-of-conflict it presents. The real conflict, obstruction or burden of state law arises not so much from the impact of any single state law, but rather from the possibility – indeed the likelihood – that an endless variety of different and irreconcilable homegrown regulations would emerge in the states, confronting national banks with an impenetrable morass of idiosyncratic state laws. For national banks operating countrywide or regionally, the burden of complying with that aggregate of differing state laws is the real "conflict" and the real justification for preemption.

We suggest several adjustments to the lists of state laws preempted in connection with lending transactions [§ 7.4008(c)(2)]. The list might explicitly include state laws dealing with **non-interest fees and charges**, since these are inextricably related to the bank's pricing of its credit products.[3] The lists ought also to include the **collection of debts in default**; there is no reason to preserve for national banks the powers to market, price, book, and service loans, without also protecting their ability to follow the collection trail to its conclusion after default.

**The preemption boundaries for preempted and retained ("incidental") state laws**

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[2] We understand that, under the proposal, even when field preemption applies, there is a residuum of state law that will continue to apply to national bank operations as part of the "infrastructure" of state law applicable generally to business activity in the state. Proposed § 34.4(b).

[3] We appreciate that OCC may understand that non-interest fees are dealt with in 7.4002, and therefore do not need a separate preemption statement.

We recognize that a stream of *ad hoc* judicial or administrative determinations about preemption, arising out of concrete examples of conflict between federal and state law, can be a frustrating and time-consuming process, as each challenge is resolved on its specific circumstances. But at least there is, usually, a definitive answer to that particular preemption issue. A comprehensive, across the board, regulatory statement on preemption of state law is inherently attractive, and CBA supports the proposed rulemaking for exactly this reason. But there is a degree of risk in shifting to a broader, more generic regulatory approach – as the pending rulemaking does. Each section of the proposed regulatory amendments lists, by "type," the kinds of state laws that are preempted, and others that are generally not preempted. Each of these lists is stated as a set of very broad categories. There is the potential that these two lists will be read in parallel, and as mutually exclusive, where we do not believe this is the OCC's intent; state law that provides "infrastructure"and "merely incidental" regulation of business activity will still need to be evaluated against the traditional preemption criteria. We therefore suggest it may be preferable to delete the broad categorical lists of state laws that are not preempted, lest the lists themselves, and the relationships between them, become the focus of preemption challenges. Alternatively, to provide greater certainty and predictability, the OCC might consider elaborating on the scope of these categories, either in the regulation proper or in authoritative interpretational material related to it.

**Predatory lending policy**

CBA strongly supports the proposed statements concerning asset-based lending in sections 7.4008(b) and 34.3(b). We urge the OCC, when interpreting this language, to keep in mind that there are sophisticated and streamlined credit products in the market, such as "low-doc" and "no-doc" loans, where income may not be considered directly, in order to serve the convenience and needs of applicants with good credit. These products are not likely to raise the predatory lending concerns that are addressed in the proposal.

We would be pleased to discuss any of these matters further with you or the OCC staff, and we thank you for considering our views.

Sincerely

Steven I. Zeisel
Senior Counsel

Ralph J. Rohner
Special Counsel

**Attachment B**

Federal Consumer Protection Standards that Apply to
National Banks and National Bank Operating Subsidiaries

- Federal Trade Commission Act
- Truth in Lending Act
- Home Ownership and Equity Protection Act
- Fair Housing Act
- Equal Credit Opportunity Act
- Real Estate Settlement Procedures Act
- Community Reinvestment Act
- Truth in Savings Act
- Electronic Fund Transfer Act
- Expedited Funds Availability Act
- Flood Disaster Protection Act
- Fair Housing Home Loan Data System
- Credit Practices Rule
- Fair Credit Reporting Act
- Federal Privacy Laws
- Fair Debt Collection Practices Act
- Consumer Leasing Act
- Fair Credit Billing Act
- CCPA Garnishment Restrictions
- Check Clearing for the $21^{st}$ Century Act
- OCC anti-predatory lending rules in Parts 7 and 34
- OCC rules imposing consumer protections in connection with the sales of debt cancellation and suspension agreements
- OCC standards on unfair and deceptive practices
- OCC standards on preventing predatory and abusive practices in direct lending and brokered and purchased loan transactions