

*enforce/enf\_search.htm*. Indeed, as recently observed by the Superior Court of Arizona, Maricopa County, in an action brought by Arizona against a national bank, among others, the restitution and remedial action ordered by the OCC in that matter against the bank was “comprehensive and significantly broader in scope than that available through [the] state court proceedings.” *State of Arizona v. Hispanic Air Conditioning and Heating, Inc.*, CV 2000–003625, Ruling at 27, Conclusions of Law, paragraph 50 (Aug. 25, 2003). Thus, the OCC has ample legal authority and resources to ensure that consumers are adequately protected.

#### List of Subjects in 12 CFR Part 7

Credit, Insurance, Investments, National banks, Reporting and recordkeeping requirements, Securities, Surety bonds.

#### Authority and Issuance

■ For the reasons set forth in the preamble, the OCC amends part 7 of chapter I of title 12 of the Code of Federal Regulations as follows:

#### PART 7—BANK ACTIVITIES AND OPERATIONS

■ 1. The authority citation for part 7 continues to read as follows:

**Authority:** 12 U.S.C. 1 *et seq.*, 71, 71a, 92, 92a, 93, 93a, 481, 484, 1818.

#### Subpart D—Preemption

■ 2. In § 7.4000:

- a. Add a new paragraph (a)(3); and
- b. Revise paragraph (b) to read as follows:

#### § 7.4000 Visitorial powers.

(a) \* \* \*

(3) Unless otherwise provided by Federal law, the OCC has exclusive visitorial authority with respect to the content and conduct of activities authorized for national banks under Federal law.

(b) *Exceptions to the general rule.* Under 12 U.S.C. 484, the OCC’s exclusive visitorial powers are subject to the following exceptions:

(1) *Exceptions authorized by Federal law.* National banks are subject to such visitorial powers as are provided by Federal law. Examples of laws vesting visitorial power in other governmental entities include laws authorizing state or other Federal officials to:

(i) Inspect the list of shareholders, provided that the official is authorized to assess taxes under state authority (12 U.S.C. 62; this section also authorizes inspection of the shareholder list by

shareholders and creditors of a national bank);

(ii) Review, at reasonable times and upon reasonable notice to a bank, the bank’s records solely to ensure compliance with applicable state unclaimed property or escheat laws upon reasonable cause to believe that the bank has failed to comply with those laws (12 U.S.C. 484(b));

(iii) Verify payroll records for unemployment compensation purposes (26 U.S.C. 3305(c));

(iv) Ascertain the correctness of Federal tax returns (26 U.S.C. 7602);

(v) Enforce the Fair Labor Standards Act (29 U.S.C. 211); and

(vi) Functionally regulate certain activities, as provided under the Gramm-Leach-Bliley Act, Pub. L. 106–102, 113 Stat. 1338 (Nov. 12, 1999).

(2) *Exception for courts of justice.*

National banks are subject to such visitorial powers as are vested in the courts of justice. This exception pertains to the powers inherent in the judiciary and does not grant state or other governmental authorities any right to inspect, superintend, direct, regulate or compel compliance by a national bank with respect to any law, regarding the content or conduct of activities authorized for national banks under Federal law.

(3) *Exception for Congress.* National banks are subject to such visitorial powers as shall be, or have been, exercised or directed by Congress or by either House thereof or by any committee of Congress or of either House duly authorized.

\* \* \* \* \*

John D. Hawke, Jr.,

Comptroller of the Currency.

[FR Doc. 04–585 Filed 1–12–04; 8:45 am]

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#### DEPARTMENT OF THE TREASURY

#### Office of the Comptroller of the Currency

#### 12 CFR Parts 7 and 34

[Docket No. 04–04]

RIN 1557–AC73

#### Bank Activities and Operations; Real Estate Lending and Appraisals

**AGENCY:** Office of the Comptroller of the Currency, Treasury.

**ACTION:** Final rule.

**SUMMARY:** The Office of the Comptroller of the Currency (OCC) is publishing a final rule amending parts 7 and 34 of our regulations to add provisions

clarifying the applicability of state law to national banks’ operations. The provisions concerning preemption identify types of state laws that are preempted, as well as the types of state laws that generally are not preempted, with respect to national banks’ lending, deposit-taking, and other operations. In tandem with these preemption provisions, we are also adopting supplemental anti-predatory lending standards governing national banks’ lending activities.

**EFFECTIVE DATE:** February 12, 2004.

**FOR FURTHER INFORMATION CONTACT:** For questions concerning the final rule, contact Michele Meyer, Counsel, or Mark Tenhundfeld, Assistant Director, Legislative and Regulatory Activities Division, (202) 874–5090.

#### SUPPLEMENTARY INFORMATION:

#### I. Introduction

The OCC is adopting this final rule to specify the types of state laws that do not apply to national banks’ lending and deposit taking activities *and* the types of state laws that generally *do* apply to national banks. Other state laws not specifically listed in this final rule also would be preempted under principles of preemption developed by the U.S. Supreme Court, if they obstruct, impair, or condition a national bank’s exercise of its lending, deposit-taking, or other powers granted to it under Federal law.

This final rule also contains a new provision prohibiting the making of any type of consumer loan based predominantly on the bank’s realization of the foreclosure value of the borrower’s collateral, without regard to the borrower’s ability to repay the loan according to its terms. (A consumer loan for this purpose is a loan made for personal, family, or household purposes). This anti-predatory lending standard applies uniformly to all consumer lending activities conducted by national banks, wherever located. A second anti-predatory lending standard in the final rule further specifically prohibits national banks from engaging in practices that are unfair and deceptive under the Federal Trade Commission Act (FTC Act)<sup>1</sup> and regulations issued thereunder, in connection with all types of lending.

The provisions concerning preemption of state laws are contained in 12 CFR part 34, which governs national banks’ real estate lending, and in three new sections to part 7 added by this final rule: § 7.4007 regarding deposit-taking activities; § 7.4008 regarding non-real estate lending

<sup>1</sup> 15 U.S.C. 45(a)(1).

activities; and § 7.4009 regarding the other Federally-authorized activities of national banks. The first anti-predatory lending standard appears both in part 34, where it applies with respect to real estate consumer lending, and in part 7, with respect to other consumer lending. The provision prohibiting a national bank from engaging in unfair or deceptive practices within the meaning of section 5 of the FTC Act and regulations promulgated thereunder<sup>2</sup> similarly appears in both parts 34 and 7.

## II. Description of Proposal

On August 5, 2003, the OCC published a notice of proposed rulemaking (NPRM or proposal) in the **Federal Register** (68 FR 46119) to amend parts 7 and 34 of our regulations to add provisions clarifying the applicability of state law to national banks. These provisions identified the types of state laws that are preempted, as well as the types of state laws that generally are not preempted, in the context of national bank lending, deposit-taking, and other Federally-authorized activities.

### A. Proposed Revisions to Part 34—Real Estate Lending

Part 34 of our regulations implements 12 U.S.C. 371, which authorizes national banks to engage in real estate lending subject to “such restrictions and requirements as the Comptroller of the Currency may prescribe by regulation or order.” Prior to the adoption of this final rule, subpart A of part 34 explicitly preempted state laws concerning five enumerated areas with respect to national banks and their operating subsidiaries.<sup>3</sup> Those are state laws concerning the loan to value ratio; the schedule for the repayment of principal and interest; the term to maturity of the loan; the aggregate amount of funds that may be loaned upon the security of real estate; and the covenants and restrictions that must be contained in a lease to qualify the leasehold as acceptable security for a real estate loan. Section 34.4(b) stated that the OCC would apply recognized principles of Federal preemption in considering whether state laws apply to other aspects of real estate lending by national banks.

Pursuant to our authority under 12 U.S.C. 93a and 371, we proposed to amend § 34.4(a) and (b) to provide a more extensive enumeration of the types of state law restrictions and requirements that do, and do not, apply

to the real estate lending activities of national banks. To the five types of state laws already listed in the regulations, proposed § 34.4(a) added a fuller, but non-exhaustive, list of the types of state laws that are preempted, many of which have already been found to be preempted by the Federal courts or OCC opinions. As also explained in the preamble to the NPRM, consistent with the applicable Federal judicial precedent, other types of state laws that wholly or partially obstruct the ability of national banks to fully exercise their real estate lending powers might be identified and, if so, preemption of those laws would be addressed by the OCC on a case-by-case basis.

We also noted in the preamble that the nature and scope of the statutory authority to set “requirements and restrictions” on national banks’ real estate lending may enable the OCC to “occupy the field” of the regulation of those activities. We invited comment on whether our regulations, like those of the Office of Thrift Supervision (OTS),<sup>4</sup> should state explicitly that Federal law occupies the field of real estate lending. We noted that such an occupation of the field necessarily would be applied in a manner consistent with other Federal laws, such as the Truth-in-Lending Act (TILA)<sup>5</sup> and the Equal Credit Opportunity Act (ECOA).<sup>6</sup>

Under proposed § 34.4(b), certain types of state laws are not preempted and would apply to national banks to the extent that they do not significantly affect the real estate lending operations of national banks or are otherwise consistent with national banks’ Federal authority to engage in real estate lending.<sup>7</sup> These types of laws generally pertain to contracts, collection of debts, acquisition and transfer of property, taxation, zoning, crimes, torts, and homestead rights. In addition, any other law that the OCC determines to interfere to only an insignificant extent with national banks’ lending authority or is otherwise consistent with national banks’ authority to engage in real estate lending would not be preempted.

The proposal retained the general rule stated in § 34.3 that national banks may “make, arrange, purchase, or sell loans or extensions of credit, or interests

therein, that are secured by liens on, or interests in, real estate, subject to terms, conditions, and limitations prescribed by the Comptroller of the Currency by regulation or order.” That provision was unchanged, other than by designating it as paragraph (a).

The proposal added a new paragraph (b), prescribing an explicit, safety and soundness-based anti-predatory lending standard to the general statement of authority concerning lending. Proposed § 34.3(b) prohibited a national bank from making a loan subject to 12 CFR part 34 based predominantly on the foreclosure value of the borrower’s collateral, rather than on the borrower’s repayment ability, including current and expected income, current obligations, employment status, and other relevant financial resources.

This standard augments the other standards that already apply to national bank real estate lending under Federal laws. These other standards include those contained in the OCC’s Advisory Letters on predatory lending;<sup>8</sup> section 5 of the FTC Act,<sup>9</sup> which makes unlawful “unfair or deceptive acts or practices” in interstate commerce; and many other Federal laws that impose standards on lending practices.<sup>10</sup> The NPRM invited commenters to suggest other anti-predatory lending standards that would be appropriate to apply to national bank real estate lending activities.

As a matter of Federal law, national bank operating subsidiaries conduct their activities subject to the same terms and conditions as apply to the parent banks, except where Federal law provides otherwise. See 12 CFR 5.34(e)(3) and 7.4006. See also 12 CFR 34.1(b) (real estate lending activities specifically). Thus, by virtue of regulations in existence prior to the proposal, the proposed changes to part 34, including the new anti-predatory lending standard, applied to both national banks and their operating subsidiaries.

<sup>8</sup> See OCC Advisory Letter 2003–2, “Guidelines for National Banks to Guard Against Predatory and Abusive Lending Practices” (Feb. 21, 2003) and OCC Advisory Letter 2003–3, “Avoiding Predatory and Abusive Lending Practices in Brokered and Purchased Loans” (Feb. 21, 2003). These documents are available on the OCC’s Web site at <http://www.occ.treas.gov/advlst03.htm>.

<sup>9</sup> 15 U.S.C. 45(a)(1).

<sup>10</sup> There is an existing network of Federal laws applicable to national banks that protect consumers in a variety of ways. In addition to TILA and ECOA, national banks are also subject to the standards contained in the Real Estate Settlement Procedures Act, 12 U.S.C. 2601 *et seq.*, the Fair Housing Act, 42 U.S.C. 3601 *et seq.*, the Home Mortgage Disclosure Act, 12 U.S.C. 2801 *et seq.*, the Fair Credit Reporting Act, 15 U.S.C. 1681 *et seq.*, the Truth in Savings Act, 12 U.S.C. 4301 *et seq.*, the Consumer Leasing Act, 15 U.S.C. 1667, and the Fair Debt Collection Practices Act, 15 U.S.C. 1692 *et seq.*

<sup>4</sup> 12 CFR 560.2.

<sup>5</sup> 15 U.S.C. 1601 *et seq.*

<sup>6</sup> 15 U.S.C. 1691 *et seq.*

<sup>7</sup> Federal law may explicitly resolve the question of whether state laws apply to the activities of national banks. There are instances where Federal law specifically incorporates state law standards, such as the fiduciary powers statute at 12 U.S.C. 92a(a). The language used in this final rule “[e]xcept where made applicable by Federal law” refers to this type of situation.

<sup>2</sup> 12 CFR part 227.

<sup>3</sup> Prior 12 CFR 34.1(b) and 34.4(a).

*B. Proposed Amendments to Part 7—Deposit-Taking, Other Lending, and Bank Operations*

The proposal also added three new sections to part 7: § 7.4007 regarding deposit-taking activities, § 7.4008 regarding non-real estate lending activities, and § 7.4009 regarding other national bank operations. The structure of the proposed amendments was the same for §§ 7.4007 and 7.4008 and was similar for § 7.4009. For §§ 7.4007 and 7.4008, the proposal first set out a statement of the authority to engage in the activity. Second, the proposal stated that state laws that obstruct, in whole or in part, a national bank's exercise of the Federally-authorized power in question are not applicable, and listed several types of state laws that are preempted. As with the list of preempted state laws set forth in the proposed amendments to part 34, this list reflects judicial precedents and OCC interpretations concerning the types of state laws that can obstruct the exercise of national banks' deposit-taking and non-real estate lending powers. Finally, the proposal listed several types of state laws that, as a general matter, are not preempted.

As with the proposed amendments to part 34, the proposed amendment to part 7 governing non-real estate lending included a safety and soundness-based anti-predatory lending standard. As proposed, § 7.4008(b) stated that a national bank shall not make a loan described in § 7.4008 based predominantly on the foreclosure value of the borrower's collateral, rather than on the borrower's repayment ability, including current and expected income, current obligations, employment status, and other relevant financial resources. The preamble to the NPRM pointed out that non-real estate lending also is subject to section 5 of the FTC Act.

For proposed § 7.4009, as with proposed §§ 7.4007 and 7.4008, the NPRM first stated that a national bank could exercise all powers authorized to it under Federal law. To address questions about the extent to which state law may permissibly govern powers or activities that have not been addressed by Federal court precedents or OCC opinions or orders, proposed new § 7.4009(b) provided that state laws do not apply to national banks if they obstruct, in whole or in part, a national bank's exercise of powers granted to it under Federal law. Next, proposed § 7.4009(c) noted that the provisions of this section apply to any national bank power or aspect of a national bank's operation that is not otherwise covered by another OCC regulation that

specifically addresses the applicability of state law. Finally, the proposal listed several types of state laws that, as a general matter, are not preempted.

As with the proposed changes to part 34, and for the same reasons, the proposal's changes to part 7 would be applicable to both national banks and their operating subsidiaries by virtue of an existing OCC regulation.

### III. Overview of Comments

The OCC received approximately 2,600 comments, most of which came from the following groups:

*Realtors.* The vast majority—approximately 85%—of the opposing comments came from realtors and others representing the real estate industry, who expressed identical concerns about the possibility that national banks' *financial subsidiaries* would be permitted to engage in real estate brokerage activities<sup>11</sup> and that, if that power were authorized, the proposal would permit them to do so without complying with state real estate brokerage licensing laws. This final rule will not have that result because it does not apply to the activities of national bank financial subsidiaries. Thus, should the Department of the Treasury (Treasury) and the Board of Governors of the Federal Reserve System (Board) proposal to permit financial subsidiaries and financial holding companies to engage in real estate brokerage activities go forward, this final rule would not affect the application of state real estate licensing requirements to national bank financial subsidiaries.

Many realtor comments also raised arguments concerning the impact of this rulemaking on consumers and market competition and some argued that preemption of state licensing requirements related to real estate *lending* is inappropriate on the basis of field or conflict preemption. These issues also were raised by other commenters and are addressed in sections IV and VI of this preamble.

*Community and consumer advocates.* In addition to the comments from realtors, the OCC received opposing comments from community and consumer advocates. These commenters argued that the OCC should not adopt further regulations preempting state law and, in particular, should not adopt in

<sup>11</sup> Pursuant to procedures established by the Gramm-Leach-Bliley Act, Pub. L. 106–102, 113 Stat. 1338 (Nov. 12, 1999), for determining that an activity is “financial in nature,” and thus permissible for financial holding companies and financial subsidiaries, the Board and Treasury jointly published a proposal to determine that real estate brokerage is “financial in nature.” See 66 FR 307 (Jan. 3, 2001). No final action has been taken on the proposal.

the final rule an “occupation of the field” preemption standard for national banks' real estate lending activities. The community and consumer advocates also asserted that the proposed “obstruct, in whole or in part” preemption standard is inconsistent with, and a lowering of, the preemption standards articulated by the U.S. Supreme Court. Whatever the standard, the community and consumer advocates expressed concern that preemption would allow national banks to escape some state tort, contract, debt collection, zoning, property transfer, and criminal laws, and would expose consumers to wide-spread predatory and abusive practices by national banks. These commenters asserted that the OCC's proposed anti-predatory lending standard is insufficient and urged the OCC to further strengthen consumer protections in parts 7 and 34, including prohibiting specific practices characterized as unfair or deceptive. These issues are addressed in sections IV and VI of this preamble.

*State officials and members of Congress.* State banking regulators, the Conference of State Bank Supervisors (CSBS), the National Conference of State Legislators, individual state legislators, the National Association of Attorneys General (NAAG), and individual state attorneys general questioned the legal basis of the proposal and argued that the OCC lacks authority to adopt it. These commenters, like the community and consumer advocates, also challenged the OCC's authority to adopt in the final rule either a “field occupation” preemption standard or the proposed “obstruct, in whole or in part” standard. These commenters raised concerns about the effect of the proposal, if adopted, on the dual banking system, and its impact on what they assert is the states' authority to apply and enforce consumer protection laws against national banks, and particularly against operating subsidiaries. Several members of Congress submitted comments, or forwarded letters from constituents and state officials, that echoed these concerns. The arguments concerning the dual banking system are addressed in the discussion of Executive Order 13132 later in this preamble.<sup>12</sup> The remaining issues raised by the state commenters are addressed in sections IV and VI of this preamble.<sup>13</sup>

<sup>12</sup> See also OCC publication entitled *National Banks and the Dual Banking System* (Sept. 2003).

<sup>13</sup> See also Letter from John D. Hawke, Jr., Comptroller of the Currency, to Senator Paul S. Sarbanes (Dec. 9, 2003), available on the OCC's Web site at <http://www.occ.treas.gov/foia/SarbanesPreemptionletter.pdf>; and identical letters sent to nine other Senators; and Letters from John

*National banks and banking industry trade groups.* National banks, other financial institutions, and industry groups supported the proposal. Many of these commenters argued that Congress has occupied the fields of deposit-taking and lending in the context of national banks and urged the OCC to adopt a final rule reflecting an extensive occupation of the field approach. These commenters concluded that various provisions of the National Bank Act establish broad statutory authority for the activities and regulation of national banks, and that these provisions suggest strongly that Congress did in fact intend to occupy the fields in question. In addition to these express grants of authority, the commenters noted that national banks may, under 12 U.S.C. 24(Seventh), “exercise \* \* \* all such incidental powers as shall be necessary to carry on the business of banking,” and that this provision has been broadly construed by the Supreme Court.<sup>14</sup> These commenters concluded that this broad grant of Federal powers, coupled with equally broad grants of rulemaking authority to the OCC,<sup>15</sup> effectively occupy the field of national bank regulation.

Many of the supporting commenters also urged the adoption of the proposal for the reasons set forth in its preamble. These commenters agreed with the OCC’s assertion in the preamble that banks with customers in more than one state “face uncertain compliance risks and substantial additional compliance burdens and expense that, for practical purposes, materially impact their ability to offer particular products and services.”<sup>16</sup> The commenters stated that, in effect, a national bank must often craft different products or services (with associated procedures and policies, and their attendant additional costs) for each state in which it does business, or elect not to provide all of its products or services (to the detriment of consumers) in one or more states. These commenters believe that the proposal, if adopted, would offer much-needed clarification of when state law does or does not apply to the activities of a national bank and its operating subsidiaries. Such clarity, these commenters argued, is critical to helping national banks maintain and expand provision of financial services. Without such clarity, these commenters

assert, the burdens and costs, and uncertain liabilities arising under a myriad of state and local laws, are a significant diversion of the resources that national banks otherwise can use to provide services to customers nationwide, and a significant deterrent to their willingness and ability to offer certain products and services in certain markets. These issues are addressed in sections IV and VI of this preamble.

#### IV. Reason and Authority for the Regulations

##### *A. The Regulations Are Issued in Furtherance of the OCC’s Responsibility To Ensure That the National Banking System Is Able To Operate As Authorized by Congress*

As the courts have recognized, Federal law authorizes the OCC to issue rules that preempt state law in furtherance of our responsibility to ensure that national banks are able to operate to the full extent authorized under Federal law, notwithstanding inconsistent state restrictions, and in furtherance of their safe and sound operations.

Federal law is the exclusive source of all of national banks’ powers and authorities. Key to these powers is the clause set forth at 12 U.S.C. 24(Seventh) that permits national banks to exercise “all such incidental powers as shall be necessary to carry on the business of banking.” This flexible grant of authority furthers Congress’s long-range goals in establishing the national banking system, including financing commerce, establishing private depositories, and generally supporting economic growth and development nationwide.<sup>17</sup> The achievement of these goals required national banks that are safe and sound and whose powers are dynamic and capable of evolving so that they can perform their intended roles. The broad grant of authority provided by 12 U.S.C. 24(Seventh), as well as the more targeted grants of authority provided by other statutes,<sup>18</sup> enable national banks to evolve their operations in order to meet the changing needs of our economy and individual consumers.<sup>19</sup>

<sup>17</sup> For a more detailed discussion of Congress’s purposes in establishing a national banking system that would operate to achieve these goals distinctly and separately from the existing system of state banks, see the preamble to the proposal, 68 FR 46119, 46120, and *National Banks and the Dual Banking System*, *supra* note 12.

<sup>18</sup> See, e.g., 12 U.S.C. 92a (authorizing national banks to engage in fiduciary activities) and 371 (authorizing national banks to engage in real estate lending activities).

<sup>19</sup> The Supreme Court expressly affirmed the dynamic, evolutionary character of national bank powers in *VALIC*, in which it held that the

The OCC is charged with the fundamental responsibility of ensuring that national banks operate on a safe and sound basis, and that they are able to do so, if they choose, to the full extent of their powers under Federal law. This responsibility includes enabling the national banking system to operate as authorized by Congress, consistent with the essential character of a national banking system and without undue confinement of their powers. Federal law gives the OCC broad rulemaking authority in order to fulfill these responsibilities. Under 12 U.S.C. 93a, the OCC is authorized “to prescribe rules and regulations to carry out the responsibilities of the office”<sup>20</sup> and, under 12 U.S.C. 371, to “prescribe by regulation or order” the “restrictions and requirements” on national banks’ real estate lending power without state-imposed conditions.<sup>21</sup>

In recent years, the financial services marketplace has undergone profound changes. Markets for credit (both consumer and commercial), deposits, and many other financial products and services are now national, if not international, in scope. These changes are the result of a combination of factors, including technological innovations, the erosion of legal barriers, and an increasingly mobile society.

Technology has expanded the potential availability of credit and made possible virtually instantaneous credit decisions. Mortgage financing that once took weeks, for example, now can take only hours. Consumer credit can be obtained at the point of sale at retailers and even when buying a major item such as a car. Consumers can shop for investment products and deposits online. With respect to deposits, they can compare rates and duration of a variety of deposit products offered by financial institutions located far from where the consumer resides.

Changes in applicable law also have contributed to the expansion of markets for national banks and their operating subsidiaries. These changes have affected both the type of products that may be offered and the geographic region in which banks—large and small—may conduct business. As a result of these changes, banks may branch across state lines and offer a broader array of products than ever before. An even wider range of

“business of banking” is not limited to the powers enumerated in 12 U.S.C. 24(Seventh) and that the OCC has the discretion to authorize activities beyond those specifically enumerated in the statute. See 513 U.S. at 258 n.2.

<sup>20</sup> 12 U.S.C. 93a.

<sup>21</sup> 12 U.S.C. 371(a).

D. Hawke, Jr., Comptroller of the Currency, to Representatives Sue Kelly, Peter King, Carolyn B. Maloney, and Carolyn McCarthy (Dec. 23, 2003).

<sup>14</sup> See, e.g., *Nationsbank of North Carolina, N.A. v. Variable Annuity Life Ins. Co.*, 513 U.S. 251, 258 n.2 (1995) (*VALIC*).

<sup>15</sup> See, e.g., 12 U.S.C. 93a.

<sup>16</sup> 68 FR 46119, 46120.

customers can be reached through the use of technology, including the Internet. Community national banks, as well as the largest national banks, use new technologies to expand their reach and service to customers.

Our modern society is also highly mobile. Forty million Americans move annually, according to a recent Congressional report issued in connection with enactment of the Fair and Accurate Credit Transactions Act of 2003.<sup>22</sup> And when they move, they often have the desire, if not the expectation, that the financial relationships and status they have established will be portable and will remain consistent.

These developments highlight the significance of being able to conduct a banking business pursuant to consistent, national standards, regardless of the location of a customer when he or she first becomes a bank customer or the location to which the customer may move *after* becoming a bank customer. They also accentuate the costs and interference that diverse and potentially conflicting state and local laws have on the ability of national banks to operate under the powers of their Federal charter. For national banks, moreover, the ability to operate under uniform standards of operation and supervision is fundamental to the character of their national charter.<sup>23</sup> When national banks are unable to operate under national standards, it also implicates the role and responsibilities of the OCC.

These concerns have been exacerbated recently, by increasing efforts by states and localities to apply state and local laws to bank activities. As we have learned from our experience supervising national banks, from the inquiries received by the OCC's Law Department, by the extent of litigation in recent years over these state efforts, and by the comments we received on the proposal, national banks' ability to conduct operations to the full extent authorized by Federal law has been curtailed as a result.

Commenters noted that the variety of state and local laws that have been enacted in recent years—including laws regulating fees, disclosures, conditions on lending, and licensing—have created higher costs and increased operational

challenges.<sup>24</sup> Other commenters noted the proliferation of state and local anti-predatory lending laws and the impact that those laws are having on lending in the affected jurisdictions. As a result, national banks must either absorb the costs, pass the costs on to consumers, or eliminate various products from jurisdictions where the costs are prohibitive. Commenters noted that this result is reached even in situations where a bank concludes that a law is preempted, simply so that the bank may avoid litigation costs or anticipated reputational injury.

As previously noted, the elimination of legal and other barriers to interstate banking and interstate financial service operations has led a number of banking organizations to operate, in multi-state metropolitan statistical areas, and on a multi-state or nationwide basis, exacerbating the impact of the overlay of state and local standards and requirements on top of the Federal standards and OCC supervisory requirements already applicable to national bank operations. When these multi-jurisdictional banking organizations are subject to regulation by each individual state or municipality in which they conduct operations, the problems noted earlier are compounded.

Even the efforts of a single state to regulate the operations of a national bank operating only within that state can have a detrimental effect on that bank's operations and consumers. As we explained in our recent preemption determination and order responding to National City Bank's inquiry concerning the Georgia Fair Lending Act (GFLA),<sup>25</sup> the GFLA caused secondary market participants to cease purchasing certain Georgia mortgages and many mortgage lenders to stop making mortgage loans in Georgia. National banks have also been forced to withdraw from some products and markets in other states as a result of the impact of state and local restrictions on their activities.

When national banks are unable to operate under uniform, consistent, and predictable standards, their business suffers, which negatively affects their

safety and soundness. The application of multiple, often unpredictable, different state or local restrictions and requirements prevents them from operating in the manner authorized under Federal law, is costly and burdensome, interferes with their ability to plan their business and manage their risks, and subjects them to uncertain liabilities and potential exposure. In some cases, this deters them from making certain products available in certain jurisdictions.<sup>26</sup>

The OCC therefore is issuing this final rule in furtherance of its responsibility to enable national banks to operate to the full extent of their powers under Federal law, without interference from inconsistent state laws, consistent with the national character of the national banking system, and in furtherance of their safe and sound operations. The final rule does not entail any new powers for national banks or any expansion of their existing powers. Rather, we intend only to ensure the soundness and efficiency of national banks' operations by making clear the standards under which they do business.

#### *B. Pursuant to 12 U.S.C. 93a and 371, the OCC May Adopt Regulations That Preempt State Law*

The OCC has ample authority to provide, by regulation, that types of state laws are not applicable to national banks. As mentioned earlier, 12 U.S.C. 93a grants the OCC comprehensive rulemaking authority to further its responsibilities, stating that—

Except to the extent that authority to issue such rules and regulations has been expressly and exclusively granted to another regulatory agency, the Comptroller of the Currency is authorized to prescribe rules and regulations to carry out the responsibilities of the office \* \* \*.<sup>27</sup>

This language is significantly broader than that customarily used to convey rulemaking authority to an agency, which is typically focused on a particular statute. This was recognized, some 20 years ago, by the United States Court of Appeals for the D.C. Circuit in

<sup>24</sup> Illustrative of comments along these lines were those of banks who noted that various state laws would result in the following costs: (a) Approximately \$44 million in start-up costs incurred by 6 banks as a result of a recently-enacted California law mandating a minimum payment warning; (b) 250 programming days required to change one of several computer systems that needed to be changed to comply with anti-predatory lending laws enacted in three states and the District of Columbia; and (c) \$7.1 million in costs a bank would incur as a result of complying with mandated annual statements to credit card customers.

<sup>25</sup> See 68 FR 46264 (Aug. 5, 2003).

<sup>26</sup> As was recently observed by Federal Reserve Board Chairman Alan Greenspan (in the context of amendments to the Fair Credit Reporting Act), "[l]imits on the flow of information among financial market participants, or increased costs resulting from restrictions that differ based on geography, may lead to an increase in the price or a reduction in the availability of credit, as well as a reduction in the optimal sharing of risk and reward." Letter of February 28, 2003, from Alan Greenspan, Chairman, Board of Governors of the Federal Reserve System, to The Honorable Ruben Hinojosa (emphasis added).

<sup>27</sup> 12 U.S.C. 93a.

<sup>22</sup> See S. Rep. No. 108-166, at 10 (2003) (quoting the hearing testimony of Secretary of the Treasury Snow).

<sup>23</sup> As we explained last year in the preamble to our amendments to part 7 concerning national banks' electronic activities, "freedom from State control over a national bank's powers protects national banks from conflicting local laws unrelated to the purpose of providing the uniform, nationwide banking system that Congress intended." 67 FR 34992, 34997 (May 17, 2002).

its decision confirming that 12 U.S.C. 93a authorizes the OCC to issue regulations preempting state law. In *Conference of State Bank Supervisors v. Conover*,<sup>28</sup> the Conference of State Bank Supervisors (CSBS) sought to overturn a district court decision upholding OCC regulations that provided flexibility regarding the terms on which national banks may make or purchase adjustable rate mortgages (ARMs) and that preempted inconsistent state laws. The regulations provided generally that national banks may make or purchase ARMs without regard to state law limitations. The district court granted the OCC's motion for summary judgment on the ground that the regulations were within the scope of the OCC's rulemaking powers granted by Congress.

On appeal, the CSBS asserted that 12 U.S.C. 93a grants the OCC authority to issue only "housekeeping" procedural regulations. In support of this argument, the CSBS cited a remark from the legislative history of 12 U.S.C. 93a by Senator Proxmire that 12 U.S.C. 93a "carries with it no new authority to confer on national banks powers which they do not have under existing law." CSBS also cited a statement in the conference report that 12 U.S.C. 93a "carries no authority [enabling the Comptroller] to permit otherwise impermissible activities of national banks with specific reference to the provisions of the McFadden Act and the Glass-Steagall Act."<sup>29</sup>

The Court of Appeals rejected the CSBS's contentions concerning the proper interpretation of 12 U.S.C. 93a. The Court of Appeals explained first that the challenged regulations (like this final rule) did not confer any new powers on national banks. Moreover, [t]hat the Comptroller also saw fit to preempt those state laws that conflict with his responsibility to ensure the safety and soundness of the national banking system, see 12 U.S.C. § 481, does not constitute an expansion of the powers of national banks.<sup>30</sup>

Nor did the Court of Appeals find support for the CSBS's position in the conference report:

As the "specific reference" to the McFadden and Glass-Steagall Acts indicates, the "impermissible activities" which the Comptroller is not empowered to permit are activities that are impermissible under federal, not state, law.<sup>31</sup>

The court summarized its rationale for holding that 12 U.S.C. 93a authorized

the OCC to issue the challenged regulations by saying:

It bears repeating that the entire legislative scheme is one that contemplates the operation of state law only in the absence of federal law and where such state law does not conflict with the policies of the National Banking Act. *So long as he does not authorize activities that run afoul of federal laws governing the activities of the national banks, therefore, the Comptroller has the power to preempt inconsistent state laws.*<sup>32</sup>

The authority under 12 U.S.C. 93a described by the court in *CSBS v. Conover* thus amply supports the adoption of regulations providing that specified types of state laws purporting to govern as applied to national banks' lending and deposit-taking activities are preempted.

Under 12 U.S.C. 371, the OCC has the additional and specific authority to provide that the specified types of laws relating to national banks' real estate lending activities are preempted. As we have described and as recognized in *CSBS v. Conover*,<sup>33</sup> 12 U.S.C. 371 grants the OCC unique rulemaking authority with regard to national banks' real estate lending activities. That section states:

[a]ny national banking association may make, arrange, purchase or sell loans or extensions of credit secured by liens on interests in real estate, subject to section 1828(o) of this title and such restrictions and requirements as the Comptroller of the Currency may prescribe by regulation or order.<sup>34</sup>

The language and history of 12 U.S.C. 371 confirm the real estate lending powers of national banks and that only the OCC "subject to other applicable Federal law "and not the states may impose restrictions or requirements on national banks' exercise of those powers. The Federal powers conferred by 12 U.S.C. 371 are subject *only* "to section 1828(o) of this title and such restrictions and requirements as the Comptroller of the Currency may prescribe by regulation or order."<sup>35</sup>

<sup>32</sup> *Id.* at 878 (emphasis added).

<sup>33</sup> In *CSBS v. Conover*, the court also held that the authority conferred by 12 U.S.C. 371, as the statute read at the time relevant to the court's decision, conferred authority upon the OCC to issue the preemptive regulations challenged in that case. The version of section 371 considered by the court authorized national banks to make real estate loans "subject to such terms, conditions, and limitations" as prescribed by the Comptroller by order, rule or regulations. The court said that the "restrictions and requirements" language contained in the statute today was "not substantially different" from the language that it was considering in that case. *Id.* at 884.

<sup>34</sup> 12 U.S.C. 371(a).

<sup>35</sup> *Id.* As noted *supra* at note 7, Federal legislation occasionally provides that national banks shall conduct certain activities subject to state law

Thus, the exercise of the powers granted by 12 U.S.C. 371 is not conditioned on compliance with any state requirement, and state laws that attempt to confine or restrain national banks' real estate lending activities are inconsistent with national banks' real estate lending powers under 12 U.S.C. 371.

This conclusion is consistent with the fact that national bank real estate lending authority has been extensively regulated at the *Federal* level since the power first was codified. Beginning with the enactment of the Federal Reserve Act of 1913,<sup>36</sup> national banks' real estate lending authority has been governed by the express terms of 12 U.S.C. 371. As originally enacted in 1913, section 371 contained a limited grant of authority to national banks to lend on the security of "improved and unencumbered farm land, situated within its Federal reserve district."<sup>37</sup> In addition to the geographic limits inherent in this authorization, the Federal Reserve Act also imposed limits on the term and amount of each loan as well as an aggregate lending limit. Over the years, 12 U.S.C. 371 was repeatedly amended to broaden the types of real estate loans national banks were permitted to make, to expand geographic limits, and to modify loan term limits and per-loan and aggregate lending limits.

In 1982, Congress removed these "rigid statutory limitations"<sup>38</sup> in favor of a broad provision that is very similar to the current law and that authorized national banks to "make, arrange, purchase or sell loans or extensions of credit secured by liens on interests in real estate, subject to such terms, conditions, and limitations as may be prescribed by the Comptroller of the Currency by order, rule, or regulation."<sup>39</sup> The purpose of the 1982 amendment was "to provide national banks with the ability to engage in more creative and flexible financing, and to become stronger participants in the home financing market."<sup>40</sup> In 1991, Congress removed the term "rule" from this phrase and enacted an additional requirement, codified at 12 U.S.C.

standards. For example, national banks conduct insurance sales, solicitation, and cross-marketing activities subject to certain types of state restrictions expressly set out in the Gramm-Leach-Bliley Act. See 15 U.S.C. 6701(d)(2)(B). There is no similar Federal legislation subjecting national banks' real estate lending activities to state law standards.

<sup>36</sup> Federal Reserve Act, Dec. 23, 1913, ch. 6, 38 Stat. 251, as amended.

<sup>37</sup> *Id.* section 24, 38 Stat. 273.

<sup>38</sup> S. Rep. No. 97-536, at 27 (1982).

<sup>39</sup> Garn-St Germain Depository Institutions Act of 1982, Pub. L. 97-320, section 403, 96 Stat. 1469, 1510-11 (1982).

<sup>40</sup> S. Rep. No. 97-536, at 27 (1982).

<sup>28</sup> 710 F.2d 878 (D.C. Cir. 1983).

<sup>29</sup> *Id.* at 885 (emphasis in original).

<sup>30</sup> *Id.* (emphasis in original).

<sup>31</sup> *Id.*

1828(o), that national banks (and other insured depository institutions) conduct real estate lending pursuant to uniform standards adopted at the Federal level by regulation of the OCC and the other Federal banking agencies.<sup>41</sup>

Thus, the history of national banks' real estate lending activities under 12 U.S.C. 371 is one of extensive Congressional involvement gradually giving way to a streamlined approach in which Congress has delegated broad rulemaking authority to the Comptroller. The two versions of 12 U.S.C. 371—namely, the lengthy and prescriptive approach prior to 1982 and the more recent statement of broad authority qualified only by reference to Federal law—may be seen as evolving articulations of the same idea.

*C. The Preemption Standard Applied in This Final Rule Is Entirely Consistent With the Standards Articulated by the Supreme Court*

State laws are preempted by Federal law, and thus rendered invalid with respect to national banks, by operation of the Supremacy Clause of the U.S. Constitution.<sup>42</sup> The Supreme Court has identified three ways in which this may occur. First, Congress can adopt express language setting forth the existence and scope of preemption.<sup>43</sup> Second, Congress can adopt a framework for regulation that “occupies the field” and leaves no room for states to adopt supplemental laws.<sup>44</sup> Third, preemption may be found when state law actually conflicts with Federal law. Conflict will be found when either: (i) compliance with both laws is a “physical impossibility;”<sup>45</sup> or (ii) when the state law stands “as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.”<sup>46</sup>

In *Barnett Bank of Marion County v. Nelson*,<sup>47</sup> the Supreme Court articulated preemption standards used by the

Supreme Court in the national bank context to determine, under the Supremacy Clause of the U.S. Constitution, whether Federal law conflicts with state law such that the state law is preempted. As observed by the Supreme Court in *Barnett*, a state law will be preempted if it conflicts with the exercise of a national bank's Federally authorized powers.

The Supreme Court noted in *Barnett* the many formulations of the conflicts standard. The Court stated:

In defining the pre-emptive scope of statutes and regulations granting a power to national banks, these cases take the view that normally Congress would not want States to forbid, or impair significantly, the exercise of a power that Congress explicitly granted. To say this is not 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. See, e.g., *Anderson Nat. Bank v. Lockett*, 321 U.S. 233, 247–252 (1944) (state statute administering abandoned deposit accounts did not “unlawful[ly] encroac[h] on the rights and privileges of national banks”); *McClellan v. Chipman*, 164 U.S. 347, 358 (1896) (application to national banks of state statute forbidding certain real estate transfers by insolvent transferees would not “destro[y] or hampe[r]” national banks' functions); *National Bank v. Commonwealth*, 76 U.S. (9 Wall.) 353, 362 (1869) (national banks subject to state law that does not “interfere with, or impair [national banks'] efficiency in performing the functions by which they are designed to serve [the Federal Government]”).<sup>48</sup>

The variety of formulations quoted by the Court—“unlawfully encroach,” “hamper,” “interfere with or impair national banks' efficiency”—defeats any suggestion that any one phrase constitutes the exclusive standard for preemption. As the Supreme Court explained in *Hines v. Davidowitz*:<sup>49</sup>

There is not—and from the very nature of the problem there cannot be—any rigid formula or rule which can be used as a universal pattern to determine the meaning and purpose of every act of Congress. This Court, in considering the validity of state laws in the light of

treaties or federal laws touching the same subject, has made use of the following expressions: conflicting; contrary to; occupying the field; repugnance; difference; irreconcilability; inconsistency; violation; curtailment; and interference. *But none of these expressions provides an infallible constitutional test or an exclusive constitutional yardstick. In the final analysis, there can be no one crystal clear distinctly marked formula.* Our primary function is to determine whether, under the circumstances of this particular case, [the state law at issue] stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.<sup>50</sup>

Thus, in *Hines*, the Court recognized that the Supremacy Clause principles of preemption can be articulated in a wide variety of formulations that do not yield substantively different legal results. The variation among formulations that carry different linguistic connotations does not produce different legal outcomes.

We have adopted in this final rule a statement of preemption principles that is consistent with the various formulations noted earlier. The phrasing used in the final rule—obstruct,<sup>51</sup> impair,<sup>52</sup> or condition<sup>53</sup>—differs somewhat from what we proposed. This standard conveys the same substantive point as the proposed standard, however; that is, that state laws do not apply to national banks if they impermissibly contain a bank's exercise of a federally authorized power. The words of the final rule, which are drawn directly from applicable Supreme Court precedents, better convey the range of effects on national bank powers that the Court has found to be impermissible. The OCC intends this phrase as the distillation of the various preemption constructs articulated by the Supreme Court, as recognized in *Hines* and *Barnett*, and not as a replacement construct that is in any way inconsistent with those standards.

In describing the proposal, we invited comment on whether it would be appropriate to assert occupation of the entire field of real estate lending. Some commenters strongly urged that we do so, and that we go beyond real estate lending to cover other lending and deposit-taking activities as well. Upon further consideration of this issue and

<sup>41</sup> See section 304 of the Federal Deposit Insurance Corporation Improvement Act, codified at 12 U.S.C. 1828(o). These standards governing national banks' real estate lending are set forth in Subpart D of 12 CFR part 34.

<sup>42</sup> “This Constitution, and the Laws of the United States which shall be made in Pursuance thereof \* \* \* shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.” U.S. Const. art. VI, cl. 2.

<sup>43</sup> See *Jones v. Rath Packing Co.*, 430 U.S. 519, 525 (1977).

<sup>44</sup> See *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947).

<sup>45</sup> *Florida Lime & Avocado Growers, Inc. v. Paul*, 373 U.S. 132, 143 (1963).

<sup>46</sup> *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941); *Barnett Bank of Marion County, N.A. v. Nelson*, 517 U.S. 25, 31 (1996) (quoting *Hines*).

<sup>47</sup> 517 U.S. 25 (1996).

<sup>48</sup> *Id.* at 33–34. Certain commenters cite *Nat'l Bank v. Commonwealth* for the proposition that national banks are subject to state law. These commenters, however, omit the important caveat, quoted by the *Barnett* Court, that state law applies only where it does not “interfere with, or impair [national banks'] efficiency in performing the functions by which they are designed to serve [the Federal] Government.”

<sup>49</sup> 312 U.S. 52 (1941).

<sup>50</sup> *Id.* at 67 (emphasis added) (citations omitted).

<sup>51</sup> See *Hines*, 312 U.S. at 76.

<sup>52</sup> See *Nat'l Bank v. Commonwealth*, 76 U.S. at 362; *Davis v. Elmira Savings Bank*, 161 U.S. 275, 283 (1896); *McClellan*, 164 U.S. at 357.

<sup>53</sup> See *Barnett*, 517 U.S. at 34; *Franklin Nat'l Bank of Franklin Square v. New York*, 347 U.S. 373, 375–79 (1954).

careful review of comments submitted pertaining to this point, we have concluded, as the Supreme Court recognized in *Hines* and reaffirmed in *Barnett*, that the effect of labeling of this nature is largely immaterial in the present circumstances. Thus, we decline to adopt the suggestion of these commenters that we declare that these regulations “occupy the field” of national banks’ real estate lending, other lending, and deposit-taking activities. We rely on our authority under both 12 U.S.C. 93a and 371, and to the extent that an issue arises concerning the application of a state law not specifically addressed in the final regulation, we retain the ability to address those questions through interpretation of the regulation, issuance of orders pursuant to our authority under 12 U.S.C. 371, or, if warranted by the significance of the issue, by rulemaking to amend the regulation.

## V. Description of the Final Rule

### A. Amendments to Part 34

1. Section 34.3(a). The final rule retains the statement of national banks’ real estate lending authority, now designated as § 34.3(a), that national banks may “make, arrange, purchase, or sell loans or extensions of credit, or interests therein, that are secured by liens on, or interests in, real estate (real estate loans), subject to 12 U.S.C. 1828(o) and such restrictions and requirements as the Comptroller of the Currency may prescribe by regulation or order.”

2. Section 34.3(b). New § 34.3(b) adds an explicit safety and soundness-derived anti-predatory lending standard to the general statement of authority concerning lending. Many bank commenters voiced concern that the proposed anti-predatory lending standard, by prohibiting a national bank from making a loan based predominantly on the foreclosure value of a borrower’s collateral without regard to the borrower’s repayment ability, would also prohibit a national bank from engaging in legitimate, non-predatory lending activities. These commenters noted that reverse mortgage, small business, and high net worth loans are often made based on the value of the collateral.

We have revised the anti-predatory lending standard in the final rule to clarify that it applies to consumer loans only, (*i.e.*, loans for personal, family, or household purposes), and to clarify that it is intended to prevent borrowers from being unwittingly placed in a situation where repayment is unlikely without the lender seizing the collateral. Where

the bargain agreed to by a borrower and a lender involves an understanding by the borrower that it is likely or expected that the collateral will be used to repay the debt, such as with a reverse mortgage, it clearly is not objectionable that the collateral will then be used in such a manner. Moreover, the final rule’s anti-predatory lending standard is not intended to apply to business lending or to situations where a borrower’s net worth would support the loan under customary underwriting standards.

Thus, we have revised the anti-predatory lending standard so that it focuses on consumer loans and permits a national bank to use a variety of reasonable methods to determine a borrower’s ability to repay, including, for example, the borrower’s current and expected income, current and expected cash flows, net worth, other relevant financial resources, current financial obligations, employment status, credit history, or other relevant factors.

Several commenters urged the OCC to expressly affirm that a national bank’s lending practices must be conducted in conformance with section 5 of the FTC Act, which makes unlawful “unfair or deceptive acts or practices” in interstate commerce,<sup>54</sup> and regulations promulgated thereunder. As discussed in more detail in section VI of this preamble, the OCC has taken actions against national banks under the FTC Act where the OCC believed they were engaged in unfair or deceptive practices. As demonstrated by these actions, the OCC recognizes the importance of national banks and their operating subsidiaries acting in conformance with the standards contained in section 5 of the FTC Act. We therefore agree that an express reference to those standards in our regulation would be appropriate and have added it to the final rules.<sup>55</sup>

3. *State laws that are preempted* (§ 34.4(a)). Pursuant to 12 U.S.C. 93a and 371, the final rule amends § 34.4(a) to add to the existing regulatory list of types of state law restrictions and requirements that are not applicable to national banks. This list, promulgated under our authority “to prescribe rules and regulations to carry out the responsibilities of the office” and to

<sup>54</sup> 15 U.S.C. 45(a)(1).

<sup>55</sup> It is important to note here that we lack the authority to do what some commenters essentially urged, namely, to specify by regulation that particular practices, such as loan “flipping” or “equity stripping,” are unfair or deceptive. While we have the ability to take enforcement actions against national banks if they engage in unfair or deceptive practices under section 5 of the FTC Act, the OCC does not have rulemaking authority to define specific practices as unfair or deceptive under section 5. See 15 U.S.C. 57a(f).

prescribe the types of restrictions and requirements to which national banks’ real estate lending activities shall be subject, reflects our experience with types of state laws that can materially affect and confine—and thus are inconsistent with—the exercise of national banks’ real estate lending powers.<sup>56</sup>

The final rule revises slightly the introductory clause used in proposed § 34.4(a) in order to conform this section more closely to the amended sections of part 7 discussed later in this preamble. Thus, the final rule provides: “Except where made applicable by Federal law, state laws that obstruct, impair, or condition a national bank’s ability to fully exercise its Federally authorized real estate lending powers do not apply to national banks.” The final rule then expands the current list of the types of state law restrictions and requirements that are not applicable to national banks.

Many of the supporting commenters requested that the final rule clarify the extent to which particular state or local laws that were not included in the proposal are preempted. For example, these commenters suggested that the final rule address particular state laws imposing various limitations on mortgage underwriting and servicing.

We decline to address most of these suggestions with the level of specificity requested by the commenters. Identifying state laws in a more generic way avoids the impression that the regulations only cover state laws that appear on the list. The list of the types of preempted state laws is not intended to be exhaustive, and we retain the ability to address other types of state laws by order on a case-by-case basis, as appropriate, to make determinations whether they are preempted under the applicable standards.<sup>57</sup>

4. *State laws that are not preempted* (§ 34.4(b)). Section 34.4(b) also provides that certain types of state laws are not preempted and would apply to national banks to the extent that they are consistent with national banks’ Federal authority to engage in real estate lending because their effect on the real estate

<sup>56</sup> As we noted in our discussion of this list in the preamble to the proposal, the “OCC and Federal courts have thus far concluded that a wide variety of state laws are preempted, either because the state laws fit within the express preemption provisions of an OCC regulation or because the laws conflict with a Federal power vested in national banks.” See 68 FR 46119, 46122–46123. The list is also substantially identical to the types of laws specified in a comparable regulation of the OTS. See 12 CFR 560.2(b).

<sup>57</sup> See, *e.g.*, OCC Determination and Order concerning the Georgia Fair Lending Act, *supra* footnote 25.

lending operations of national banks is only incidental. These types of laws generally pertain to contracts, rights to collect debts, acquisition and transfer of property, taxation, zoning, crimes, torts,<sup>58</sup> and homestead rights. In addition, any other law the effect of which is incidental to national banks' lending authority or otherwise consistent with national banks' authority to engage in real estate lending would not be preempted.<sup>59</sup> In general, these would be laws that do not attempt to regulate the manner or content of national banks' real estate lending, but that instead form the legal infrastructure that makes it practicable to exercise a permissible Federal power.

One category of state law included in the proposed list of state laws generally not preempted was "debt collection." Consistent with Supreme Court precedents addressing this type of state law,<sup>60</sup> we have revised the language of the final rule to refer to national banks' "right to collect debts."

#### *B. Amendments to Part 7—Deposit-Taking, Other Consumer Lending, and National Bank Operations*

The final rule adds three new sections to part 7: § 7.4007 regarding deposit-taking activities, § 7.4008 regarding non-real estate lending activities, and § 7.4009 regarding national bank operations. The structure of the amendments is the same for §§ 7.4007 and 7.4008 and is similar for § 7.4009.

For § 7.4007, the final rule first sets out a statement of the authority to engage in the activity. Second, the final

rule notes that state laws that obstruct, impair, or condition a national bank's ability to fully exercise the power in question are not applicable, and lists several types of state laws that are preempted. Types of state laws that are generally preempted under § 7.4007 include state requirements concerning abandoned and dormant accounts, checking accounts, disclosure requirements, funds availability, savings account orders of withdrawal, state licensing or registration requirements, and special purpose savings services. Finally, the final rule lists types of state laws that, as a general matter, are not preempted. Examples of these laws include state laws concerning contract, rights to collect debt, tort, zoning, and property transfers. These lists are not intended to be exhaustive, and the OCC retains the ability to address other types of state laws on a case-by-case basis to make preemption determinations under the applicable standards.

For § 7.4008, the final rule also sets out a statement of the authority to engage in the activity (non-real estate lending), notes that state laws that obstruct, impair, or condition a national bank's ability to fully exercise this power are not applicable, and lists several types of state laws that are, or are not, preempted. Section 7.4008 also includes a safety and soundness-based anti-predatory lending standard. Final § 7.4008(b) states that "[a] national bank shall not make a consumer loan subject to this § 7.4008 based predominantly on the bank's realization of the foreclosure or liquidation value of the borrower's collateral, without regard to the borrower's ability to repay the loan according to its terms. A bank may use any reasonable method to determine a borrower's ability to repay, including, for example, the borrower's current and expected income, current and expected cash flows, net worth, other relevant financial resources, current financial obligations, employment status, credit history, or other relevant factors." Separately, § 7.4008(c) also includes a statement that a national bank shall not engage in unfair or deceptive practices within the meaning of section 5 of the FTC Act and regulations promulgated thereunder in connection with making non-real estate related loans. The standards set forth in § 7.4008(b) and (c), plus an array of Federal consumer protection standards,<sup>61</sup> ensure that national banks are subject to consistent and uniform Federal standards, administered and enforced by the OCC, that provide strong and extensive customer protections and appropriate

safety and soundness-based criteria for their lending activities.

In § 7.4009, the final rule first states that national banks may exercise all powers authorized to them under Federal law.<sup>62</sup> Second, the final rule states that except as otherwise made applicable by Federal law, state laws that obstruct, impair, or condition a national bank's ability to fully exercise its authorized powers do not apply to the national bank.<sup>63</sup> Finally, the final rule lists several types of state laws that, as a general matter, are *not* preempted. For the reasons outlined earlier in the discussion of the amendments to 12 CFR part 34, the reference to debt collection laws has been revised to refer to state laws concerning national banks' "rights to collect debts."

The OCC's regulations adopted in this final rule address the applicability of state law with respect to a number of specific types of activities. The question may persist, however, about the extent to which state law may permissibly govern powers or activities that have not been addressed by Federal court precedents or OCC opinions or orders. Accordingly, as noted earlier, new § 7.4009 provides that state laws do not apply to national banks if they obstruct, impair, or condition a national bank's ability to fully exercise the powers authorized to it under Federal law, including the content of those activities and the manner in which and standards whereby they are conducted.

As explained previously, in some circumstances, of course, Federal law directs the application of state standards to a national bank. The wording of § 7.4009 reflects that a Federal statute may require the application of state

<sup>58</sup> See *Bank of America v. City & County of San Francisco*, 309 F.3d 551, 559 (9th Cir. 2002).

<sup>59</sup> The label a state attaches to its laws will not affect the analysis of whether that law is preempted. For instance, laws related to the transfer of real property may contain provisions that give borrowers the right to "cure" a default upon acceleration of a loan if the lender has not foreclosed on the property securing the loan. Viewed one way, this could be seen as part of the state laws governing foreclosure, which historically have been within a state's purview. However, as we concluded in the OCC Determination and Order concerning the GFLA, to the extent that this type of law limits the ability of a national bank to adjust the terms of a particular class of loans once there has been a default, it would be a state law limitation "concerning \* \* \* (2) The schedule for the repayment of principal and interest; [or] (3) The term to maturity of the loan \* \* \* " 12 CFR 34.4(a). In such a situation, we would be governed by the effect of the state statute.

<sup>60</sup> See, e.g., *Nat'l Bank v. Commonwealth*, 76 U.S. at 362 (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. All their contracts are governed and construed by State laws. Their acquisition and transfer of property, their right to collect their debts, and their liability to be sued for debts, are all based on State law.") (emphasis added); see also *McClellan*, 164 U.S. at 356-57 (quoting *Nat'l Bank v. Commonwealth*).

<sup>61</sup> See *supra* note 10.

<sup>62</sup> As noted in the proposal, the OTS has issued a regulation providing generally that state laws purporting to address the operations of Federal savings associations are preempted. See 12 CFR 545.2. The extent of Federal regulation and supervision of Federal savings associations under the Home Owners' Loan Act is substantially the same as for national banks under the national banking laws, a fact that warrants similar conclusions about the applicability of state laws to the conduct of the Federally authorized activities of both types of entities. Compare, e.g., 12 U.S.C. 1464(a) (OTS authorities with respect to the organization, incorporation, examination, operation, regulation, and chartering of Federal savings associations) with 12 U.S.C. 21 (organization and formation of national banking associations), 12 U.S.C. 481 (OCC authority to examine national banks and their affiliates), 12 U.S.C. 484 (OCC's exclusive visitatorial authority), and 12 U.S.C. 93a (OCC authority to issue regulations).

<sup>63</sup> As noted previously, the final rule makes changes to the introductory clause concerning the applicability of state law in 12 CFR 34.4(a), 7.4007(b), 7.4008(d), and 7.4009(b) to make the language of these sections more consistent with each other.

law,<sup>64</sup> or it may incorporate—or “Federalize”—state standards.<sup>65</sup> In those circumstances, the state standard obviously applies. State law may also apply if it only incidentally affects a national bank’s Federally authorized powers or if it is otherwise consistent with national banks’ uniquely Federal status. Like the other provisions of this final rule, § 7.4009 recognizes the potential applicability of state law in these circumstances. This approach is consistent with the Supreme Court’s observation that national banks “are governed in their daily course of business far more by the laws of the state than of the nation.”<sup>66</sup> However, as noted previously, these types of laws typically do not regulate the manner or content of the business of banking authorized for national banks, but rather establish the legal infrastructure that makes practicable the conduct of that business.

### C. Application of Amendments to Operating Subsidiaries

As a matter of Federal law, national bank operating subsidiaries conduct their activities under a Federal license, subject to the same terms and conditions as apply to the parent banks, except where Federal law provides otherwise. See 12 CFR 5.34 and 7.4006. See also 12 CFR 34.1(b)(real estate activities specifically).<sup>67</sup> Thus, by virtue of preexisting OCC regulations, the changes to parts 7 and 34, including the new anti-predatory lending standards applicable to lending activities, apply to both national banks and their operating subsidiaries. The final rule makes no change to these existing provisions.

## VI. The OCC’s Commitment to Fair Treatment of National Bank Customers and High Standards of National Bank Operations

The OCC shares the view of the commenters that predatory and abusive lending practices are inconsistent with national objectives of encouraging home ownership and community revitalization, and can be devastating to individuals, families, and communities.

<sup>64</sup> See, e.g., 15 U.S.C. 6711 (insurance activities of national banks are “functionally regulated” by the states, subject to the provisions on the operation of state law contained in section 104 of the Gramm-Leach-Bliley Act).

<sup>65</sup> See, e.g., 12 U.S.C. 92a (permissible fiduciary activities for national banks determined by reference to state law).

<sup>66</sup> *Nat’l Bank v. Commonwealth*, 76 U.S. at 362 (holding that shares held by shareholders of a national bank were lawfully subject to state taxation).

<sup>67</sup> For a detailed discussion of this issue, see the OCC’s visitorial powers rulemaking also published today in the **Federal Register**.

We will not tolerate such practices by national banks and their operating subsidiaries. Our Advisory Letters on predatory lending,<sup>68</sup> our pioneering enforcement positions resulting in substantial restitution to affected consumers, and the anti-predatory lending standards adopted in this final rule reflect our commitment that national banks operate pursuant to high standards of integrity in all respects. The provisions of this final rule, clarifying that certain state laws are not applicable to national banks’ operations, do not undermine the application of these standards to all national banks, for the protection of all national bank customers—wherever they are located.

Advisory Letters 2003–2, which addresses loan originations, and 2003–3, which addresses loan purchases and the use of third party loan brokers, contain the most comprehensive supervisory standards ever published by any Federal financial regulatory agency to address predatory and abusive lending practices and detail steps for national banks to take to ensure that they do not engage in such practices. As explained in the Advisory Letters, if the OCC has evidence that a national bank has engaged in abusive lending practices, we will review those practices not only to determine whether they violate specific provisions of law such as the Homeowners Equity Protection Act of 1994 (HOEPA), the Fair Housing Act, or the Equal Credit Opportunity Act, but also to determine whether they involve unfair or deceptive practices that violate the FTC Act. Indeed, several practices that we identify as abusive in our Advisory Letters—such as equity stripping, loan flipping, and the refinancing of special subsidized mortgage loans that originally contained terms favorable to the borrower—generally can be found to be unfair or deceptive practices that violate the FTC Act.

Moreover, our enforcement record, including the OCC’s pioneering actions using the FTC Act to address consumer abuses that were not specifically prohibited by regulation, demonstrates our commitment to keeping abusive practices out of the national banking system. For example, *In the Matter of Providian Nat’l Bank, Tilton, New Hampshire*,<sup>69</sup> pursuant to the FTC Act, the OCC required payment by a national bank to consumers in excess of \$300 million and imposed numerous

conditions on the conduct of future business. Since the Providian settlement in 2000, the OCC has taken action under the FTC Act to address unfair or deceptive practices and consumer harm involving five other national banks.<sup>70</sup>

Most recently, on November 7, 2003, the OCC entered into a consent order with Clear Lake National Bank that requires the bank to reimburse fees and interest charged to consumers in a series of abusive home equity loans. More than \$100,000 will be paid to 30 or more borrowers. This is the first case brought by a Federal regulator under the FTC Act that cites the unfair nature of the terms of the loan. The OCC also found that the loans violated HOEPA, the Truth in Lending Act, and Real Estate Settlement Procedures Act.<sup>71</sup>

The OCC also has moved aggressively against national banks engaged in payday lending programs that involved consumer abuses. Specifically, we concluded four enforcement actions against national banks that had entered into contracts with payday lenders for loan originations, and in each case ordered the bank to terminate the relationship with the payday lender.<sup>72</sup>

<sup>70</sup> See *In the Matter of First Consumers National Bank, Beaverton, Oregon*, Enforcement Action 2003–100 (required restitution of annual fees and overlimit fees for credit cards); *In the Matter of Household Bank (SB), N.A., Las Vegas, Nevada*, Enforcement Action 2003–17 (required restitution regarding private label credit cards); *In the Matter of First National Bank in Brookings, Brookings, South Dakota*, Enforcement Action 2003–1 (required restitution regarding credit cards); *In the Matter of First National Bank of Marin, Las Vegas, Nevada*, Enforcement Action 2001–97 (restitution regarding credit cards); and *In the Matter of Direct Merchants Credit Card Bank, N.A., Scottsdale, Arizona*, Enforcement Action 2001–24 (restitution regarding credit cards). These orders can be found on the OCC’s Web site within the “Popular FOIA Requests” section at <http://www.occ.treas.gov/foia/foiadocs.htm>.

<sup>71</sup> See *In the Matter of Clear Lake National Bank, San Antonio, Texas*, Enforcement Action 2003–135 (Nov. 7, 2003), available at <http://www.occ.treas.gov/FTP/EAs/ea2003-135.pdf>. We believe these enforcement actions, which have generated hundreds of millions of dollars for consumers in restitution, also demonstrate that the OCC has the resources to enforce applicable laws. Indeed, as recently observed by the Superior Court of Arizona, Maricopa County, in an action brought by Arizona against a national bank, among others, the restitution and remedial action ordered by the OCC in that matter against the bank was “comprehensive and significantly broader in scope than that available through [the] state court proceedings.” *State of Arizona v. Hispanic Air Conditioning and Heating, Inc.*, CV 2000–003625, Ruling at 27, Conclusions of Law, paragraph 50 (Aug. 25, 2003).

<sup>72</sup> See *In the Matter of Peoples National Bank, Paris, Texas*, Enforcement Action 2003–2; *In the Matter of First National Bank in Brookings, Brookings, South Dakota*, Enforcement Action 2003–1; *In the Matter of Goleta National Bank, Goleta, California*, Enforcement Action 2002–93; and *In the Matter of Eagle National Bank, Upper Darby, Pennsylvania*, Enforcement Action 2001–

Other than these isolated incidences of abusive practices that have triggered the OCC's aggressive supervisory response, evidence that national banks are engaged in predatory lending practices is scant. Based on the absence of such information—from third parties, our consumer complaint database, and our supervisory process—we have no reason to believe that such practices are occurring in the national banking system to any significant degree. Although several of the commenters suggested this conclusion is implausible given the significant share of the lending market occupied by national banks, this observation is consistent with an extensive study of predatory lending conducted by the Department of Housing and Urban Development (HUD) and the Treasury Department,<sup>73</sup> and even with comments submitted in connection with an OTS rulemaking concerning preemption of state lending standards by 46 State Attorneys General.

Less than one year ago, nearly two dozen State Attorneys General signed a brief in litigation that reached the same conclusion. That case involved a revised regulation issued by the Office of Thrift Supervision to implement the Alternative Mortgage Transaction Parity Act (AMTPA). The revised regulation seeks to distinguish between Federally supervised thrift institutions and non-bank mortgage lenders and makes non-bank mortgage lenders subject to state law restrictions on prepayment penalties and late fees. In *supporting* the OTS's decision to retain preemption of state laws for supervised depository

institutions and their subsidiaries but *not* for unsupervised housing creditors, the State Attorneys General 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 of the leading subprime lenders are mortgage companies and finance companies, not banks or direct bank subsidiaries.*<sup>74</sup>

It is relevant for purposes of this final rule that the preemption regulations adopted by the OCC are substantially identical to the preemption regulations of the OTS that have been applicable to Federal thrifts for a number of years. It does not appear from public commentary—nor have the state officials indicated—that OTS preemption regulations have undermined the protection of customers of Federal thrifts. In their brief in the OTS litigation described above, the State Attorneys General referenced “the burdens of federal supervision,” in concluding that there “clearly is a substantial basis for OTS’s distinction”<sup>75</sup> between its supervised institutions and state housing creditors.

These considerations are equally applicable in the context of national banks, and were recognized, *again*, by all 50 State Attorneys General, in their comment letter to the OCC on this very regulation, which stated:

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*).<sup>76</sup>

The OCC is firmly committed to assuring that abusive practices—whether in connection with mortgage lending or other national bank activities—continue to have no place in the national banking system.

## VII. Regulatory Analysis

### *CDRI Act Delayed Effective Date*

This final rule takes effect 30 days after the date of its publication in the **Federal Register**, consistent with the delayed effective date requirement of the Administrative Procedure Act. *See*

5 U.S.C. 553(d). Section 302 of the Riegle Community Development and Regulatory Improvement Act of 1994 (CDRI Act), 12 U.S.C. 4802(b), provides that regulations that impose additional reporting, disclosure, or other requirements on insured depository institutions may not take effect before the first day of the quarter following publication unless the agency finds that there is good cause to make the rule effective at an earlier date. The regulations in this final rule require national banks to adhere to explicit safety and soundness-based anti-predatory lending standards. These standards prohibit national banks from engaging in certain harmful lending practices, thereby benefiting consumers. The final rule imposes no additional reporting, disclosure, or other requirements on national banks. Accordingly, in order for the benefits to become available as soon as possible, the OCC finds that there is good cause to dispense with the requirements of the CDRI Act.

### *Regulatory Flexibility Act*

Pursuant to section 605(b) of the Regulatory Flexibility Act, 5 U.S.C. 605(b) (RFA), the regulatory flexibility analysis otherwise required under section 604 of the RFA is not required if the agency certifies that the rule will not have a significant economic impact on a substantial number of small entities and publishes its certification and a short, explanatory statement in the **Federal Register** along with its rule.

Pursuant to section 605(b) of the RFA, the OCC hereby certifies that this final rule will not have a significant economic impact on a substantial number of small entities. Accordingly, a regulatory flexibility analysis is not needed. The amendments to the regulations identify the types of state laws that are preempted, as well as the types of state laws that generally are not preempted, in the context of national bank lending, deposit-taking, and other activities. These amendments simply provide the OCC's analysis and do not impose any new requirements or burdens. As such, they will not result in any adverse economic impact.

### *Executive Order 12866*

The OCC has determined that this final rule is not a significant regulatory action under Executive Order 12866.

### *Unfunded Mandates Reform Act of 1995*

Section 202 of the Unfunded Mandates Reform Act of 1995, Pub. L. 104-4 (2 U.S.C. 1532) (Unfunded Mandates Act), requires that an agency prepare a budgetary impact statement

104. These orders can also be found on the OCC's Web site within the “Popular FOIA Requests” section at <http://www.occ.treas.gov/foia/foiadocs.htm>.

<sup>73</sup> A Treasury-HUD joint report issued in 2000 found that predatory lending practices in the subprime market are less likely to occur in lending by—

banks, thrifts, and credit unions that are subject to extensive oversight and regulation \* \* \*. The subprime mortgage and finance companies that dominate mortgage lending in many low-income and minority communities, while subject to the same consumer protection laws, are not subject to as much federal oversight as their prime market counterparts—who are largely federally-supervised banks, thrifts, and credit unions. The absence of such accountability may create an environment where predatory practices flourish because they are unlikely to be detected.

Departments of Housing and Urban Development and the Treasury, “Curbing Predatory Home Mortgage Lending: A Joint Report” 17–18 (June 2000), available at <http://www.treas.gov/press/releases/report3076.htm>.

In addition, the report found that a significant source of abusive lending practices is non-regulated mortgage brokers and similar intermediaries who, because they “do not actually take on the credit risk of making the loan, \* \* \* may be less concerned about the loan’s ultimate repayment, and more concerned with the fee income they earn from the transaction.” *Id.* at 40.

<sup>74</sup> Brief for Amicus Curiae State Attorneys General, *Nat'l Home Equity Mortgage Ass'n v. OTS*, Civil Action No. 02-2506 (GK) (D.D.C.) at 10–11 (emphasis added).

<sup>75</sup> *Id.* at 10.

<sup>76</sup> National Association of Attorneys General comment letter on the proposal at 10 (Oct. 6, 2003) (emphasis added).

before promulgating any rule likely to result in a Federal mandate that may result in the expenditure by State, local, and tribal governments, in the aggregate, or by the private sector of \$100 million or more in any one year. If a budgetary impact statement is required, section 205 of the Unfunded Mandates Act also requires an agency to identify and consider a reasonable number of regulatory alternatives before promulgating a rule. The OCC has determined that this final rule will not result in expenditures by State, local, and tribal governments, or by the private sector, of \$100 million or more in any one year. Accordingly, this rulemaking is not subject to section 202 of the Unfunded Mandates Act.

#### *Executive Order 13132*

Executive Order 13132, entitled "Federalism" (Order), requires Federal agencies, including the OCC, to certify their compliance with that Order when they transmit to the Office of Management and Budget any draft final regulation that has Federalism implications. Under the Order, a regulation has Federalism implications if it has "substantial direct effects on the States, on the relationship between the national government and the States, or on the distribution of power and responsibilities among the various levels of government." In the case of a regulation that has Federalism implications and that preempts state law, the Order imposes certain consultation requirements with state and local officials; requires publication in the preamble of a Federalism summary impact statement; and requires the OCC to make available to the Director of the Office of Management and Budget any written communications submitted by state and local officials. By the terms of the Order, these requirements apply to the extent that they are practicable and permitted by law and, to that extent, must be satisfied before the OCC promulgates a final regulation.

In the proposal, we noted that the regulation may have Federalism implications. Therefore, in formulating the proposal and the final rule, the OCC has adhered to the fundamental Federalism principles and the Federalism policymaking criteria. Moreover, the OCC has satisfied the requirements set forth in the Order for regulations that have Federalism implications and preempt state law. The steps taken to comply with these requirements are set forth below.

*Consultation.* The Order requires that, to the extent practicable and permitted by law, no agency shall promulgate any

regulation that has Federalism implications and that preempts state law unless, prior to the formal promulgation of the regulation, the agency consults with state and local officials early in the process of developing the proposal. We have consulted with state and local officials on the issues addressed herein through the rulemaking process. Following the publication of the proposal, representatives from the Conference of State Bank Supervisors (CSBS) met with the OCC to clarify their understanding of the proposal and, subsequently, the CSBS submitted a detailed comment letter regarding the proposal. As mentioned previously, additional comments were also submitted on the proposal by other state and local officials and state banking regulators. Pursuant to the Order, we will make these comments available to the Director of the OMB. Subsequent, public statements by representatives of the CSBS have restated their concerns, and CSBS representatives have further discussed these concerns with the OCC on several additional occasions.

In addition to consultation, the Order requires a Federalism summary impact statement that addresses the following:

*Nature of concerns expressed.* The Order requires a summary of the nature of the concerns of the state and local officials and the agency's position supporting the need to issue the regulation. The nature of the state and local official commenters' concerns and the OCC's position supporting the need to issue the regulation are set forth in the preamble, but may be summarized as follows. Broadly speaking, the states disagree with our interpretation of the applicable law, they are concerned about the impact the rule will have on the dual banking system, and they are concerned about the ability of the OCC to protect consumers adequately.

*Extent to which the concerns have been addressed.* The Order requires a statement of the extent to which the concerns of state and local officials have been met.

a. There is fundamental disagreement between state and local officials and the OCC regarding preemption in the national bank context. For the reasons set forth in the materials that precede this Federalism impact statement, we believe that this final rule is necessary to enable national banks to operate to the full extent of their powers under Federal law, and without interference from inconsistent state laws; consistent with the national character of the national banks; and in furtherance of their safe and sound operations. We also believe that this final rule has ample

support in statute and judicial precedent. The concerns of the state and local officials could only be fully met if the OCC were to take a position that is contrary to Federal law and judicial precedent. Nevertheless, to respond to some of the issues raised, the language in this final regulation has been refined, and this preamble further explains the standards used to determine when preemption occurs and the criteria for when state laws generally would *not* be preempted.

b. Similarly, we fundamentally disagree with the state and local officials about whether this final rule will undermine the dual banking system. As discussed in the OCC's visitorial powers rulemaking also published today in the **Federal Register**, differences in national and state bank powers and in the supervision and regulation of national and state banks are not inconsistent with the dual banking system; rather, they are the defining characteristics of it. The dual banking system is universally understood to refer to the chartering and supervision of state-chartered banks by state authorities and the chartering and supervision of national banks by Federal authority, the OCC. Thus, we believe that the final rule preserves, rather than undermines, the dual banking system.

c. Finally, we stand ready to work with the states in the enforcement of applicable laws. The OCC has extended invitations to state Attorneys General and state banking departments to enter into discussions that would lead to a memorandum of understanding about the handling of consumer complaints and the pursuit of remedies, and we remain eager to do so. Moreover, as discussed in the preamble, we believe the OCC has the resources to enforce applicable laws, as is evidenced by the enforcement actions that have generated hundreds of millions of dollars for consumers in restitution, that have required national banks to disassociate themselves from payday lenders, and that have ordered national banks to stop abusive practices. Thus, the OCC has ample legal authority and resources to ensure that consumers are adequately protected.

#### **List of Subjects**

##### *12 CFR Part 7*

Credit, Insurance, Investments, National banks, Reporting and recordkeeping requirements, Securities, Surety bonds.

##### *12 CFR Part 34*

Mortgages, National banks, Real estate appraisals, Real estate lending

standards, Reporting and recordkeeping requirements.

#### Authority and Issuance

■ For the reasons set forth in the preamble, parts 7 and 34 of chapter I of title 12 of the Code of Federal Regulations are amended as follows:

### PART 7—BANK ACTIVITIES AND OPERATIONS

■ 1. The authority citation for part 7 is revised to read as follows:

**Authority:** 12 U.S.C. 1 *et seq.*, 71, 71a, 92, 92a, 93, 93a, 481, 484, and 1818.

#### Subpart D—Preemption

■ 2. A new § 7.4007 is added to read as follows:

##### § 7.4007 Deposit-taking.

(a) *Authority of national banks.* A national bank may receive deposits and engage in any activity incidental to receiving deposits, including issuing evidence of accounts, subject to such terms, conditions, and limitations prescribed by the Comptroller of the Currency and any other applicable Federal law.

(b) *Applicability of state law.* (1) Except where made applicable by Federal law, state laws that obstruct, impair, or condition a national bank's ability to fully exercise its Federally authorized deposit-taking powers are not applicable to national banks.

(2) A national bank may exercise its deposit-taking powers without regard to state law limitations concerning:

(i) Abandoned and dormant accounts;<sup>3</sup>

(ii) Checking accounts;

(iii) Disclosure requirements;

(iv) Funds availability;

(v) Savings account orders of withdrawal;

(vi) State licensing or registration requirements (except for purposes of service of process); and

(vii) Special purpose savings services;<sup>4</sup>

(c) *State laws that are not preempted.* State laws on the following subjects are not inconsistent with the deposit-taking powers of national banks and apply to national banks to the extent that they only incidentally affect the exercise of national banks' deposit-taking powers:

- (1) Contracts;
- (2) Torts;
- (3) Criminal law;<sup>5</sup>
- (4) Rights to collect debts;
- (5) Acquisition and transfer of property;

- (6) Taxation;
- (7) Zoning; and

(8) Any other law the effect of which the OCC determines to be incidental to the deposit-taking operations of national banks or otherwise consistent with the powers set out in paragraph (a) of this section.

■ 3. A new § 7.4008 is added to read as follows:

##### § 7.4008 Lending.

(a) *Authority of national banks.* A national bank may make, sell, purchase, participate in, or otherwise deal in loans and interests in loans that are not secured by liens on, or interests in, real estate, subject to such terms, conditions, and limitations prescribed by the Comptroller of the Currency and any other applicable Federal law.

(b) *Standards for loans.* A national bank shall not make a consumer loan subject to this § 7.4008 based predominantly on the bank's realization of the foreclosure or liquidation value of the borrower's collateral, without regard to the borrower's ability to repay the loan according to its terms. A bank may use any reasonable method to determine a borrower's ability to repay, including, for example, the borrower's current and expected income, current and expected cash flows, net worth, other relevant financial resources, current financial obligations, employment status, credit history, or other relevant factors.

(c) *Unfair and deceptive practices.* A national bank shall not engage in unfair or deceptive practices within the meaning of section 5 of the Federal Trade Commission Act, 15 U.S.C. 45(a)(1), and regulations promulgated thereunder in connection with loans made under this § 7.4008.

(d) *Applicability of state law.* (1) Except where made applicable by Federal law, state laws that obstruct, impair, or condition a national bank's

<sup>5</sup> But see the distinction drawn by the Supreme Court in *Easton v. Iowa*, 188 U.S. 220, 238 (1903) between "crimes defined and punishable at common law or by the general statutes of a state and crimes and offenses cognizable under the authority of the United States." The Court stated that "[u]ndoubtedly a state has the legitimate power to define and punish crimes by general laws applicable to all persons within its jurisdiction \* \* \*. But it is without lawful power to make such special laws applicable to banks organized and operating under the laws of the United States." *Id.* at 239 (holding that Federal law governing the operations of national banks preempted a state criminal law prohibiting insolvent banks from accepting deposits).

ability to fully exercise its Federally authorized non-real estate lending powers are not applicable to national banks.

(2) A national bank may make non-real estate loans without regard to state law limitations concerning:

(i) Licensing, registration (except for purposes of service of process), filings, or reports by creditors;

(ii) The ability of a creditor to require or obtain insurance for collateral or other credit enhancements or risk mitigants, in furtherance of safe and sound banking practices;

(iii) Loan-to-value ratios;

(iv) The terms of credit, including the schedule for repayment of principal and interest, amortization of loans, balance, payments due, minimum payments, or term to maturity of the loan, including the circumstances under which a loan may be called due and payable upon the passage of time or a specified event external to the loan;

(v) Escrow accounts, impound accounts, and similar accounts;

(vi) Security property, including leaseholds;

(vii) Access to, and use of, credit reports;

(viii) Disclosure and advertising, including laws requiring specific statements, information, or other content to be included in credit application forms, credit solicitations, billing statements, credit contracts, or other credit-related documents;

(ix) Disbursements and repayments; and

(x) Rates of interest on loans.<sup>6</sup>

(e) *State laws that are not preempted.* State laws on the following subjects are not inconsistent with the non-real estate lending powers of national banks and apply to national banks to the extent that they only incidentally affect the exercise of national banks' non-real estate lending powers:

(1) Contracts;

(2) Torts;

(3) Criminal law;<sup>7</sup>

(4) Rights to collect debts;

(5) Acquisition and transfer of property;

(6) Taxation;

(7) Zoning; and

<sup>6</sup> The limitations on charges that comprise rates of interest on loans by national banks are determined under Federal law. See 12 U.S.C. 85; 12 CFR 7.4001. State laws purporting to regulate national bank fees and charges that do not constitute interest are addressed in 12 CFR 7.4002.

<sup>7</sup> See *supra* note 5 regarding the distinction drawn by the Supreme Court in *Easton v. Iowa*, 188 U.S. 220, 238 (1903) between "crimes defined and punishable at common law or by the general statutes of a state and crimes and offenses cognizable under the authority of the United States."

<sup>3</sup> This does not apply to state laws of the type upheld by the United States Supreme Court in *Anderson Nat'l Bank v. Lockett*, 321 U.S. 233 (1944), which obligate a national bank to "pay [deposits] to the persons entitled to demand payment according to the law of the state where it does business." *Id.* at 248–249.

<sup>4</sup> State laws purporting to regulate national bank fees and charges are addressed in 12 CFR 7.4002.

(8) Any other law the effect of which the OCC determines to be incidental to the non-real estate lending operations of national banks or otherwise consistent with the powers set out in paragraph (a) of this section.

■ 4. A new § 7.4009 is added to read as follows:

**§ 7.4009 Applicability of state law to national bank operations.**

(a) *Authority of national banks.* A national bank may exercise all powers authorized to it under Federal law, including conducting any activity that is part of, or incidental to, the business of banking, subject to such terms, conditions, and limitations prescribed by the Comptroller of the Currency and any applicable Federal law.

(b) *Applicability of state law.* Except where made applicable by Federal law, state laws that obstruct, impair, or condition a national bank's ability to fully exercise its powers to conduct activities authorized under Federal law do not apply to national banks.

(c) *Applicability of state law to particular national bank activities.* (1) The provisions of this section govern with respect to any national bank power or aspect of a national bank's operations that is not covered by another OCC regulation specifically addressing the applicability of state law.

(2) State laws on the following subjects are not inconsistent with the powers of national banks and apply to national banks to the extent that they only incidentally affect the exercise of national bank powers:

- (i) Contracts;
- (ii) Torts;
- (iii) Criminal law<sup>8</sup>
- (iv) Rights to collect debts;
- (v) Acquisition and transfer of property;
- (vi) Taxation;
- (vii) Zoning; and
- (viii) Any other law the effect of which the OCC determines to be incidental to the exercise of national bank powers or otherwise consistent with the powers set out in paragraph (a) of this section.

**PART 34—REAL ESTATE LENDING AND APPRAISALS**

**Subpart A—General**

■ 5. The authority citation for part 34 continues to read as follows:

**Authority:** 12 U.S.C. 1 *et seq.*, 29, 93a, 371, 1701j–3, 1828(o), and 3331 *et seq.*

■ 6. In § 34.3, the existing text is designated as paragraph (a), and new

paragraphs (b) and (c) are added to read as follows:

**§ 34.3 General rule.**

\* \* \* \* \*

(b) A national bank shall not make a consumer loan subject to this subpart based predominantly on the bank's realization of the foreclosure or liquidation value of the borrower's collateral, without regard to the borrower's ability to repay the loan according to its terms. A bank may use any reasonable method to determine a borrower's ability to repay, including, for example, the borrower's current and expected income, current and expected cash flows, net worth, other relevant financial resources, current financial obligations, employment status, credit history, or other relevant factors.

(c) A national bank shall not engage in unfair or deceptive practices within the meaning of section 5 of the Federal Trade Commission Act, 15 U.S.C. 45(a)(1), and regulations promulgated thereunder in connection with loans made under this part.

■ 7. Section 34.4 is revised to read as follows:

**§ 34.4 Applicability of state law.**

(a) Except where made applicable by Federal law, state laws that obstruct, impair, or condition a national bank's ability to fully exercise its Federally authorized real estate lending powers do not apply to national banks. Specifically, a national bank may make real estate loans under 12 U.S.C. 371 and § 34.3, without regard to state law limitations concerning:

- (1) Licensing, registration (except for purposes of service of process), filings, or reports by creditors;
- (2) The ability of a creditor to require or obtain private mortgage insurance, insurance for other collateral, or other credit enhancements or risk mitigants, in furtherance of safe and sound banking practices;
- (3) Loan-to-value ratios;
- (4) The terms of credit, including schedule for repayment of principal and interest, amortization of loans, balance, payments due, minimum payments, or term to maturity of the loan, including the circumstances under which a loan may be called due and payable upon the passage of time or a specified event external to the loan;
- (5) The aggregate amount of funds that may be loaned upon the security of real estate;
- (6) Escrow accounts, impound accounts, and similar accounts;
- (7) Security property, including leaseholds;

(8) Access to, and use of, credit reports;

(9) Disclosure and advertising, including laws requiring specific statements, information, or other content to be included in credit application forms, credit solicitations, billing statements, credit contracts, or other credit-related documents;

(10) Processing, origination, servicing, sale or purchase of, or investment or participation in, mortgages;

(11) Disbursements and repayments;

(12) Rates of interest on loans;<sup>1</sup>

(13) Due-on-sale clauses except to the extent provided in 12 U.S.C. 1701j–3 and 12 CFR part 591; and

(14) Covenants and restrictions that must be contained in a lease to qualify the leasehold as acceptable security for a real estate loan.

(b) State laws on the following subjects are not inconsistent with the real estate lending powers of national banks and apply to national banks to the extent that they only incidentally affect the exercise of national banks' real estate lending powers:

- (1) Contracts;
- (2) Torts;
- (3) Criminal law;<sup>2</sup>
- (4) Homestead laws specified in 12 U.S.C. 1462a(f);
- (5) Rights to collect debts;
- (6) Acquisition and transfer of real property;
- (7) Taxation;
- (8) Zoning; and
- (9) Any other law the effect of which the OCC determines to be incidental to the real estate lending operations of national banks or otherwise consistent with the powers and purposes set out in § 34.3(a).

(8) Access to, and use of, credit reports;

- (9) Disclosure and advertising, including laws requiring specific statements, information, or other content to be included in credit application forms, credit solicitations, billing statements, credit contracts, or other credit-related documents;
- (10) Processing, origination, servicing, sale or purchase of, or investment or participation in, mortgages;
- (11) Disbursements and repayments;
- (12) Rates of interest on loans;<sup>1</sup>
- (13) Due-on-sale clauses except to the extent provided in 12 U.S.C. 1701j–3 and 12 CFR part 591; and
- (14) Covenants and restrictions that must be contained in a lease to qualify the leasehold as acceptable security for a real estate loan.

(b) State laws on the following subjects are not inconsistent with the real estate lending powers of national banks and apply to national banks to the extent that they only incidentally affect the exercise of national banks' real estate lending powers:

- (1) Contracts;
- (2) Torts;
- (3) Criminal law;<sup>2</sup>
- (4) Homestead laws specified in 12 U.S.C. 1462a(f);
- (5) Rights to collect debts;
- (6) Acquisition and transfer of real property;
- (7) Taxation;
- (8) Zoning; and
- (9) Any other law the effect of which the OCC determines to be incidental to the real estate lending operations of national banks or otherwise consistent with the powers and purposes set out in § 34.3(a).

Dated: January 6, 2004.

**John D. Hawke, Jr.,**

*Comptroller of the Currency.*

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<sup>1</sup> The limitations on charges that comprise rates of interest on loans by national banks are determined under Federal law. See 12 U.S.C. 85 and 1735f–7a; 12 CFR 7.4001. State laws purporting to regulate national bank fees and charges that do not constitute interest are addressed in 12 CFR 7.4002.

<sup>2</sup> But see the distinction drawn by the Supreme Court in *Easton v. Iowa*, 188 U.S. 220, 238 (1903) between “crimes defined and punishable at common law or by the general statutes of a state and crimes and offences cognizable under the authority of the United States.” The Court stated that “[u]ndoubtedly a state has the legitimate power to define and punish crimes by general laws applicable to all persons within its jurisdiction \* \* \*. But it is without lawful power to make such special laws applicable to banks organized and operating under the laws of the United States.” *Id.* at 239 (holding that Federal law governing the operations of national banks preempted a state criminal law prohibiting insolvent banks from accepting deposits).

<sup>8</sup> *Id.*