The OCC, the National Bank Charter, & Current Issues Facing the National Banking System"

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Prepared for the
Financial Services Regulatory Conference
March 17, 2003
Washington, D.C.

Early in *The Tempest*, one of Shakespeare's characters advises that "What's past is prologue;"[1] meaning, in that context, that events of the past provide guidance for a present day course of action. Much the same could be said for many of the most significant issues facing the OCC and national banks today. The mission of the agency, and the essence of the powers and character of the national bank charter, are deeply rooted in the circumstances that gave rise to the creation of both the agency and national banks in 1863. As the OCC celebrates its 140th anniversary this year, that past provides the principles that define the OCC's contemporary role, and the characteristics and legal status of the national bank charter.

Prologue[2]

Banks have never been particularly popular American institutions, and in the early days of this country, banks that operated under a broad grant of national authority may have been most unpopular of all. Thomas Jefferson spoke for many of his time when he said that "banking institutions are more dangerous than standing armies." American history buffs will recall that even George Washington was opposed to an American standing army, so Jefferson's comment was saying quite a lot.

Yet even Jefferson did not believe that the country could afford to dispense with banks altogether. In fact, America needed banks even more than Britain did, for the U.S. was a young, undeveloped, and far-flung country noticeably lacking in the great private accumulations of liquid wealth with which England was blessed. In order to mobilize capital in such a place, banks were essential to create and facilitate the flow of money.

In 1791, at the urging of Alexander Hamilton, the first Secretary of the Treasury, Congress created the First Bank of the United States – America's first venture into the area of central banking. When the Bank's 20-year charter expired, the Bank expired with it. But a crumbling economy led lawmakers five years later to create the Second Bank of the United States, which proved no more popular than the first. And state-chartered banks, of which there were well over a hundred by 1816, took advantage of that unpopularity by encouraging State legislatures to pass a variety of discriminatory laws, hoping to rein in, if not destroy, the sometimes overbearing Second Bank.

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[1] *The Tempest*, II, I, 257.

[2] Special thanks to Jesse Stiller, OCC Special Advisor for Executive Communications, for much of the content of this section.

Maryland's contribution to this State effort was an annual tax of $15,000 levied against the Baltimore branch of the Second Bank of the U.S. When the bank refused to pay, it was successfully sued in State court. In the name of its cashier, J.W. McCulloch, the Second Bank appealed that verdict to the U.S. Supreme Court.

What emerged was one of the landmark judicial decisions in our history. Speaking for a unanimous Supreme Court, Chief Justice Marshall declared constitutional Congress's creation of a national bank and declared unconstitutional Maryland's attempt to weaken it through taxation. On the first point, Marshall elaborated the view of federal power associated with Alexander Hamilton, an expansive view, based on a strong union.

On the second point, regarding Maryland's attack on the Second Bank, Marshall invoked the Supremacy Clause -- paragraph 2 of Article VI -- holding that the Constitution of the United States, and the laws promulgated under it, are the law of the land and carry a presumption of supremacy over the States. "The States," Marshall affirmed, "have no power, by taxation or otherwise, to retard, impede, burden, or in any manner control the operations" of any agency created by lawful exercise of federal authority.

But, the States could still send elected representatives to Washington to accomplish the same end by federal legislation or presidential authority, and under President Andrew Jackson, legislation to extend the life of the Second Bank was vetoed.

With the loss of this centralizing and stabilizing influence, the U.S. banking system stumbled into disarray. Indeed, it was hardly a system at all, because standards and practices varied enormously from State to State. In States like Indiana and New York, new bank organizers were required to have real capital, and their operations were subject to some degree of government supervision. But in many States, banks could organize without a dollar's capital to their name, and supervision was virtually nonexistent. That permitted the shadiest of operators to enter the field -- and dominate it in some States.

The currency of the country consisted of notes issued by those banks, and the practice of issuing bank notes with no or inadequate real assets backing them up became a national scandal, and a huge burden on interstate commerce, which needed a reliable, nationally accepted currency. To keep redemption-minded note-holders at a safe distance, shady bank operators became experts at evasion, moving their hole-in-the-wall offices to frontier backwaters "where only the wildcats roamed." The term "Wildcat banking" has its source in this experience.

Today, we would probably characterize such a situation, where a customer provides value and receives in return an instrument of uncertain and possibly dubious value, as a consumer protection problem. But in the mid-1800's, the lack of uniformity in the value of currency was a great flaw in our banking system before the Civil War, because it gave rise to confusion and uncertainty -- two major obstacles to economic development.

This situation cried out for a remedy, and the Civil War provided the catalyst for a new system to deal with it. The Office of the Comptroller of the Currency was created to charter and supervise a new system of national banks, which would serve as the instruments of a uniform and sound national currency, and help finance the Civil War.

When the Comptroller chartered a new national bank, a portion of the bank's paid-in capital was required to be used to purchase U.S. Treasury securities, which not only filled the Union's coffers, but which were pledged as backing for a new species of circulating notes issued by the banks with the Comptroller's approval. Because these new national banks were to be subject to uniform federal supervision, with capital in the form of government securities, their circulating notes would hold a stable value and could be used, reliably, from State to State. The design of the new national banks thus solved the safety and soundness problem that plagued many State banks, and at the same time, addressed the fraud and deception that resulted from the issuance of notes of dubious value by many State banks.

But, in creating a system of national banks, Congress was not only aiming to solve an immediate problem. By establishing a national banking system, and creating the Office of the Comptroller of the Currency to oversee it, Congress also erected a framework for change, growth, integrity and expansion of the business of banking, under the Comptroller's supervision, designed to support and foster the Nation's economic development. As Carter Golembe put it in one of his famous commentaries: "The responsibility of the Office carries with it, in addition to safety and soundness considerations, the need for the Comptroller to assure that the national banking system is healthy, vigorous, competitive, profitable, innovative, and capable of serving in the best possible manner the banking needs of its customers."

This history -- my prologue – helps to explain three defining characteristics of national banks and the national banking system, which are so important in the financial marketplace today: 1) the dynamic powers of national banks to engage in the business of banking, as that business evolves over time; 2) the role and responsibilities of the OCC as the charterer, supervisor and regulator of national banks, and 3) the National Bank Act's preemption of State laws that would seek to direct or control activities of national banks that are authorized under Federal law.

The Powers of National Banks

The long-range goals of Congress for the national banking system – supporting a stable national currency, financing commerce, acting as private depositories, and generally supporting the Nation's economic growth and development -- required a type of bank that was not just safe and sound, but whose powers were dynamic and capable of evolving, so that national banks could perform their intended roles, well beyond the aftermath of the Civil War. Key to these powers is language set forth at 12 U.S.C. § 24 (Seventh), which provides that national banks are authorized to exercise "all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin and bullion; by loaning money on personal security; and by obtaining, issuing, and circulating notes…."

Congress had modeled this authority on the bank charter authorized by the New York Free Banking Act; a type of charter that the New York courts explicitly had found to possess flexible and adaptive powers. Shortly before enactment of the National Bank Act, the New York Court of Appeals described the dynamic nature of the New York bank charter, stating that "[t]he implied powers [of a bank] exist by virtue of the grant [to do the banking business] and are not enumerated and defined; because no human sagacity can foresee what implied powers may in the progress of time, the discovery and perfection of better methods of business, and the ever-varying attitude of human relations, be required to give effect to the express powers.[3]

The specifications of certain banking activities that were contained in the New York banking laws, (and subsequently copied into the National Bank Act), were "eminently useful," but "not indispensable," according to the court in that case. Based on this lineage, in construing the National Bank Act the OCC typically looks to the objectives in addition to simply the mechanics of the Act, approaching the statute, as one commentator put it, as "an architect's drawing and not a set of specifications."[4] As a result, the powers of national banks to engage in the business and banking and activities that are "incidental" thereto have been continually updated and consistently interpreted by the OCC -- and accepted by the courts -- as evolutionary; capable of developing and adjusting as needed to support the evolving financial and economic needs of the Nation.

Any doubt concerning this characterization of the powers of national banks was settled with the Supreme Court's decision in NationsBank v. Variable Annuity Life Insurance Co. (VALIC) in which the Court expressly held that the "business of banking" is not limited to the enumerated powers in § 24(Seventh) and that the Comptroller has discretion to authorize activities beyond those specifically enumerated in the statute.[5] In the same decision, the Court also reiterated a previous admonition that the Comptroller's determinations regarding the scope of permissible national bank activities pursuant to this authority should be accorded great deference, stating emphatically that "it is settled that courts should give great weight to any reasonable construction of a regulatory statute adopted by the agency charged with enforcement of that statute. The Comptroller of the Currency is charged with the enforcement of banking laws to an extent that warrants the invocation of this principle with respect to his deliberative conclusions as to the meaning of these laws."[6]

So, today, national banks operate pursuant to federal authority contained in a federally-granted charter; that authority is recognized as flexible and adaptable to serve changing customer and business needs and desires, and the OCC is uniquely authorized to define and refine the content of the business of banking in order to enable national banks to best serve those changing needs on a safe and sound basis.

The Role and Responsibilities of the OCC As Supervisor of National Banks

The OCC's authority to regulate, supervise and examine national banks is extensive, and in many respects, exclusive. The latter feature is not always popular with State authorities, but the scope of the OCC's exclusive "visitorial" power is firmly grounded in the National Bank Act and its history.

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[3] Curtis v. Leavitt, 15 N.Y. 9 (1857).

[4] Harfield, "The National Bank Act and Foreign Trade Practices," 61 Harv. L. Rev. 782 (1948).

[5] NationsBank of North Carolina v. Variable Annuity Life Insurance Co., 513 U.S. 251.

[6] Clarke v. Securities Industry Assn., 479 U.S. 388, 403-404 (1987) (quoting Investment Company Institute v. Camp, 401 U.S. 617, 626-627.

At the beginning of the national banking system, both proponents and opponents of the new system expected that it would supersede the existing system of State banks.[7] Given this anticipated impact on State banks and the resulting diminution of control by the States over banking in general,[8] proponents of the national banking system were concerned that States would attempt to undermine it. Remarks of Senator Sumner, addressing the prospect of state taxation of national banks, illustrate the sentiment of many legislators of the time. He said, "[c]learly, the bank must not be subjected to any local government, State or municipal; it must be kept absolutely and exclusively under that Government from which it derives its functions." [9]

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[7] Representative Samuel Hooper, who reported the bill to the House, stated in support of the legislation that one of its purposes was "to render the law [Currency Act] so perfect that the State banks may be induced to organize under it, in preference to continuing under their State charters." Cong. Globe, 38th Cong. 1st Sess. 1256 (March 23, 1864). While he did not believe that the legislation was necessarily harmful to the state bank system, he did "look upon the system of State banks as having outlived its usefulness . . . ." Id. Opponents of the legislation believed that it was intended to "take from the States . . . all authority whatsoever over their own State banks, and to vest that authority . . . in Washington . . . ." Cong. Globe, 38th Cong., 1st Sess. 1267 (March 24, 1864) (statement of Rep. Brooks). Rep. Brooks made that statement to support the idea that the legislation was intended to transfer control over banking from the states to the federal government. Given that the legislation's objective was to replace state banks with national banks, its passage would, in Rep. Brooks' opinion, mean that there would be no state banks left over which the states would have authority. Thus, by observing that the legislation was intended to take authority over state banks from the states, Rep. Brooks was not suggesting that the Federal government would have authority over state banks; rather, he was explaining the bill in a context that assumed the demise of state banks. Rep. Pruyn opposed the bill stating that the legislation would "be the greatest blow yet inflicted upon the States . . . ." Cong. Globe, 38th Cong., 1st Sess. 1271 (March 24, 1864). See also John Wilson Million, The Debate on the National Bank Act of 1863, 2 Journal of Political Economy 251, 267 (1893-94) regarding the Currency Act. ("Nothing can be more obvious from the debates than that the national system was to supersede the system of state banks.").

[8] See, e.g., Tiffany v. National Bank of the State of Missouri, 85 U.S. 409, 412-413 (1874) ("It cannot be doubted, in view of the purpose of Congress in providing for the organization of national banking associations, that it was intended to give them a firm footing in the different states where they might be located. It was expected they would come into competition with state banks, and it was intended to give them at least equal advantages in such competition . . . . National banks have been national favorites. They were established for the purpose, in part, of providing a currency for the whole country, and in part to create a market for the loans of the general government. It could not have been intended, therefore, to expose them to the hazard of unfriendly legislation by the states, or to ruinous competition with state banks."). See also B. Hammond, Banks and Politics in America from the Revolution to the Civil War, 725-34 (1957); P. Studenski & H. Krooss, Financial History of the United States, 155 (1st ed. 1952).

[9] Cong. Globe, 38th Cong., 1st Sess., at 1893 (April 27, 1864). See also Anderson v. H&R Block, __ F.3d __, 2002 U.S. App. LEXIS 5978, at 15-16 (No 01-11863, April 3, 2002) ("congressional debates amply demonstrate Congress's desire to protect national banks from state legislation . . . .").

The allocation of any supervisory responsibility for the new national banking system to the States would have been inconsistent with this need to protect national banks from State interference. Congress, accordingly, established a Federal supervisory regime and vested responsibility to carry it out in the newly created OCC. Congress granted the OCC the broad authority "to make a thorough examination of all the affairs of [a national] bank,"[10] and solidified this Federal supervisory authority by vesting the OCC with exclusive "visitorial" powers over national banks. These provisions assured, among other things, that the OCC would have comprehensive authority to examine all the affairs of a national bank and protected national banks from potential State hostility by establishing that the authority to examine national banks is vested only in the OCC, unless otherwise provided by federal law.[11]

Courts have consistently recognized the distinct status of the national banking system and the limits placed on state involvement in national bank supervision and regulation by the National Bank Act. The Supreme Court stated in one of the first cases to address the role of the national banking system that "[t]he national banks organized under the [National Bank Act] are instruments designed to be used to aid the government in the administration of an important branch of the public service. They are means appropriate to that end."[12]

Subsequent opinions of the Court have been equally clear about national banks' distinct role and status.[13] For example, in Guthrie v. Harkness,[14] the Supreme Court stated that "Congress had in mind, in passing this section [section 484] that in other sections of the law it had made full and complete provision for investigation by the Comptroller of the Currency and examiners appointed by him, and, authorizing the appointment of a receiver, to take possession of the business with a view to winding up the affairs of the bank. It was the intention that this statute should contain a full code of provisions upon the subject, and that no State law or enactment should undertake to exercise the right of visitation over a national corporation. Except in so far as such corporation was liable to control in the courts of justice, this act was to be the full measure of visitorial power".[15]

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[10] Act of June 3, 1864, c. 106, § 54, 13 Stat. 116, codified at 12 U.S.C. 481.

[11] Writing shortly after the Currency Act and National Bank Act were enacted, then-Secretary of the Treasury, and formerly the first Comptroller of the Currency, Hugh McCulloch observed that "Congress has assumed entire control of the currency of the country, and, to a very considerable extent, of its banking interests, prohibiting the interference of State governments . . . ." Cong. Globe, 39th Cong., 1st Sess., Misc. Doc. No. 100, at 2 (April 23, 1866).

[12] Farmers' and Mechanics' National Bank v. Dearing, 91 U.S. 29, 33 (1875).

[13] See Marquette National Bank v. First of Omaha Service Corp., 439 U.S. 299, 314-315 (1978) ("Close examination of the National Bank Act of 1864, its legislative history, and its historical context makes clear that, . . . Congress intended to facilitate . . . a 'national banking system'." (citation omitted)); Franklin National Bank of Franklin Square v. New York, 347 U.S. 373, 375 (1954) ("The United States has set up a system of national banks as Federal instrumentalities to perform various functions such as providing circulating medium and government credit, as well as financing commerce and acting as private depositories."); Davis v. Elmira Savings Bank, 161 U.S. 275, 283 (1896) ("National banks are instrumentalities of the Federal government, created for a public purpose, and as such necessarily subject to the paramount authority of the United States.").

[14] 199 U.S. 148 (1905).

The Supreme Court also has recognized the clear intent on the part of Congress to limit the authority of states over national banks precisely so that the nationwide system of banking that was created in the Currency Act could develop and flourish. For instance, in Easton v. Iowa,[16] the Court stated that the National Bank Act "has in view the erection of a system extending throughout the country, and independent, so far as the powers conferred are concerned, of state legislation which, if permitted to be applicable, might impose limitations and restrictions as various and as numerous as the States. * * * If [the States] had such power it would have to be exercised and limited by their own discretion, and confusion would necessarily result from control possessed and exercised by two independent authorities.[17]

The Court in Farmers' and Mechanics' Bank, similarly found that "States can exercise no control over [national banks] nor in any wise affect their operation, except in so far as Congress may see proper to permit." Any thing beyond this is "an abuse, because it is the usurpation of power which a single State cannot give."[18].

Consistent with the need for a uniform system of laws and uniform supervision that would foster the nationwide banking system, courts have interpreted the OCC's visitorial powers expansively. The Supreme Court in Guthrie noted that the term "visitorial" as used in section 484 derives from English common law, which used the term "visitation" to refer to the act of a superintending officer who visits a corporation to examine its manner of conducting business and enforce observance of the laws and regulations (citing First National Bank of Youngstown v. Hughes[19]).[20] "Visitors" of corporations "have power to keep them within the legitimate sphere of their operations, and to correct all abuses of authority, and to nullify all irregular proceedings." The Guthrie Court also specifically noted that visitorial powers include bringing "judicial proceedings" against a corporation to enforce compliance with applicable law.[21] Thus, section 484 establishes the OCC as the exclusive regulator of the business of national banks, except where otherwise provided by Federal law.

Congress recently affirmed the OCC's exclusive visitorial powers with respect to national banks operating on an interstate basis in the Riegle-Neal Interstate Banking Act of 1994 (Riegle-Neal).[22] Although Riegle-Neal makes interstate branches of national banks subject to specified

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[15] Id. at 159.

[16] 188 U.S. 220 (1903).

[17] Id. at 229, 231-232 (emphasis added).

[18] Farmers' and Mechanics' Bank, 91 U.S. at 34 (citation omitted).

[19] 6 F. 737, 740 (6th Cir. 1881), appeal dismissed, 106 U.S. 523 (1883).

[20] Guthrie, 199 U.S. at 158. See also Peoples Bank v. Williams, 449 F. Supp. 254, 259 (W. D. Va. 1978) (visitorial powers involve the exercise of the right of inspection, superintendence, direction, or regulation over a bank's affairs).

[21] Enforcement through judicial proceedings was the most common—and perhaps exclusive—means of exercising the visitorial power to enforce compliance with applicable law at the time section 484 was enacted into law. Administrative actions were not widely used until well into the 20th century. Thus, by vesting the OCC with exclusive visitorial power, section 484 vests the OCC with the exclusive authority to enforce, whether through judicial or administrative proceedings.

[22] Pub. L. 103-328, 108 Stat. 2338 (Sept. 29, 1994).

types of laws of a "host" State in which the bank has an interstate branch (except when Federal law preempts the application of such State laws to national banks), the statute then makes clear that even where the State law is applicable, authority to enforce the law is vested in the OCC.[23]

Federal Preemption of State Laws Under the National Bank Act

The OCC's exclusive visitorial authority complements principles of Federal preemption, to accomplish the objectives of the National Bank Act. Again, the subject of preemption may not be popular in some quarters, but it flows directly from the Supremacy Clause of the United States Constitution,[24] which provides that Federal law prevails over any conflicting State law, and has long been recognized with respect to authority granted national banks under the National Bank Act. An extensive body of judicial precedent has developed over the 140 years of existence of the national banking system, explaining and defining the standards of Federal preemption of State laws as applied to national banks.[25] Together, Federal preemption and the

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[23] See 12 U.S.C. 36(f)(1)(B) ("The provisions of any State law to which a branch of a national bank is subject under this paragraph shall be enforced, with respect to such branch, by the Comptroller of the Currency.").

[24] U.S. Const. Art. VI, cl. 2 ("This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, 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.").

[25] See, e.g., Barnett Bank of Marion County, N.A. v. Nelson, 517 U.S. 25, 26, 32, 33 (1996) ("grants of both enumerated and incidental 'powers' to national banks [are] grants of authority not normally limited by, but rather ordinarily pre-empting, contrary state law." States may not "prevent or significantly interfere with the national bank's exercise of its powers."); Franklin National Bank, 347 U.S. at 378-379 (1954) (federal law preempts state law when there is a conflict between the two; "The compact between the states creating the Federal Government resolves them as a matter of supremacy. However wise or needful [the state's] policy, . . . it must give way to contrary federal policy."); Anderson National Bank v. Luckett, 321 U.S. 233, 248, 252 (1944) (state law may not "infringe the national banking laws or impose an undue burden on the performance of the banks' functions" or "unlawful[ly] encroac[h] on the rights and privileges of national banks"); First National Bank v. Missouri, 263 U.S. 640, 656 (1924) (Federal law preempts state laws that "interfere with the purposes of [national banks'] creation, tend to impair or destroy their efficiency as federal agencies or conflict with the paramount law of the United States."); First National Bank of San Jose v. California, 262 U.S. 366, 368-369 (1923) ("[National banks] are instrumentalities of the federal government. * * * [A]ny attempt by a state to define their duties or control the conduct of their affairs is void, whenever it conflicts with the laws of the United Sates or frustrates the purposes of the national legislation, or impairs the efficiency of the bank to discharge the duties for which it was created."); 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 bank functions); First National Bank of Louisville v. Commonwealth of Kentucky, 76 U.S. (9 Wall.) 353, 362-63 (1870) (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"); Association of Banks in Insurance, Inc. v. Duryee, 270 F.3d

OCC's exclusive visitorial authority are defining characteristics of the national bank charter, and constitute one of the essential distinctions between the national banking system and the system of State-chartered and State-regulated banks that comprise the other half of our "dual banking system."

As described above, Congress established the national banking system in 1863 as a means of achieving the economic policy objectives of the United States, including furnishing a stable and reliable national currency through national bank circulating notes, and promoting the nationwide availability of private credit and sound banking services vital to economic development and opportunity though soundly operated and rigorously supervised banks. With the National Bank Act, Congress built a banking system intended to be nationwide in scope, built upon banks whose powers were intended to be uniform, established under Federal law, regardless of where in the nation they were doing business. As the Supreme Court noted in Deitrick, Receiver v. Greaney,[26] "[t]he National Bank Act constitutes 'by itself a complete system for the establishment and government of National Banks.'" In an earlier case, the Supreme Court stated that "[n]ational banks are instrumentalities of the federal government, created for a public purpose, and as such necessarily subject to the paramount authority of the United States. It follows that an attempt, by a State, to define their duties or control the conduct of their affairs is absolutely void, wherever such attempted exercise of authority expressly conflicts with the laws of the United States, and either frustrates the purpose of the national legislation or impairs the efficiency of these agencies of the Federal government to discharge the duties, for the performance of which they were created."[27]

This independence from State direction and control both recognizes the essentially federal character is national banks and protects them from conflicting local laws that may undermine the uniform, nationwide character of the national banking system. Indeed, the Supreme Court has consistently held that subjecting national banks' exercise of their Federally authorized powers to State regulation or supervision would be inconsistent with the system that Congress designed.[28] The Court also has recognized that because national banks are Federal creations, State law aimed at regulating national banks and their activities applies to national banks only when Congress directs that result,[29] and "the States can exercise no control over them, nor in any wise affect their operation, except in so far as Congress may see proper to permit."[30]

397, 403-404 (6th Cir. 2001) ("The Supremacy Clause 'invalidates state laws that "interfere with, or are contrary to," federal law.' * * * A state law also is pre-empted if it interferes with the methods by which the federal statute was designed to reach th[at] goal.") (citations omitted).

[26] 309 U.S. 190, 194 (1939).

[27] Davis, 161 U.S. at 283.

[28] See, e.g., Marquette Nat. Bank of Minneapolis, 439 U.S. at 314-315 ("Congress intended to facilitate a 'national banking system.'"); First National Bank of San Jose, 262 U.S. 366, 369 (1923) (national banks are instrumentalities of the Federal government; "any attempt by a State to define their duties or control the conduct of their affairs is void, whenever it conflicts with the laws of the United States or frustrates the purpose of national legislation or impairs the efficiency of the bank to discharge the duties for which it was created.").

[29] Of course, Congress may specifically require the application of state law to national banks for certain purposes. See, e.g., 12 U.S.C. 92a(a) (the extent of a national bank's fiduciary powers is determined by reference to the law of the state where the national bank is located).

The Court's decisions also have agreed that Congress was concerned not just with the application of certain States' laws to individual national banks but also with the application of multiple states' standards, which would undermine the uniform, national character of the powers of national banks throughout the system. This point was highlighted by the Supreme Court in Talbott v. Silver Bow Country Commissioners where the Court stressed that the "entire body of the Statute respecting national banks emphasize that which the character of the system implies – an intent to create a national banking system co-extensive with the territorial limits of the United States, and with uniform operation within those limits…."[31] A similar point was made by the Court in the Easton case, which stressed that the national banking system was "a system extending throughout the country, and independent, so far as the powers conferred are concerned, of state legislation which, if permitted to be applicable, might impose limitations and restrictions as various and as numerous as the States.[32]

This Federal character has consistently informed the decisions of the Supreme Court when the Court has considered whether particular State laws apply to national banks. In a recent instance in which the Supreme Court had occasion to review the Federal constitutional foundations of the national banking system, the Court concluded that, because of the Federal status and purpose of national banks, national bank powers are not normally limited by State law.[33]

In sum, operating under a broad and potent grant of enumerated powers and such "incidental powers as shall be necessary to carry on the business of banking," national banks were designed from the outset to carry on their business under uniform federally-granted powers, uniform federal supervision, and uniform, federally-set standards.

While this means that the national banking system and the State banking system are distinct -- indeed that difference is the essence of the dual banking system that we highly value today -- the distinct character of the national banking system definitely does *not* mean that national banks operate with lesser standards or less rigorous oversight than generally applicable to State banks. While State laws necessarily will vary State-by-State, national banks are subject

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Congress may also, more generally, establish standards that govern when state law will apply to national banks' activities. See, e.g., 15 U.S.C. 6701 (codification of section 104 of the Gramm-Leach-Bliley Act, which establishes standards for determining the applicability of state law to different types of activities conducted by national banks, other insured depository institutions, and their affiliates). In such cases, the OCC applies the law or the standards that Congress has required or established.

[30] Farmers' & Mechanics' National Bank, 91 U.S. at 33-34.

[31] Talbott v. Silver Bow County Commissioners, 139 U.S. 438, 443 (1891).

[32] Easton, 188 U.S. at 229, 231-232 (emphasis added).

[33] Barnett Bank of Marion County, N.A. v. Nelson, 517 U.S. 25, 32 (1996) (the history of the legal concept of national bank powers "is one of interpreting grants of both enumerated and incidental 'powers' to national banks as grants of authority not normally limited by, but rather ordinarily pre-empting, contrary state law.").

to rigorous standards and supervision, administered from the Federal level, that applies uniformly to their business, wherever and in whatever form, they conduct it.

The OCC thus bears a heavy responsibility as administrator of the national banking system. The national banking system portion of the dual banking system is designed and premised on the OCC carrying out *multiple* responsibilities that trace to the agency's origins: ensuring the safety and soundness of the national banking system, overseeing the standards by which national banks operate, and assuring that national banks are playing an appropriate role in the national economy. In this mix, the safety and soundness of national banks is of obvious importance, but so too is the fairness and integrity national banks display in conducting their business. As Judge Posner of the Seventh Circuit observed in Central National Bank of Mattoon v. U.S. Dept of Treasury, "[national] banks are [the Comptroller's] wards, and his only wards; if they fail in droves, he will be blamed."[34] And so too is the Comptroller responsible if national banks commit modern-day versions of the customer frauds and deception that plagued the pre-Civil War banking scene. And so too will he be criticized if national banks fail to provide products and services that support a healthy, stable and growing economy.

The OCC's Place in the Dual Banking System and the Tripartite Banking Agency Regulatory System[35]

The OCC carries out these duties from a somewhat unusual status within the Federal government. The original decision to create the OCC as an *independent* agency was a landmark step, and it was one that reflected Congress's understanding of the importance of bank supervision in the Nation's overall economic scheme. While formally a "bureau" of the Treasury Department – indeed, until the 1970s, the Comptroller's offices were actually housed within the main Treasury building in Washington -- the OCC has always enjoyed considerable operational autonomy. Although appointed by the President with Senate confirmation, the President cannot remove the Comptroller before the expiration of the statutory five-year term without providing to the Senate in writing a statement of his reasons for doing so. Wisely, many Administrations have recognized that sound supervision and regulation of the banking system is a responsibility that should not be politicized.

Today, supervision of the U.S. banking industry is split between the OCC for national banks, and the Federal Reserve and the FDIC, dividing up Federal-level supervision of State banks. As already mentioned, at the time of creation of the national banking system, most in Congress apparently hoped for or at least anticipated the elimination of State-chartered banks and believed that the offer of easy conversion to the national charter would provide sufficient incentive for state banking to liquidate itself. But the lagging pace of voluntary conversions led Congress to adopt the Marshall dictum so nicely expressed in the McCulloch case -- "the power to tax is the power to destroy." It imposed a "death tax" on the notes of State banks, a tax that Congressional backers promised would be every bit as effective in driving out State banks as an outright ban, which was also considered.

They were wrong. State banking was able to adapt simply by substituting deposit-taking for note-issuing, and by taking advantage of State regulations deliberately tailored to permit them

[34] 912 F 2.2d 897, 905 (7th Cir. 1990).
[35] Thanks again to Jesse Stiller for much of the content of this section.

to engage in many activities deemed too risky for national banks. The dual banking system was thus born. Reflecting the country's basic ambivalence about banking and the use of national power, a less confrontational Congress then reconciled itself over time to a dual banking system rather than a unified one, embracing a more benign view of State banking as a legitimate expression of state sovereignty and a source of salutary competition for national banks.

Dual banking made for a complicated regulatory system that would soon grow more complicated. Today we entrust the Federal Reserve and the Federal Deposit Insurance Corporation with significant responsibilities for State bank supervision. State-chartered banks, in addition to their State supervisors, each have one primary federal bank supervisor: the FDIC if it's a State-chartered bank that is not a member of the Federal Reserve system (membership is optional for all State banks and mandatory for most OCC-supervised national banks), and the Federal Reserve if the State bank is a Fed member.

We are sometimes asked to explain why this complicated regulatory structure arose – and why we have not attempted systematically to simplify it. The question of origins has a relatively straightforward answer and takes us back to a theme from the beginning of these remarks -- Americans' ambivalence toward banking institutions, their suspicion of concentrated political authority and their belief that establishing multiple and competing government bureaucracies would serve to check their ambitions and excesses. Thus, when the Federal Reserve System was created in 1914 – becoming the second federal agency with a bank supervisory mission – Congress simply layered it on top of the existing supervisory structure and parceled supervisory authority between the new Fed and the OCC. The same pattern held in 1933, when the FDIC – the third of the federal banking agencies -- was created.

Why has this system persisted? Perhaps because it has produced some valuable benefits, albeit inadvertently. Competition can be a good thing in the public as well as private sector, and competition among the banking agencies challenges each agency to excel. Our system shows that competition among regulatory agencies can be a force to *enhance* the quality of supervision, and help prevent any one regulator from becoming unduly rigid. As Ken Lewis, Chairman and CEO of Bank of America, said in speech just last week, "[w]e don't always think of competition as a desirable aspect of regulation, but in our industry it has worked well. Healthy competition among the agencies leads to market-inspired innovation…."

Issues of the Day at the OCC

As we celebrate the OCC's 140th anniversary this year, many of the most significant issues facing the OCC and national banks today have their roots in essential characteristics of the national bank charter and the OCC's fundamental responsibilities as administrator of the national banking system.

Preemption and Visitorial Powers. Today, the original design of the national bank charter and national banking system is the source of preemption and visitorial powers issues in connection with many facets of national banks' operations. In recent years, national banks have encountered State and municipal efforts to limit the amount of fees that national banks may charge – such as ATM fess – and have argued in response that such restrictions are preempted under the National Bank Act, since the authority of national banks to do business under Federal law necessarily includes the ability to charge for, and make a profit on the products and services the banks' provide.

Because of the value of being able to operate under uniform national standards, preemption is an important characteristic of the national bank charter, and some non-bank companies, such as payday lenders, have even tried to enter into contracts with national banks whereby the banks would book the payday loans originated through the payday company's facilities, enabling the non-bank company to conduct that aspect of its business through the national charter, and prompting the company then to claim that its activities enjoyed Federal preemption as if it were a national bank. While the OCC has been supportive of national banks when preemption issues arise, it has vigorously opposed such "rent-a-charter" arrangements.

The lending authorities of national banks also have raised preemption issues in connection with State restrictions on the interest rates that national banks may charge, and State limitations on other terms and conditions of extensions of credit by national banks. State and local limitations and restrictions on loan terms contained in "anti-predatory lending" legislation and ordinances have raised preemption questions that the OCC is now considering. At the same time, in order to assure that national banks do not directly or indirectly participate in abusive or predatory lending practices, the OCC has issued two advisory letters setting out the factors that national banks should take into account in developing polices and standards for their operations to enable them to avoid such practices.

With respect to permissible interest rates, national banks operate under a standard set by Federal law, 12 U.S.C. § 85, which references State law in part, but does not completely defer to it. Twice in the last decade, issues concerning the nature of national banks' authority under that section have been addressed by the Supreme Court. The second instance is a case now pending before the High Court, which will be argued at the end of April.

Closely related to preemption, issues concerning the scope of the OCC's exclusive visitorial powers to supervise and examine national banks have arisen recently in connection with activities national banks conduct through "operating subsidiaries." Under OCC regulations, national bank operating subsidiaries conduct their activities pursuant to the same authorization, terms and conditions that apply to the conduct of those activities by their parent national bank, and are subject to State law, only to the extent of their parent bank. Recent State efforts to examine and regulate mortgage lending "op subs" of national banks has led to litigation that is currently pending in California.

Safety and Soundness and Bank Capital. One of the original objectives of the OCC, establishing a nationwide system of uniformly *sound* banking institutions, is highly relevant to the OCC's supervisory responsibilities today, as the fragile economy continues to present challenges for banks of all sizes. High corporate and consumer leverage and stressed real estate conditions in several markets persist. Credit weakness continues to be centered primarily in corporate portfolios. Yet, improved credit risk management practices, a strong capital base, and diversified earnings have enabled banks to continue to post record earnings despite the adverse credit conditions. Notably, an important component of the earnings diversification that helps enhance national banks' soundness today results from decisions in years past by the OCC to recognize new types of activities and risk management techniques as permissible for national banks as part of the dynamic and evolving nature of the business of banking.

We also continue to refine our supervisory tools. The OCC's "Project Canary" is a groundbreaking initiative to develop computer-based analytical products to support early risk identification and evaluation at national banks. Examiners are integrating "Canary" tools (*i.e.* analytical programs) into their bank supervision. Senior staff will use the "Canary" data to supplement analyses from other sources to develop an ongoing assessment of risk in the national banking system. National banks can even access the Canary analysis of their own institution through the OCC's "National BankNet" internet-based network for national banks.

Credit quality issues resulting from softness in the economy make it particularly important that bank capital is robust. Exactly what constitutes adequate capital – particularly for the larger, internationally active banks, is currently under review on an international basis. The Basel Committee on Banking Supervision, as a forum for international cooperation on bank supervision, is undertaking a major revision of its 1988 Capital Accord. Initiatives in 2003 will include issuance of its latest proposal for public comment. The OCC and other U.S. financial regulators expect to issue an advance notice of propose rulemaking to enable the industry to formally comment of the details of the proposal this Summer.

Privacy and Customer Treatment. The historically-grounded responsibilities of the OCC to oversee the integrity of national banks' operations have a present-day incarnation in the highly visible topic of customer privacy. Today, privacy issues test the balance between customer concerns regarding protection of their non-public information, and banks' desire to utilize such information to manage and control their risk as well as to market financial services.

Privacy-related issues will be in the spotlight in 2003 for several reasons. First is the scheduled expiration, on December 31st of various preemption provisions of the Fair Credit Reporting Act. Second is a set of consumer concerns involving particular privacy-related issues such as identity theft and obnoxious, often dinnertime-disturbing, telemarketing practices. And third may be the generally agreed poor quality of the privacy notices that consumers have received in the last several years pursuant to the new privacy standards contained in the Gramm-Leach-Bliley Act. I say that the quality of the notices is generally agreed to be poor, not because banks have not been trying hard to do a good job. They have. Unfortunately, the requirements of the law are complex, and the agencies, in promulgating the privacy regulations, didn't make them any easier.

OCC Comptroller Jerry Hawke recently took aim at this very issue in a speech he delivered earlier this month. He said that "unreadable, unfathomable, and costly disclosures may be no better – and they're probably worse – than no disclosures at all." He particularly singled out privacy disclosures as an area that could be improved with a layered approach under which consumers would receive a short-form with a few basic facts presented in a simple standardized format. "This disclosure," he said "would provide the basic information – such as the fact that the institution shares the consumer's information with third parties for marketing purposes and that the consumer has the right to block such sharing arrangements. But it would also advise consumers about where to turn – with a phone number or a website address, for example – to obtain a more detailed disclosure with all the information required by the Gramm-Leach-Bliley Act."

In recent years, the OCC also has taken a pioneering position to protect national bank customers against unfair treatment , by using our enforcement authority under section 8 of the Federal Deposit Insurance Act to enforce section 5 of the Federal Trade Commission Act. Section 5 declares unfair and deceptive acts and practices in or affecting commerce to be unlawful, but assigns enforcement of the Act with respect to banks to the Federal banking agencies. We are the only Federal banking agency that, in recent years, has taken enforcement actions to combat unfair and deceptive practices using our cease–and-desist powers.

PATRIOT Act and Sarbanes-Oxley Implementation. The PATRIOT Act has established a formidable arsenal of new standards to combat facilitation of financing of terrorist activities. The OCC has worked extensively as part of inter-agency efforts to adopt implementing regulations, and continues to support the Act's objectives though ongoing supervision of banks' anti-money laundering systems, including terrorist financing controls, and Patriot Act compliance.

We also are implementing, where appropriate, the new requirements of the Sarbanes-Oxley Act. This means some additional rulemaking activity, but even more importantly, Sarbanes-Oxley has heightened sensitivities to issues of operational integrity and sound corporate governance. In addition to what the new law may require, we, and the banking industry, are keeping a closer watch on how banks identify, assess and address activities or transactions that pose reputation risk to the bank.

Another corporate governance issue of particular interest to us is assuring that the reputation and interests of national banks within financial conglomerates are properly respected and maintained. While a typical conglomerate, made up of multiple corporations, might be able to ignore the legal entity distinctions of the companies in the corporate family, when one of the members of the family is a Federally-insured bank, the situation is quite different. Banks enjoy particular government-derived benefits, such a Federal deposit insurance, and they are also subject to special protections, such as the transaction-with-affiliates standards of section 23A and 23B of the Federal Reserve Act. Equally important, banks' reputation for soundness and integrity is a priceless asset. We intend to make sure that it is not tarnished.

Conclusion

This journey from the roots of the national banking system, to the present-day issues we face at the OCC, provides context for how we face those issues – and the future. The national banking system is a unique asset of the U.S. financial system and valuable pillar of our national economy. At the OCC, our responsibilities for overseeing the system, are in fact, multi-dimensional, as Carter Golembe put it – "to assure that national banks are safe and sound, competitive and profitable, and capable of serving in the best possible manner the banking needs of their customers."