Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

December 9, 2003

The Honorable Paul S. Sarbanes
United States Senate
Washington, DC 20510

Dear Senator Sarbanes:

I am writing in response to your letter of November 24, 2003, in which you raise several concerns regarding positions taken by the Office of the Comptroller of the Currency (OCC) with respect to federal preemption of state laws and the ability of state law enforcement officials to exercise visitorial powers with respect to national banks. These issues are complex, and there have been some unfortunate misperceptions of our position in recent public discussions of the issues. Accordingly, I welcome the opportunity to explain our views on the subjects you have noted.

The letter raises several points concerning federal preemption and the standards used by the OCC in addressing national bank preemption issues. While the letter recognizes that "national banks are creatures of federal law and the OCC is the exclusive supervisor of national banks," it then goes on to suggest that "it has been widely accepted by Supreme Court decisions as well as actual practice, that national banks are subject to state laws that do not discriminate against, or significantly burden," their operations. The letter notes the intent of Congress (reflected in the Conference Report on the 1994 Riegle-Neal Act) that "[n]ational banks not be immune from coverage by state laws," cites the 1999 Gramm-Leach-Bliley Act for the proposition that "state laws appl[y] to national banks unless those laws serve to prohibit or significantly interfere with a national bank's congressionally-authorized powers," and asserts that the OCC "now appears to be ignoring both the Supreme Court and Congress by pursing a preemption agenda that would override any state law that has any impact on a national bank." Finally, the letter contends that the OCC is "asserting that it has the right to supplant all state enforcement of state laws of general application that may affect national banks" and their subsidiaries and that our actions "would dramatically alter established preemption standards."

These are important concerns, and it is important that our positions be clearly understood. With the greatest respect, the letter's characterizations of national bank preemption precedents, and of the OCC's positions, are simply not correct. Hopefully, some clarifications in this regard will be responsive to the issues you have raised:

- The Supreme Court's decisions on national bank preemption questions *do not* establish a standard that state law is preempted only when it "discriminates against or significantly

burdens" a national bank's operations. Precedents of the Court have used a variety of formulations of the test for preemption of state laws as applied to national banks, including "interfere with" or "impair [the] efficiency" of national banks in performing their functions, "encroach on the rights and privileges of national banks," impose "local restrictions" on national banks' federal powers, or "condition" national banks' federal authority.

- The OCC *does not* assert that national banks are "immune" from state law and we *do not* contend that "any state law that [would have] any impact on a national bank" is preempted. We apply the tests developed by the Supreme Court, which recognize that national banks are "subject to the laws of the State, and are governed in their daily course of business" by state laws in many respects.

- We *agree* that the Riegle-Neal Act did not change the substantive principles of preemption developed by the Supreme Court. Both the language of the Riegle-Neal Act and its legislative history make clear that these principles were preserved.

- The Gramm-Leach-Bliley Act *did not* revise the standards of preemption under the National Bank Act. The Gramm-Leach-Bliley Act uses the phrase "prevent or significantly interfere" only in the context of preemption of state laws governing certain *insurance activities*. Moreover, it expressly preserves the applicability of the Supreme Court's *Barnett* decision, thus preserving the principles articulated by the Supreme Court in that case.

- With respect to the exercise of visitorial powers and the enforcement of state laws against national banks and their subsidiaries, the OCC *is not* trying to supplant all state enforcement of state laws. Federal law, in existence for 140 years, makes clear that the OCC is the exclusive supervisor of the business of banking conducted by national banks, except where federal law provides otherwise. Pre-existing OCC regulations also provide that operating subsidiaries are subject to the same standards as national banks in this regard because of their unique status as federally-licensed, federally-authorized means by which national banks conduct federally-authorized activities.

- The OCC *is not* dramatically altering established preemption standards. On the contrary, established preemption standards are precisely what we are applying.

In order that our position on these important issues is clearly understood, I have taken the liberty of discussing them in some detail.

National Bank Preemption Standards

The OCC employs principles of federal preemption articulated by the Supreme Court when we evaluate the applicability of state laws to national banks. Precedents of the Court dating back to 1869 have used a variety of formulations in finding that state laws are (or are not) preempted as applied to national banks. For example, the Court has said that state laws would be preempted

where they "interfere with, or impair [national banks'] efficiency" in performing authorized activities, [1] "tend[] to impair or destroy the utility"[2] of, or "destro[y] or hampe[r]" national banks' functions,[3] "expressly conflict with the laws of the United States, or frustrate the purpose for which the national banks were created, or impair their efficiency,"[4] "encroach[] on the rights and privileges of national banks,"[5] impose "local restrictions" on their federal powers,[6] or "prevent or significantly interfere" with or "condition" an authorization, permission or power of a national bank.[7] Clearly, the applicable standard is more than simply whether the state law "discriminates against" or "significantly burdens" the operations of national banks.

It is vital to appreciate that these formulations of the threshold for preemption are a part of the Supreme Court's consistent and repeated recognition of the national banking system as being comprised of federally-established banks operating under uniform, federally-set standards of banking operations. In the earliest years of the national banking system, the Court stressed the character of national banks as federal creations and stated that "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."[8] In a later decision, 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 coextensive with the territorial limits of the United States, and with uniform operation within those limits…."[9] In yet another case, the Court explained more fully that the National Bank Act "has in view the erection of a system extending throughout the country, and independent, so far as 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."[10] "Such being the nature of these national institutions, it must be obvious that their operations cannot be limited or controlled by state legislation…."[11]

More recently, in the *Barnett* case, the Supreme Court had occasion to review the federal constitutional foundations of the national banking system, and reaffirmed that national bank powers are not normally limited by state law.[12] The Court concluded that "where Congress has not expressly conditioned the grant of 'power' upon a grant of state permission, the Court has ordinarily found that no such condition applies."[13] The OCC scrupulously follows these and other applicable precedents when we evaluate a national bank preemption issue.

It is also crucial to understand the practical implications of these issues. National banks find themselves faced with a multiplicity of state and local restrictions and directives that would

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[1] *National Bank v. Commonwealth*, 76 U.S. (9 Wall.) 353, 362 (1869).
[2] *Waite v. Dowley*, 94 U.S. 527, 533 (1876).
[3] *McClellan v. Chipman*, 164 U.S. 347, 358 (1896).
[4] *Id.* at 357.
[5] *Anderson National Bank v. Luckett*, 321 U.S. 233, 252 (1944).
[6] *Franklin National Bank v. New York*, 347 U.S. 373, 378 (1954).
[7] *Barnett Bank of Marion County, N.A. v. Nelson*, 517 U.S. 25, 33-35 (1996).
[8] *Farmers' and Mechanics' National Bank v. Dearing*, 91 U.S. 29, 34 (1875).
[9] *Talbott v. Silver Bow County*, 139 U.S. 438, 443 (1891).
[10] *Easton v. Iowa*, 188 U.S. 220, 229 (1903).
[11] *Id.* at 230.
[12] *Barnett*, at 32.
[13] *Barnett*, at 34.

instruct them – in different ways – on how to conduct their business. They find their federal authority subject to assertions of state-imposed conditions and constraints, and they face uncertainty about the standards applicable to their business and their potential liability for a misstep. OCC becomes involved in addressing preemption issues when national banks seek guidance and clarification of the standards under which they are expected to operate. Our positions on preemption issues have the vital, valuable practical result of clarifying for national banks the standards that govern their banking operations.

Application of State Laws to National Banks

The foregoing does not mean that national banks are immune from state laws, and we do not contend that "any state law that would [have] any impact on a national bank" is preempted. For example, the Supreme Court has observed that national banks are "subject to the laws of the State, and are governed in their daily course of business far more by the laws of the State than of the nation. 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."[14]

But, the Court has also declared that state laws cease to be applicable to national banks "whenever they expressly conflict with the laws of the United States, or frustrate the purpose for which national banks were created, or impair their efficiency to discharge the duties imposed upon them by the law of the United States."[15] The Ninth Circuit recently applied these principles, noting that the types of state laws applicable to national banks include areas such as contracts, debt collection, acquisition and transfer of property, taxation, zoning, and tort law.[16] Thus, our typical approach to national bank preemption questions, consistent with these principles, is to assess whether a state law obstructs, impairs or conditions the exercise of a national bank's federally-authorized powers. This most assuredly does not mean that national banks are immune from all state laws or that any law that would have any impact on a national bank would be preempted.

Riegle-Neal Reaffirms Recognized Principles of Preemption

It was to these same principles that the Conference Report on the Riegle-Neal Act referred when it stated that "[u]nder well-established judicial principles, national banks are subject to State law in many significant respects …."[17] These standards in fact were expressly *preserved*, not rewritten, in the legislation itself. Indeed, the Act expressly contemplated that state laws might be preempted as to national banks. The Act provides that interstate branches of national banks are subject to certain state laws, including consumer protection laws, *except if* those laws are preempted as applied to the national bank. That Act states, in pertinent part:

[14] *National Bank v. Commonwealth*, 164 U.S. at 362.
[15] *McClellan v. Chipman*, 76 U.S. at 357.
[16] *Bank of America. v. City and County of San Francisco*, 309 F.3d 551, 559 (9th Cir. 2002).
[17] H.R. Conf. Rep. No. 103-651 at 53 (1994), *reprinted in* U.S.C.C.A.N. 2068, 2074.

> The laws of the host State regarding community reinvestment, consumer protection, fair lending, and establishment of interstate branches shall apply to any branch in the host State of an out-of-State national bank to the same extent as such State laws apply to a branch of a bank chartered by that State, *except* –
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> (i) *when Federal law preempts the application of such State laws to a national bank*; or
> (ii) when the Comptroller of the Currency determines that the application of such State laws would have a discriminatory effect on the branch in comparison with the effect the application of such State laws would have with respect to branches of a bank chartered by the host State.[18]

The Riegle-Neal Act also imposed a new public notice and comment process when the OCC was considering the application to national banks of state laws concerning community reinvestment, consumer protection, fair lending, and establishment of intrastate branches, but even there, Congress expressed the intent that the new process was "not intended…to change the substantive theories of preemption as set forth in existing law."[19]

Impact of the Gramm-Leach-Bliley Act On National Bank Preemption Principles

Nor did the Gramm-Leach-Bliley Act rewrite the principles of preemption applicable to national banks. The letter suggests that the Act reaffirms a standard set by the Supreme Court to the effect that state laws apply to national banks unless those laws "prohibit or significantly interfere" with a national bank's congressionally authorized powers. This is simply not so.

First, the "prohibit or significantly interfere" test refers to the "prevent or significantly interfere" test in section 104(d)(2) of the Act.[20] That section *only pertains to certain insurance sales activities*, not to all of a national bank's federally-authorized activities. Second, section 104(d)(2) expressly preserves the applicability of the Supreme Court's *Barnett* decision, thus retaining – at least with respect to national banks – the principles of preemption relied upon by the Supreme Court in its analysis in the *Barnett* case.[21]

Supervision and Enforcement Activities with Respect to National Banks

It is also important to understand our position concerning the scope of the OCC's exclusive supervisory and regulatory authority (i.e., our "visitorial powers") with respect to national banks (and their operating subsidiaries). The long-standing federal statute that confers on the OCC exclusive visitorial authority with respect to national banks, 12 U.S.C. § 484, is virtually unqualified in its reach and provides simply that national banks shall not be subject to "any

[18] Pub. L. No. 103-328, § 102, 108 Stat. 2338, 2349-50 (Sept. 29, 1994) (codified at 12 U.S.C. § 36(f)(1)(A)) (emphasis added).
[19] H.R. Conf. Rep. No 103-651 at 55 (1994), *reprinted in* 1994 U.S.C.C.A.N. 2068, 2076.
[20] Pub. L. No. 106-102 § 104(d)(2), 113 Stat. 1338, 1353 (November 12, 1999) (codified at 15 U.S.C. § 6701(d)(2)).
[21] *Id.*

visitorial powers except as authorized by Federal law, vested in the courts of justice," or exercised by Congress. One specific exception provided in section 484(b) permits state auditors and examiners to examine national bank records to ensure compliance with state unclaimed property or escheat laws. Consistent with the original purpose of section 484, judicial precedent, and as may be inferred by the nature of the exception carved out in subsection (b), the OCC's authority under section 484 applies comprehensively to the content and conduct of the business of banking by national banks, including safety and soundness and consumer protection aspects of that business.

This principle of exclusive authority was reinforced by Congress in the Riegle-Neal Act. As noted above, the Riegle-Neal Act provides that interstate branches of national banks are subject to certain state laws, including consumer protection laws, if those laws are not preempted as applied to national banks. However, Congress expressly provided that, in the case of any non-preempted state consumer law, "[t]he provisions of any State law to which a branch of a national bank is subject... shall be enforced, with respect to such branch, by the Comptroller of the Currency." 12 U.S.C. § 36(f)(1)(B). In short, Congress clearly recognized the OCC's exclusive power to enforce against national banks state consumer protection laws that are not preempted.

Preexisting OCC regulations also provide that operating subsidiaries of national banks are subject to state law to the same extent as their parent bank.[22] Essentially, our position is that operating subsidiaries of national banks are federally-licensed, federally-authorized means by which national banks conduct federally-authorized activities. Operating subsidiaries may only conduct activities permissible for their parent banks, at locations at which the bank would be permitted to engage in those activities. To date, two district court decisions that have directly addressed this issue have agreed with the position expressed by the OCC.[23] A third case currently is pending.[24]

Here again, we do not contend that states have no enforcement role. First, our position with respect to the role of the OCC concerns enforcement of state laws that affect the business of banking authorized for national banks under federal law. Second, I have repeatedly made clear the OCC's willingness to work on a cooperative basis with state officials when they have evidence that national banks, or their operating subsidiaries, may have engaged in activities that could be considered to violate state law. The OCC has a broad range of enforcement powers to remedy and sanction unfair and deceptive practices and unsafe and unsound banking practices, and we have made clear that we will use these powers if abusive practices are brought to our attention. This approach would be both consistent with our statutory authority and would also result in the broadest application of federal and state resources to protect consumers, since scarce state resources might then be applied to entities that are not already highly regulated.

In furtherance of this approach, in recent correspondence with Iowa Attorney General Tom Miller, I described special new processes the OCC has put into place to handle referrals from

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[22] 12 C.F.R. § 7.4006. *See also* 12 C.F.R. §§ 5.34 and 34.1(b).
[23] *Wells Fargo Bank, N.A. v. Boutris*, 265 F. Supp.2d 1162 (E.D. Cal. 2003); *National City Bank of Indiana v. Boutris*, 2003 WL 21536818 (E.D. Cal. July 2, 2003).
[24] *Wachovia Bank, N.A. v. Burke*, Civil No. 303CV0738(MRK) (D.C. Conn. filed April 25, 2003).

state officials with regard to potential violations by national banks.[25] In that letter, I strongly urged Attorney General Miller and his fellow Attorneys General to bring to our attention complaints that they receive that allege that national banks are engaged in any illegal, predatory, unfair or deceptive practices, so that we may take appropriate action. To the extent that the matter involves an individual customer grievance, the complaint would appropriately be sent to the OCC's Customer Assistance Group. Where there is a broader issue, such as the applicability of a particular state law to national banks generally, or if information indicates that a specific national bank is engaged in a particular practice affecting multiple customers that is predatory, unfair or deceptive, this information would be communicated to the OCC's Office of Chief Counsel for coordination.

Conclusion

Please be assured that we approach national bank preemption issues with great care, thorough consideration of the applicable judicial precedents as well as any legislative history surrounding the provisions of law at issue, an appreciation of the character of the national banking system as one half of our nation's dual banking system, and with an awareness of our responsibilities, as your letter put it, as "the exclusive supervisor of national banks." We will continue to take proactive steps to prevent national banks or their operating subsidiaries from engaging in inappropriate practices, and to react vigorously to evidence that they may have done so. We are very aware of our responsibilities in that regard in cases where preemption affects the application of state anti-predatory lending laws, and I previously corresponded at length with you on that particular issue.[26] Any future actions we may take – in litigation, interpretations, determinations, or rulemaking – will continue to be based on thorough evaluation of all the considerations and ramifications of the action.

Sincerely,

John D. Hawke, Jr.
Comptroller of the Currency

[25] Letter dated July 25, 2003.
[26] Letter dated July 22, 2003.