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Memo

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Date: August 12, 2003

To: Members of the House Financial Services Committee

From: Edward L. Yingling, Executive Vice President, ABA

Re: OCC Determination and Order Preempting the Georgia Fair Lending Act

On behalf of the membership of the American Bankers Association (ABA), I am writing to express strong support for the determination of the Comptroller of the Currency that the Georgia Fair Lending Act¹ ("GFLA") is preempted by the National Bank Act and existing regulations of his Office ("OCC"). ABA member banks support the OCC's action because it carries out the long-standing principles of the National Bank Act and because of the difficulty of complying with differing, though well-intended, state statutes.

The measured approach taken by OCC – preservation of national standards for real estate lending by national banks, coupled with vigorous enforcement of fair dealing and high ethical standards for national bank lending relationships with consumers – will ensure both that home loans remain available to low-income consumers and that national banks and their operating subsidiaries do not engage in predatory or unfair and deceptive practices.

OCC has clearly demonstrated its commitment to fair dealing through the development of comprehensive supervisory standards to prevent national banks from engaging in predatory lending practices, both directly and indirectly, as well as through its strong enforcement efforts. OCC took the lead among the bank regulators in strongly asserting its authority to enforce unfair and deceptive trade practices under the Federal Trade Commission Act.² Using that authority, as well as its traditional safety and soundness authority, the agency has taken strong enforcement efforts against abusive lending practices in connection with subprime credit card disclosures and payday lending. OCC has also determined that abusive lending practices will necessarily be taken into account when determining a national bank's Community Reinvestment Act rating.

OCC's determination is a carefully thought out response to the request by National City Bank, National City Bank of Indiana, and their operating subsidiaries for a preemption determination and order pursuant to 12 U.S.C. § 371 and OCC's implementing regulations at 12 C.F.R. Part 34. The order is wholly consistent with

¹ GA Code. Ann. §§ 7-6A-1 *et seq.*

² 15 U.S.C. §§ 41-58 as amended.

existing OCC precedents as well as longstanding U.S. Supreme Court analyses of conflicts between federal and state law. Indeed, in case-after-case, courts have held that the National Bank Act provides for just this type of approach for national banks; there can be no doubt that the OCC is correctly interpreting the law. Moreover, the result of the order – preemption of GFLA for a class of nationally chartered financial institutions – is exactly the same as the results of previous actions taken by other federal financial institution regulators, namely, the Office of Thrift Supervision (“OTS”) and the National Credit Union Administration. Indeed, those agencies have preempted, for their constituent institutions, predatory lending laws in Georgia and New York and, most recently, OTS added New Jersey to its list.

OCC’s Response is a Conservative One

OCC’s determination does not break new ground – it is based on existing OCC regulations as well as longstanding preemption precedents of the U.S. Supreme Court. Indeed, OCC was asked by the requester and commenters to base its decision on the fact that 12 U.S.C. § 371 demonstrates Congress’ intent that the agency “occupy the field” of national bank real estate lending, leaving no room for any state regulation of this activity. OCC chose, however, to take a more conservative approach.

Existing Regulations

OCC held that provisions of GFLA purporting to limit repayment schedules or the term to maturity of a loan are expressly preempted under its existing rules (12 C.F.R. § 34.4(a)). OCC further found that provisions of GFLA that purport to limit the interest a national bank can charge for loans are preempted under 12 C.F.R. § 7.4001 (most favored lender status). Similarly, GFLA provisions that purport to limit the non-interest fees a national bank can charge in connection with a loan are preempted under 12 C.F.R. § 7.4002(a) (express authority to charge fees for services).

Established Preemption Analysis

In its preemption determination, OCC applied the preemption analysis established by the U.S. Supreme Court over the last 140 years. In *McCulloch v. Maryland*, which involved the Second Bank of the United States, the Supreme Court enunciated the basic preemption principle: under the Supremacy Clause of the U.S. Constitution, states “have no power, by taxation or otherwise, to retard, impede, burden, or in any other manner control, the operations” of an entity created by lawful exercise of federal authority.³ This preemption doctrine was consistently reiterated in later Supreme Court decisions interpreting the 1863 National Bank Act. See, for example, *Farmers’ & Mechanics’ Nat’l Bank v. Dearing*, 91 U.S. 29 (1875) and *Easton v. Iowa*, 188 U.S. 220 (1903). This line of reasoning was most recently reiterated in the Supreme Court’s 1996 case, *Barnett Bank of Marion County N.A. v. Nelson*. In *Barnett*, the Supreme Court stated that the history of national bank powers is one of “interpreting grants of both enumerated and incidental ‘powers’ to national banks as

³ 17 U.S. (4 Wheat.) 316, 436 (1819).

grants of authority not normally limited by, but rather ordinarily preempting, contrary state law.”⁴ Indeed, in 1999 Congress favorably cited the analysis in *Barnett* and codified it in the Gramm-Leach-Bliley Act.

Thus, the Supreme Court has consistently recognized that state laws are preempted where they: 1) impair the efficiency of national banks to exercise federally authorized powers; 2) conflict with federal law; 3) frustrate the purpose of the National Bank Act; or 4) obstruct the scope and effective exercise of unconditional national bank powers.⁵

In analyzing the provisions of GFLA, OCC applied the basic principle of preemption analysis that, absent evidence of specific Congressional intent to the contrary, states may not condition the exercise of national bank federally granted powers upon compliance with state law.⁶ OCC determined that the standards imposed on a category of subprime loans, *i.e.*, “high-cost” loans, in GFLA are vague and not susceptible of certainty for national banks assessing their costs and risks. This inability to determine how to comply with a statute at the risk of civil liability is a restraint imposed on national banks engaged in real estate lending in Georgia. In addition, GFLA has impaired the ability of national banks to sell subprime loans into the secondary mortgage market. As a result, GFLA, and similar predatory lending statutes of other states, materially increase national banks’ costs and compliance risks in connection with subprime lending, to the extent that some national banks have left this market. Stated differently, the practical effect of GFLA and similar state predatory lending laws has been to obstruct or prevent national banks’ conduct of their federally authorized power to engage in real estate lending. Therefore, OCC concluded that several provisions of GFLA are preempted.

Contrary to concerns that have been raised, OCC’s action is fully in accord with Congress’ intent as enacted in the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994.⁷ We note that Section 114 of that Act imposes on OCC a process for ensuring public comment on preemption requests of certain types of state consumer protection laws, which OCC did.⁸ Section 114 does not, however, impose a standard for preemption determinations. Rather, it incorporates traditional judicial preemption analysis by stating that state consumer protection laws apply except “(i) when Federal law preempts the application of such State laws to a national bank ...”⁹

Concern has also been raised that OCC’s preemption determination has ignored the savings provision in the Home Owner’s Equity Protection Act of 1994 (“HOEPA”).

⁴ 517 U.S. 25, 32 (1996).

⁵ See *Barnett*, 517 U.S. at 31-32; *Franklin Nat’l Bank of Franklin Square v. New York*, 347 U.S. 373, 378 (1954); and *Ass’n of Banks in Ins., Inc. v. Duryee*, 270 F.3d. 397, 409 (6th Cir. 2001).

⁶ *Id.* See also, *United States v. Locke*, 529 U.S. 89, 108 (2000) (There is no presumption against preemption when “the State regulates in an area where there has been a history of significant federal presence”).

⁷ Pub. L. 103-328, 108 Stat. 2338 (1994).

⁸ 68 *Federal Register* 8959 (February 26, 2003).

⁹ Pub. L. 103-328, 108 Stat. 2338 (1994).

That provision, which is part of the Truth in Lending Act (“TILA”), applies only to state laws that are inconsistent with HOEPA. Indeed, the U.S. District Court for the Eastern District of California in *American Bankers Association v. Lockyer*, held that the TILA savings provision does not reach beyond TILA to control the preemption analysis under any other federal law.¹⁰

Finally, concern has been raised that exempting national banks from GFLA will have a negative impact on state regulatory schemes. As demonstrated above, the vigorous supervision and regulation of national bank real estate lending practices by the OCC will continue. Even OCC’s critics acknowledge that there is no evidence that national banks and their operating subsidiaries are engaging in so-called predatory lending practices; rather the types of abuses which have received so much media attention have been perpetrated by unregulated entities. Thus, the likely practical effect will be to free up increasingly scarce state resources to address predatory lending practices by the unregulated entities that are responsible for predatory lending abuses.

We appreciate the opportunity to share our views on this important subject.

¹⁰ 239 F. Supp. 2d 1000, 1009 (E.D. Cal. 2002).