



April 8, 2003

The Honorable John D. Hawke, Jr.
Comptroller of the Currency
Office of the Comptroller of the Currency
250 E Street, S.W.
Public Information Room, Mailstop 1-5
Attention: Docket No. 03-02
Washington, DC 20219

Re: OCC Docket No. 03-02 – Notice of Proposed Rulemaking, 68 Fed. Reg. 6363 (2003).

Dear Comptroller Hawke:

The Conference of State Bank Supervisors (“CSBS”)¹ appreciates this opportunity to comment on the Notice of Proposed Rulemaking, Docket No. 03-02, which was published by the Office of the Comptroller of the Currency (“OCC”) at 68 Fed. Reg. 6363 (Feb. 7, 2003). Specifically, as discussed below, CSBS is providing comments on the OCC’s proposed amendments to 12 C.F.R. §§ 7.4000 & 5.33. The OCC has stated that its proposed revisions to Section 7.4000 are intended to “clarify” the meaning and application of 12 U.S.C. § 484 with respect to the OCC’s exercise of “visitorial powers” over national banks and their operating subsidiaries. The OCC has explained that its proposed revisions to Section 5.33 will establish procedures for mergers between national banks and their nonbank affiliates, based on the authority granted under 12 U.S.C. § 215a-3.

The scope of the proposal is breathtaking and raises important public policy questions:

1. Creation of a new Corporate Structure for Non Insured National Banks – CSBS supports the dual banking system and advancements made by both the OCC and by state banking agencies to continually improve the flexibility, quality and responsiveness of bank charters. Such improvements provide great value to the financial services marketplace, to consumers and help make our economy vibrant and strong. However, the OCC’s proposal to allow limited purpose national banks to conduct fiduciary activities *or* “any other activities within the business of banking” raises important questions. The OCC has interpreted the business

¹ CSBS is the professional organization that represents the regulators of the nation’s 6,500 state-chartered banks and works to advance the state banking system. In preparing our comment letter, CSBS worked with numerous state banking departments.

of banking more and more broadly over the years. We note for example, that under recent authority granted by the OCC in regulations relating to electronic banking, national banks are acting as web site hosts and operating “virtual malls” which bring together buyers and sellers for products and services not necessarily related to banking activities.

There are many existing options for national banks and their holding companies to exercise a broad range of powers. CSBS is concerned that expansion of the limited purpose national bank charter creates a safe harbor - enabling wholesale preemption of state oversight and consumer protection laws for a group of entities conducting activities only loosely related to banking.

The OCC has taken a strong stand on banks “renting their charters” to non banks. However, additional clarification on the OCC’s plans for expanding limited purpose national bank powers is needed to avoid a perception that the OCC is availing the national bank charter to a group of entities not conducting core banking activities. CSBS questions what authority the OCC has to undertake such a sweeping measure.

2. Exclusive Visitorial Authority: The proposal seeks to codify the OCC’s recent determination that their exclusive visitorial authority applies not only to national banks but also to operating subsidiaries of national banks. This has led some mortgage lending national bank operating subsidiaries - licensed and regulated at the state level - to turn in their licenses and even refuse to pay consumer restitution ordered after state examinations discovered consumer abuses. The courts have not clearly addressed this issue and CSBS recently submitted comments (see March 28, 2003 letter re: OCC request for comments on preemption of the Georgia Fair Lending Act.) to the OCC challenging the assertion that national bank preemption extends to national bank operating subsidiaries.
3. State Law and State Incorporated Operating Subsidiaries - CSBS opposes the OCC’s proposal that national bank operating subsidiaries that can only gain their corporate existence under state law are immune from state laws and conditions under which they gain their corporate status. Accordingly, CSBS questions the OCC’s authority to preempt state laws for state licensed/incorporated operating subsidiaries of national banks.
4. Consumer Protection - Preemption of state licensure requirements, including the ability to license and examine mortgage lending entities, is not sound public policy. Through vehicles such as mortgage licensure and examination, state banking departments, working in concert with other state law enforcement agencies, identify fraud and consumer abuses and work to make defrauded consumers whole. A recent agreement between state banking agencies, state attorneys general and a nationwide mortgage lender, provides a prominent example of the valuable role that state officials fill. The settlement was the largest amount (more than \$484 million) of consumer restitution in our nation’s history.

Eliminating the examination and enforcement resources that state officials currently provide to deter predatory lending, and replacing it with the OCC’s proposed unilateral approach to become the sole regulator of national bank operating subsidiaries, would leave shadows in which predatory lenders could find refuge. We encourage the OCC to revise its position and instead partner with state regulators, as the FTC has, to identify and stop abusive practices. Such partnerships benefit consumers and prevent harm to the reputation of an otherwise very

reputable financial services industry.

Government Sunshine Facilitates Sound Policymaking – The OCC has proposed that mergers of uninsured national banks with non bank affiliates when the surviving institution is the national bank are not subject to the public hearing or public comment process unless the OCC determines that the application presents a significant and novel policy, supervisory or legal issue(s). CSBS suggests that such an approach to an unprecedented form of mergers provides an inappropriate shield and limits the OCC from the receipt of potentially valuable information as the Agency considers such merger requests.

CSBS strongly urges the OCC to withdraw its proposed amendments to Section 7.4000, and to make significant changes in its proposed revisions to Section 5.33. Apart from the public policy questions articulated above, there are significant legal questions concerning the legitimacy of the OCC’s proposed regulatory changes. For the reasons set forth in Part A below, the OCC’s proposed amendments to Section 7.4000 are contrary to governing statutes and judicial precedents. Part B of this comment letter addresses the merger provisions of the proposal between national banks and non bank affiliates.

As for the Section 7.4000 proposed changes relating to visitorial powers, the OCC does not have legal authority to adopt those proposed amendments. In summary, CSBS maintains that:

- (1) The OCC’s apparent theory of “field preemption” is contrary to a long line of decisions issued by the U.S. Supreme Court and other courts. The proposed amendments appear to be part of a campaign by the OCC to establish a “uniform system of laws and uniform supervision” (68 Fed. Reg. at 6369), which would preempt *all* state laws from applying to national banks *unless* Congress has *expressly* incorporated state-law standards into the National Bank Act. Judicial authorities, however, have consistently upheld the principle that “federally chartered banks are subject to state law.” *Atherton v. FDIC*, 519 U.S. 213, 222 (1997). Based on this principle, national banks must comply with applicable state laws *unless* such laws “prevent or significantly interfere with” the ability of national banks to exercise their congressionally-authorized powers. *Barnett Bank of Marion County, N.A. v. Nelson*, 517 U.S. 25, 33 (1996).
- (2) Congress has endorsed the presumptive application of state laws to national banks. In passing the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994, Congress affirmed that (i) “States have a legitimate interest in protecting the rights of their consumers, businesses and communities,” and therefore (ii) “States have a strong interest in the activities and operations of depository institutions doing business within their jurisdictions, *regardless of the type of charter an institution holds.*” H.R. Rep. No. 103-651, at 53 (1994) (Conf. Rep.) (emphasis added). This clear congressional mandate would be seriously compromised by the OCC’s proposed amendments to Section 7.4000.

- (3) The courts have repeatedly upheld the authority of state officials to sue in federal or state court to enforce valid state laws against national banks, however, the OCC's proposal would bar the states from suing in federal or state courts to enforce applicable state laws against national banks. The proposed amendments to Section 7.4000 are contrary to the Tenth Amendment, because they would deprive the states of their sovereign right to exercise their historic police powers through the use of judicial process.
- (4) The proposed amendments to Section 7.4000 are also unlawful because they seek to prevent the states from exercising "visitorial powers" over the operating subsidiaries of national banks. The OCC has no legal authority to exclude the states from licensing, examining and otherwise regulating state-chartered corporations that are subsidiaries of national banks. Federal banking statutes and state corporate laws establish a clear separation between national banks and their "affiliates," including their operating subsidiaries. Operating subsidiaries are chartered as separate corporate entities under the authority of state law. Because they exist solely as a creation of state law, they must comply with all applicable state requirements, including regulations and orders issued by state officials. The proposed amendments would effectively "federalize" state-chartered operating subsidiaries by subjecting them to the exclusive supervisory control of the OCC. The amendments are therefore contrary to the Tenth Amendment, because they would infringe upon the sovereign right of the states to regulate corporations created under the authority of state law.

In addition, for the reasons set forth in Part B below, CSBS strongly urges the OCC to make the following changes to its proposed revisions to 12 C.F.R. § 5.33:

- (1) The OCC must change Section 5.33(f) to provide that every application by a national bank to merge with a nonbank affiliate will comply with the OCC's procedures under 12 C.F.R. §§ 5.10 & 5.11, which allow members of the public to submit comments and request a hearing. Mergers between national banks and nonbank affiliates are unprecedented and are likely to raise many important issues implicating bank supervision, bank safety and soundness, and the general public interest. No such merger should be approved without providing a full opportunity for members of the public to submit comments and request a hearing.
- (2) Section 5.33 must be revised, in accordance with 12 U.S.C. §§ 215a-3(b)(1) & 1828(c)(1)(A), to provide that each merger between an insured national bank and a nonbank affiliate must receive the prior written approval of the FDIC.
- (3) Section 5.33(g)(4)(v) must be changed, in accordance with Section 215a-3(b)(2), to provide that any merger between a national bank and a nonbank affiliate that results in a national bank will *not* permit that bank to exercise any power or authority to engage in an activity that is not permissible for a national bank under applicable provisions of federal law *other than* Section 215a-3.

- (4) Section 5.33(g)(5)(v) must be revised, in accordance with 12 U.S.C. § 214b, to provide that any merger between an uninsured national bank and a nonbank affiliate that results in a nonbank *company* will become a state-chartered/licensed entity, and therefore, will be regulated by the appropriate state authority. In addition, it should be clarified that the nonbank company will *not* be permitted to exercise (i) any power or authority to engage in an activity for which a bank charter is required under federal or state law, or (ii) any power or authority to engage in an activity that is not permissible for a similar state-chartered company under applicable provisions of state law.

Finally, although the OCC noted that the proposed rulemaking *may* have Federalism implications, the proposed amendments to Sections 7.4000 and 5.33 have *significant* “federalism implications” and therefore require the OCC to comply with Executive Order 13132, 64 Fed. Reg. 43255 (Aug. 10, 1999). CSBS calls upon the OCC to postpone any further action on its Notice of Proposed Rulemaking until the OCC has fully complied with the consultative procedures and other requirements of Executive Order 13132.

A. The OCC Must Withdraw Its Proposed Revisions to 12 C.F.R. § 7.4000.

1. The Apparent Theory of “Field Preemption” Contained in the OCC’s Notice of Proposed Rulemaking Is Contrary to Judicial Authorities That Affirm the Presumptive Application of State Laws to National Banks.

In its Notice of Proposed Rulemaking, the OCC asserts that “section 484 directs that, unless Federal law supplies an exception, the OCC is *exclusively authorized* to determine what standards apply to a national bank’s activities and whether a national bank’s conduct complies with applicable standards, and to enforce adherence to those standards.” 68 Fed. Reg. at 6369 (emphasis added). The Notice further claims that the OCC’s “exclusive” exercise of “visitorial powers” is justified by (i) “the need for a *uniform system of laws and uniform supervision* that would foster the nationwide banking system,” and (ii) the need to “avoid inconsistent and potentially hostile application of [state law] standards by state authorities.” *Id.* (emphasis added).

The OCC’s proposal to expand the preemptive scope of Section 7.4000 appears to be part of a broader campaign by the OCC to destroy a fundamental tenet of our dual banking system. Under our dual banking system, which incorporates basic principles of federalism, the states have authority to regulate the business operations of all banks, *including* national banks, *unless* Congress chooses to preempt state laws in a *specific* area. In 1997, the Supreme Court affirmed, based on prior decisions stretching back more than a century, that federally-chartered 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. . . . It is only when the State law incapacitates the [national] banks from discharging their duties to the [federal] government that it becomes unconstitutional.” *Atherton v. FDIC*, 519 U.S. 213, 222-23 (1997) (quoting *National Bank v. Commonwealth*, 76 U.S. (9 Wall.) 353, 362 (1870)).

The OCC's recent actions are fundamentally at odds with this essential feature of our dual banking system. For example, in another pending regulatory proceeding (OCC Docket No. 03-04, published at 68 Fed. Reg. 8959, Feb. 26, 2003), the OCC is considering whether to grant a request for a preemptive determination filed by National City Bank. National City has urged the OCC to issue a regulation or order that would "occupy the field" of real estate lending by national banks and preempt all state laws in that area. In discussing National City's request, the OCC has stated that "[i]t may . . . be argued that [12 U.S.C. § 371] evidences an intent for the OCC to occupy the field of regulation of national banks' real estate lending, except, of course, where Congress in other legislation has made them subject to additional requirements." 68 Fed. Reg. at 8961. On March 28, 2003, CSBS filed a 27-page comment letter that strenuously opposed National City's request and demonstrated that the OCC has no legal authority to "occupy the field" of real estate lending or any other area of business operations carried on by national banks.

Based on the OCC's above-quoted comment in Docket 03-04, as well as the OCC's description of its proposed amendments to Section 7.4000, the OCC apparently believes that it can preempt the application of *all* state laws to national banks *except for* state-law standards that Congress has *expressly* incorporated by reference in federal statutes (e.g., 12 U.S.C. § 36, with regard to branching, or 12 U.S.C. § 92a, with regard to trust powers). Further evidence of this attitude appears in OCC Advisory Letter 2002-9, at 3 (Nov. 25, 2002), where the OCC declared: "Congress provided that the *uniform federal standards* that would govern national banks – and state laws, *where federal law makes them applicable* – would be enforced by a single, federal supervisor, the OCC" (emphasis added). Similarly, in a recent letter to CSBS, the OCC argued that "[n]ational banks were established by Congress as instrumentalities to carry out multiple Congressional objectives and were designed to constitute a national banking system, *independent of State direction or supervision, operating under Federal standards administered by the OCC.*" Letter dated Feb. 21, 2003, from Comptroller of the Currency John D. Hawke, Jr. to CSBS President Neil Milner, at 4 (emphasis added).

In short, the OCC is evidently promoting a theory of "field preemption" that would justify a sweeping preemption of state laws. This theory, however, is flatly contradicted by many court decisions that have examined the structure of our dual banking system. Those decisions have repeatedly upheld the application of state laws to national banks *without* requiring any express congressional incorporation of state-law standards into the National Bank Act ("NBA"). As previously mention, CSBS filed a comment letter on March 28, 2003, that details case law supporting our position against the OCC's ability to use "field preemption. For your convenience, we have attached a copy of that letter to cross-reference CSBS' rationale on this point.

In *Atherton v. FDIC*, the Supreme Court reaffirmed the basic principle that "federally chartered banks are subject to state law," and the Court cited several of its previous decisions in support of that decision. In *Barnett Bank of Marion County, N.A. v. Nelson*, 517 U.S. 25 (1996), a case frequently cited by the OCC, the Court observed that preemption of state law will "normally" occur if a state takes action "to *forbid, or impair significantly*, the exercise of a

power that Congress *explicitly* granted.” 517 U.S. at 33 (emphasis added). However, immediately after this statement, the Court added: “To say this is *not* to deprive States of the power to regulate national banks, where . . . doing so *does not prevent or significantly interfere with* the national bank’s exercise of its powers.” Id. at 33-34 (emphasis added, citing *Luckett, McClellan* and *Commonwealth*). This crucial qualifying statement and the Court’s supporting citations demonstrate that *Barnett* did *not* overrule the presumptive application of state laws to national banks.² Three other Supreme Court cases, which are frequently invoked by the OCC, similarly recognize that state laws apply to national banks as long as they do not discriminate against national banks or create an impermissible conflict with their federally-granted powers.³

In *Long*, the Third Circuit upheld a New Jersey statute that prohibited all banks, including national banks, from engaging in geographic discrimination in their home mortgage lending (“redlining”). The Third Circuit pointed out that Congress had passed three statutes – the Home Mortgage Disclosure Act, the Community Reinvestment Act and the Equal Credit Opportunity Act – that were designed to encourage fair lending by banks, and the court noted that those statutes “[do] not expressly prohibit redlining.” 630 F.2d at 984. In addition, the court observed that Congress had *not* granted to the states any *express* authority to enact anti-redlining legislation. Nevertheless, the court overruled a preemption claim made by two national banks, and the court held that national banks must comply with New Jersey’s anti-redlining law. In doing so, the court declared: “[W]e reject the plaintiffs’ argument that once Congress legislates on a matter in the banking field, specific authorization must be given before supplementary state laws may take effect.” Id. at 987. Two subsequent decisions have similarly held that federal

² The OCC has often cited the Court’s observation in *Barnett* that the express and incidental powers of national banks are “grants of authority not normally limited by, but rather ordinarily pre-empting contrary state law.” 517 U.S. at 32. However, the Court’s careful use of the terms “normally,” “ordinarily” and “contrary” indicates a clear understanding by the Court that a finding of preemption can only be made *after* determining whether, in fact, a challenged state law is “contrary” to federal law under the “prevent or significantly interfere” test articulated by the Court, id. at 33. See *Peatros v. Bank of American NT&SA*, 22 Cal. 4th 147, 990 P.2d 539, 550 (2000).

³ See *Franklin National Bank v. New York*, 347 U.S. 373, 378 n.7 (1954) (citing *McClellan* and *Luckett*, and noting that “national banks may be subject to some state laws in the normal course of business if there is no conflict with federal law,” even though Congress has not incorporated such state laws into the NBA); *Davis v. Elmira Savings Bank*, 161 U.S. 275 (1896) (affirming that (i) “so far as not repugnant to acts of Congress, the contracts and dealings of national banks are left subject to the state law,” id. at 287, and (ii) “[n]othing, of course, in this opinion is intended to deny the operation of general and undiscriminating state laws on the contracts of national banks, so long as such laws do not conflict with the letter or the general objects and purposes of Congressional legislation”, id. at 290); *First National Bank of San Jose v. California*, 262 U.S. at 368-69 (recognizing that the “contracts and dealings [of national banks] are subject to the operation of general and undiscriminating state laws which do not conflict with the letter or the general objects and purposes of congressional legislation”).

banking laws do *not* preempt the states from requiring all banks, including national banks, to refrain from imposing unreasonable or unconscionable service charges on their customers. *Perdue*, 702 P.2d at 516-25; *Video Trax*, 33 F. Supp. 2d at 1047-49, 1058.

The foregoing lower court decisions are entirely consistent with the line of Supreme Court precedents cited in CSBS' March 28, 2003, comment letter on Docket No. 03-04. Taken together, these decisions establish that (i) the regulation of banking is an area of longstanding and fundamental state concern, (ii) Congress has *not* "regulate[d] national banks to the exclusion of state control," because "congressional support remains for dual regulation," and (iii) state laws therefore presumptively apply to the contracts and operations of national banks *unless* federal preemption of state law is mandated by "the clear and manifest purpose of Congress." *Long*, 630 F.2d at 985 (citing *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 219, 230 (1947)); *Video Trax*, 33 F. Supp. 2d at 1048 (same); *Peatros*, 990 P.2d at 543 (quoting *Cipollone v. Liggett Group, Inc.*, 505 U.S. 504, 516 (1992)); *Perdue*, 702 P.2d at 519-23. *See also* *Luckett*, 321 U.S. at 248 (holding that "national banks are subject to state laws, unless those laws infringe the national banking laws or impose an undue burden on the performance of the [national] banks' functions"); *Northeast Bancorp v. Board of Governors*, 472 U.S. 159, 177 (1985) (recognizing that "banking and related financial activities are of profound local concern"); *Lewis v. BT Investment Managers, Inc.*, 447 U.S. 27, 38 (1980) (same).⁴

The OCC's apparent theory of "field preemption" cannot be squared with the judicial precedents discussed above. Those cases *rejected* any notion that the federal law has "occupied the field" with regard to the business operations of national banks.⁵ Instead, the Supreme Court has consistently upheld the validity of state laws that (i) do not conflict with any express statutory power of national banks, (ii) apply equally to all banks and therefore do not discriminate against national banks, and (iii) do not place an undue burden on the operations of national banks. By contrast, in each case where the Supreme Court has determined that a state statute *was* preempted by federal law, the Court found that the challenged state law either discriminated against national banks or significantly interfered with the exercise of an *express* power granted to national banks under federal law.⁶

⁴ For leading Supreme Court cases that have applied the presumption *against* preemption in other fields of traditional state regulation, *see, e.g.,* *Medtronic, Inc. v. Lohr*, 518 U.S. 470, 475, 484-85 (1996); *N.Y. State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co.*, 514 U.S. 645, 654-56 (1995); *Cipollone*, 505 U.S. at 516-18; *California v. ARC America Corp.*, 490 U.S. 93, 100-01 (1989).

⁵ In fact, in *Bank of America v. City and County of San Francisco*, 309 F.3d 551 (9th Cir. 2002), the Ninth Circuit applied conflict preemption principles, rather than a field preemption analysis, in deciding that the challenged local ordinances could not be validly applied to national banks.

⁶ *E.g.,* *Barnett Bank*, 517 U.S. at 28-31 (invalidating a Florida law that prohibited national banks from exercising their *express* authority to sell insurance in towns of 5,000 or less under 12 U.S.C. § 92); *Franklin National Bank*, 347 U.S. at 374-78 (striking down a New York

2. Congress Has Specifically Endorsed the Presumptive Application of State Laws to National Banks

When it passed the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (“Riegle-Neal Act”), Congress specifically recognized and endorsed the presumption that state laws apply to the activities of national banks. The report of the House-Senate conference committee on the Riegle-Neal Act declared:

- (1) “States have a strong interest in the activities and operations of depository institutions doing business within their jurisdictions, *regardless of the type of charter an institution holds*. In particular, States have a legitimate interest in protecting the rights of their consumers, businesses and communities.”
- (2) “Congress does not intend that the [Riegle-Neal] Act of 1994 alter [the balance of Federal and State law under the dual banking system] and thereby weaken States’ authority to protect the interest of their consumers, businesses and communities.”
- (3) “Under well-established judicial principles, *national banks are subject to State law in many significant respects*.”
- (4) In determining whether state laws are preempted by federal law, “[c]ourts generally use a rule of construction that *avoids finding a conflict between Federal*

law that favored state-chartered savings banks and prohibited national banks from using advertising to promote their *express* power to accept “savings deposits” under former 12 U.S.C. § 371); *First National Bank of San Jose v. California*, 262 U.S. at 368-70 (invalidating a California statute that escheated bank accounts to the state upon mere dormancy for a specified period and without any proof of abandonment, because the state law threatened a “possible confiscation” of depositors’ funds and, therefore, significantly interfered with national banks’ exercise of their *express* authority to accept deposits); *Davis v. Elmira Savings Bank*, 161 U.S. at 283-85 (striking down a New York law requiring receivers of insolvent national banks to give priority to deposit claims by state-chartered savings banks: *held*, the state law violated the NBA’s *express* command that the OCC, as receiver for national banks, must make a “ratable distribution” to all creditors); *Easton v. Iowa*, 188 U.S. 220, 227-232 (1903) (invalidating Iowa statutes that prohibited insolvent national banks from accepting deposits and imposed criminal penalties for violations on officers of national banks; *held*, the state laws significantly interfered with the NBA’s *express* grant of *exclusive* authority to the OCC to determine whether a national bank was insolvent and, if so, to supervise the winding up of its business and liquidation of its assets); *Farmers’ and Mechanics’ National Bank v. Dearing*, 91 U.S. 29 (1875) (invalidating a New York law that required national banks to forfeit the principal of usurious loans, because that forfeiture penalty was contrary to the *express* terms of Section 30 of the NBA, presently codified at 12 U.S.C. § 85).

*and State law where possible.”*⁷

The foregoing “Congressional intent” statements refute any suggestion that the OCC has authority to adopt a theory of “field preemption” in dealing with state-law issues. On the contrary, the Riegle-Neal Act expressly mandates that local branches of out-of-state national banks must generally comply with host state laws dealing with community reinvestment, consumer protection and fair lending. See 12 U.S.C. § 36(f). During the debates on the House-Senate conference report for the Riegle-Neal Act, members of Congress declared that the general application of state laws to national banks in these areas was essential to preserve a viable dual banking system.⁸ Again, CSBS would refer you to our attached 27-page comment letter on Docket No. 03-04, dated March 28, 2003, which details the analysis supporting our belief that Congress never intended for the OCC to “occupy the field” in regard to national banks. Even the OCC’s prior reasoning and conclusions (in Interpretative Letter #647) flatly contradict any notion that federal law “occupies the field” with regard to the business operations of national banks.

Furthermore, CSBS understands that Congress is beginning to directly question the OCC’s recent proposals to preempt the Georgia Fair Lending Act for both national banks and their operating subsidiaries as well as the OCC’s legal ability and examination resource capacity to pursue exclusive visitorial authority as it relates to operating subsidiaries. Considering much of the OCC’s argument for field preemption of state laws relies heavily on Congressional intent, CSBS would strongly urge the OCC to fully clarify any outstanding Congressional questions prior to finalizing its final rule.

3. Section 484 Does Not Authorize the OCC to Prevent State Officials from Suing in Federal or State Courts to Enforce State Laws against National Banks.

In its Notice of Proposed Rulemaking, the OCC asserts that

the OCC’s visitorial powers [over national banks] are *exclusive* (except where otherwise provided by Federal law) with respect to activities comprising or in furtherance of the content of national banks’ business, that are expressly

⁷ H.R. Rep. No. 103-651 (Conf. Rep.), at 53 (emphasis added), reprinted in 1994 U.S. Code Cong. & Ad. News 2068, 2074.

⁸ See, e.g., 140 Cong. Rec. H 6777 (daily ed. Aug. 4, 1994) (remarks of Rep. Roukema, stating that “[t]he dual banking system and States’ rights are preserved in that the [Riegle-Neal Act] . . . preserves the States’ ability to apply State laws regarding intrastate branching, fair lending and consumer protection”); *id.* at S 12787 (Sept. 13, 1994) (remarks of Sen. Dodd, stating that the Riegle-Neal Act “strikes the proper balance between creating a more efficient national banking system and protecting States rights and the dual banking system . . . [by] requiring branches to abide by applicable State laws”).

authorized or recognized as permissible for national banks under Federal law. . . . [S]ection 484 directs that, unless Federal law supplies an exception, the OCC is *exclusively* authorized to determine what standards apply to a national bank's activities and whether a national bank's conduct complies with applicable standards, and to enforce adherence to those standards.

63 Fed. Reg. at 6369 (emphasis added). The OCC's proposed amendments to Section 7.4000 are expressly intended to prevent the states from suing in federal or state court to "supervise the activities of national banks and compel their adherence to a variety of state-set standards." *Id.* at 6369, 6370. According to the OCC, the proposed amendments would permit states "to seek a declaratory judgment from a court as to whether a particular state law . . . is preempted. However, if a court rules that a state law is not preempted, [judicial] enforcement of a national bank's compliance with that law is within the OCC's *exclusive* purview." *Id.* at 6370 (emphasis added).

The OCC's claim of *exclusive* "visitorial powers" over national banks is *not* supported by the terms of Section 484. Section 484(a) provides:

No national bank shall be subject to any visitorial powers except as authorized by Federal law, vested in the courts of justice or such 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.

Thus, the text of Section 484(a) "does *not* contain an *explicit* grant of *exclusive* regulatory or visitorial power over national banks to the OCC." *First Union National Bank v. Burke*, 48 F. Supp. 2d 132, 144 (D. Conn. 1999) (emphasis added); see also *id.* at 137 (noting that "the OCC is not explicitly referenced in Section 484"). Other provisions of federal law authorize the OCC to (i) examine national banks, (ii) bring administrative enforcement actions against national banks (e.g., proceedings for cease-and-desist orders and civil money penalty orders), and (iii) sue in federal court to revoke the charter of a national bank whose directors have knowingly violated, or knowingly permitted other bank officers or agents, to violate the NBA. See 12 U.S.C. §§ 481, 1818 & 93. None of those provisions, however, purports to grant *exclusive* visitorial powers to the OCC over national banks or to bar other government officials from enforcing laws within their purview that apply to national banks. For example, the FDIC is authorized to make special examinations of national banks and may institute administrative proceedings to terminate their deposit insurance for unsafe or unsafe practices or conditions. *Id.* §§ 1820(b)(3) & 1818(a). Similarly, the Federal Reserve Board has authority to make special examinations of national banks that are subsidiaries of bank holding companies. *Id.* § 1844(c)(2).

The OCC's claim of *exclusive* visitorial authority over national banks has no explicit statutory basis. The OCC relies on 12 U.S.C. § 36(f)(1)(B), which provides that host state laws applicable to the local branches of out-of-state national banks "shall be enforced" by the OCC. See 68 Fed. Reg. at 6369. However, the terms of Section 36(f) do *not* expressly bar state officials from seeking judicial orders compelling national banks to comply with applicable state

laws. The legislative history of Section 36(f)(1)(B) clearly indicates that the provision was intended to provide the OCC with the sole authority to examine, or take supervisory (i.e., administrative) enforcement actions against, national bank branches.⁹ When Section 36(f)(1)(B) is read together with Section 484(a), it becomes clear that state officials retain their authority to obtain judicial orders requiring national banks to comply with valid state laws. Such orders would represent a proper exercise of “visitorial powers” that are expressly permitted to the courts under Section 484(a).

The original NBA made clear that *both federal courts and state courts* could exercise “visitorial powers” over national banks in appropriate cases. Section 57 provided that “suits, actions and proceedings against any association under this act may be had in any circuit, district, or territorial court of the United States held within the district in which such association may be established; *or in any state, county or municipal court in the county or city in which said association is located, having jurisdiction in similar cases.*” 13 Stat. 116-17 (emphasis added). Section 57 included a proviso stating that “all proceedings to enjoin the [OCC] under this act” must be filed federal court. *Id.* at 117. By negative implication, this proviso made clear that judicial proceedings *against national banks* could be brought in *either* federal or state courts. Based on the language of Section 57, the Supreme Court repeatedly upheld the jurisdiction of state courts to adjudicate claims filed against national banks. E.g., *First National Bank of Charlotte v. Morgan*, 132 U.S. 141 (1889); *Bank of Bethel v. Pahquioque Bank*, 81 U.S. (14 Wall.) 383 (1871). In *Morgan*, the Supreme Court noted that the “exemption of national banking associations from suits in state courts, established elsewhere than in the county or city in which such associations were located, was . . . prescribed for the convenience of those institutions, and to prevent interruption in their business that might result from *their books being sent to distant counties in obedience to process from state courts.*” 132 U.S. at 145. Thus, the *Morgan* decision specifically recognized the authority of state courts to issue subpoenas requiring defendant national banks to produce their books and records, because the Court explained that the local venue provisions of Section 57 were designed to protect national banks from being burdened by subpoenas issued by distant state courts.

The “visitorial powers” provision of Section 57 was later incorporated, with modifications, in Rev. Stat. § 5241. Section 5241 stated that “[n]o association shall be subject to any visitorial powers other than such as are authorized by this Title, *or are vested in the courts of justice*” (emphasis added). Like Section 57, Section 5241 did *not* expressly provide the OCC with *exclusive* visitorial authority over national banks. Instead, Section 5241 (again, like its predecessor) recognized that “visitorial powers” over national banks were *also* “vested in the courts of justice.” Based on the terms of Section 5241, the Supreme Court and lower courts repeatedly held that state officials and private parties could sue in state courts to enforce valid state laws against national banks. E.g., *Colorado National Bank v. Bedford*, 310 U.S. 41, 43-46, 51-53 (1940); *St. Louis*, 262 U.S. at 659-61; *Guthrie v. Harkness*, 199 U.S. 148, 155-59 (1905); *Waite*, 94 U.S. at 532-33; *First National Bank of Youngstown v. Hughes*, 6 Fed. 737, 740-42

⁹ See 140 Cong. Rec. H 12786 (daily ed., Sept. 13, 1994) (colloquy between Sen. D’Amato and Sen. Riegle).

(C.C.A., N.D. Ohio 1881), *appeal dismissed*, 106 U.S. 523 (1883). The courts also repeatedly upheld the authority of state courts to issue subpoenas or writs of mandamus, or to impose penalties, as a means of requiring national banks to produce their records in response to valid state laws. E.g., *Guthrie*, 199 U.S. at 150, 156, 159 (mandamus); *Waite*, 94 U.S. at 533 (penalty); *Hughes*, 6 Fed. at 737-42 (subpoena).

Accordingly, state officials have the undoubted authority to sue in federal or state courts to obtain judicial orders enforcing applicable state laws against national banks, based on Section 484's explicit recognition of the "visitorial powers . . . vested in the courts of justice." E.g., *Burke*, 48 F. Supp. 2d at 146 (holding that, under Section 484, "a state may seek enforcement of its state banking laws in either federal or state court"); *id.* at 149 (stating that Section 484 "expressly leaves available judicial remedies to compel national bank compliance with state law"); *St. Louis*, 263 U.S. at 659-51 (reaching same conclusion).¹⁰ In addition, before filing suit against national banks, state officials can require the banks to provide reports (as contrasted with the underlying bank "records") to determine whether the banks are complying with valid state laws. If the required reports show that a national bank is violating state laws, or if a national bank refuses to furnish such reports, state officials may then file suit and use the court's subpoena power to compel the bank to provide either the reports or its underlying records. E.g., *Luckett*, 321 U.S. at 252-53, *Waite*, 94 U.S. at 532-33; *Hughes*, 6 Fed. at 737-42; see also *Guthrie*, 199 U.S. at 159 (holding that "[i]f the right to compel [by judicial process] the inspection of [a national bank's] books was a well-recognized common-law remedy, as we have no doubt it was, even if included in visitorial powers . . . it would belong to that class 'vested in courts of justice' which are expressly excepted from the inhibition of the statute").¹¹

¹⁰ Contrary to the OCC's suggestion, the decision in *Long* did *not* bar the New Jersey banking commissioner from filing suit in federal or state court to enforce New Jersey's anti-redlining laws against national banks. In its opinion, the Third Circuit made clear (including in the passage quoted by the OCC, 68 Fed. Reg. at 6370) that Section 484 preempted *only* two provisions of the state law that allowed the commissioner to issue *administrative* cease and desist orders and civil money penalty orders. See 630 F.2d at 983, 989 (describing §§ 9 and 10 of the state statute, and holding that *only* those provisions were preempted by Section 484); *id.* at 988 (stating that (1) "we find ourselves unable to agree with the district court's determination that state officials have the power to issue cease and desist orders against national banks"; and (2) "federal interest[s] subject to enforcement by the [OCC] are present in the cease and desist measures of the New Jersey Statute").

¹¹ The Third Circuit's decision in *Long* is highly instructive on the crucial difference between the authority of state officials to require "reports" from national banks and the authority of state officials to inspect "records" of national banks under Section 484. The court held that Section 484 preempted any "examination of [national] bank records" by state officials, because the term "visitorial powers" would "encompass examination of the [national] bank's books and records." 630 F.2d at 989. In contrast, the court did *not* refer to Section 484 in considering whether New Jersey could require national banks to provide statistical reports of their mortgage lending activity. The court concluded that the state's reporting requirements were preempted because "the [federal] Home Mortgage Disclosure Act superseded the reporting provisions of the

The Supreme Court’s decision in *St. Louis* removes all doubts regarding the authority of state officials to sue in state courts to obtain judicial enforcement of valid state laws against national banks. In that case, the defendant national bank *and* the Solicitor General of the United States contended that Rev. Stat. § 5241 (the predecessor of Section 484) and other provisions of the NBA barred state officials and state courts from suing to enforce any state law against national banks. See 263 U.S. at 642-43 (argument of counsel for the bank); *id.* at 645-48 (argument of the Solicitor General). The Supreme Court, however, *rejected* those arguments, and the Court held that state officials do *not* exercise prohibited “visitorial powers” when they bring judicial proceedings to compel national banks to comply with valid state laws:

What the State is seeking to do is to vindicate and enforce its own law, and the ultimate inquiry which it propounds is whether the [national] bank is violating that law, not whether it is complying with the charter or law of its creation. . . . Having determined that the power sought to be exercised by the [national] bank finds no justification in any law or authority of the United States, the way is open for the enforcement of the state statute. . . . The application of the state statute to the present case and the power of the State to enforce it being established, the nature of the [judicial] remedy to be employed [by State officials] is a question for state determination.

263 U.S. at 660-61(emphasis added). Similarly, state officials clearly have the authority to sue in *federal* court to secure judicial enforcement of valid state laws against national banks. (e.g. *Brown v. Clarke*, 878 F.2d 627(2d) Cir. 1989).

In view of the foregoing authorities, the proposed amendments to Section 7.4000(a)(3) and (b)(2) must be withdrawn. The OCC does *not* possess any “exclusive visitorial authority” that gives it the sole power to determine whether to file suit to enforce applicable state laws against national banks. Congress has *not* authorized the OCC to prevent state officials from either (1) requiring national banks to furnish descriptive reports (as contrasted with underlying bank “records”) that would give state officials a reasonable basis for determining whether national banks are complying with valid state laws, or (2) suing in federal or state courts to compel national banks to comply with applicable state laws. Notwithstanding the OCC’s assertions (68 Fed. Reg. at 6370), the OCC does *not* have statutory power to limit the judicial enforcement powers of state officials by requiring them to seek a declaratory judgment as to whether a particular state law is preempted, and then to delegate all their discretion as to judicial enforcement remedies to the OCC.

New Jersey statute.” *Id.* at 986. Thus, the court evidently did *not* believe that New Jersey’s reporting requirements ran afoul of Section 484. It is noteworthy that the New Jersey statute required national banks to “compile and disclose to the public statistical information” regarding their mortgage lending business, but the statute did *not* require national banks to produce their “records” (e.g., loan agreements and promissory notes) related to the underlying loans. See *id.* at 983 (describing the New Jersey statute).

In sum, the proposed amendments to Section 7.4000 are unlawful because they would radically expand, without congressional authority, the OCC's power to preempt the states' long-established role in regulating the business operations of national banks. Similarly, the proposed amendments would drastically reduce the scope of judicial enforcement powers available to state officials, thereby contravening the clear congressional mandate embodied in Section 484(a) and affirmed by the courts. The OCC has no authority to expand its preemptive authority unilaterally by adopting a regulation that vitiates Section 484's explicit and unconditional recognition of "visitorial powers . . . vested in the courts of justice." Indeed, the OCC's proposed amendments to Section 7.4000 raise serious constitutional questions under the principles of federalism embodied in the Tenth Amendment. Recent court decisions make clear that the federal government may not infringe upon the sovereign authority of the states to exercise their reserved police powers. By preventing states from using traditional judicial remedies to enforce applicable state laws against national banks, the proposed amendments would undeniably impair the police powers of the states in the field of banking.

4. The OCC Has No Authority to Prevent States from Exercising Visitorial Powers over Operating Subsidiaries of National Banks.

In a single sentence and accompanying footnote, the OCC states that the proposed amendments to Section 7.4000 would "also determine the scope of the OCC's exclusive visitorial authority with respect to national banks' operating subsidiaries." The OCC claims that its preemptive "visitorial authority" over national banks also extends to their operating subsidiaries, because those subsidiaries are "the equivalent of departments or divisions of their parent banks." 68 Fed. Reg. at 6369 & n.21. In making this claim, the OCC relies on the notice of final rulemaking that adopted 12 C.F.R. § 7.4006. See 66 Fed. Reg. 34784, 34788-89 (July 2, 2001).

Section 7.4006 provides that "[u]nless otherwise provided by Federal law or OCC regulation, State laws apply to national bank operating subsidiaries to the same extent that those laws apply to the parent national bank." In promulgating Section 7.4006, the OCC relied on Section 121 of the Gramm-Leach-Bliley Act ("GLBA"), codified at 12 U.S.C. § 24a(g)(3), and the OCC's operating subsidiary regulation, codified at 12 C.F.R. §§ 5.34(e). As shown below, none of these provisions supports the OCC's assertion that it can exercise "exclusive visitorial authority" over operating subsidiaries of national banks. Operating subsidiaries are state-chartered *nonbank* corporations. They are separate legal entities incorporated under state law, and they are *not* part of the "body corporate" that is established when the OCC charters a national bank. See 12 U.S.C. § 24 (stating that "a national banking association shall become, as from the date of execution of its organization certificate, a body corporate . . . [with] the name designated in the organization certificate"). As shown below, operating subsidiaries *cannot* invoke the preemption doctrine that applies to national banks.

Section 24a of the NBA, added by GLBA, permits national banks to establish "financial subsidiaries," which are authorized to engage in activities (e.g., securities underwriting and dealing) that are *not* permissible for their parent banks. Section 24a requires national banks to

satisfy numerous conditions (e.g., capital requirements, managerial ratings and community reinvestment standards) in order to establish and maintain financial subsidiaries. In this regard, Section 24a(g)(3) provides that the term “financial subsidiary” does *not* include a subsidiary that “engages solely in activities that national banks are permitted to engage in directly and are conducted subject to the same terms and conditions that govern the conduct of such activities by national banks.” Thus, Section 24a(g)(3) simply limits the scope of the definition of “financial subsidiary” by stating that the definition does *not* include an operating subsidiary that engages solely in activities permitted to its parent bank. Section 24a(g)(3) is *not* a power-granting provision, and it does *not* express any intent to bar the states from regulating operating subsidiaries. Instead, Section 24a merely provides that operating subsidiaries will not be treated as financial subsidiaries for purposes of *federal* law.

Neither GLBA nor its legislative history contains any statement indicating that Section 24a was intended to preempt the application of state laws to the activities of operating subsidiaries of national banks. The Senate Report on GLBA expressly *disclaims* any intent to expand the authority of operating subsidiaries, because it declares: “Nothing in this legislation is intended to affect the authority of national banks to engage in bank permissible activities through subsidiary corporations.” S. Rep. No. 106-44, at 8 (1999). The Senate Report confirms what is obvious from the terms of Section 24a(g)(3) – viz., that the provision does *not* grant any new authority to operating subsidiaries, and it merely exempts them having to comply with the *federal* requirements for financial subsidiaries.

In fact, Congress intended that Section 24a would *restrict* – not expand – the OCC’s authority to approve activities for operating subsidiaries. When Congress enacting GLBA, the House-Senate conferees directed the OCC to *rescind* its prior rule that allowed operating subsidiaries to engage in activities that were *not* permissible for national banks. The OCC responded to GLBA by promptly rescinding its prior rule, and by confirming that operating subsidiaries thereafter could only conduct operations that were permissible for their parent banks.¹² It is therefore a complete distortion of the terms and legislative history of Section 24a to assert, as the OCC has, that a statutory provision designed to *restrict* the OCC’s authority over operating subsidiaries can somehow be transformed into a grant of *additional preemptive power* to the OCC.

¹² See H.R. Rep. No. 106-434, at 160 (1999) (Conf. Rep.) (stating that Section 24a would “supercede and replace the OCC’s Part 5 regulations on operating subsidiaries”); OCC Decision on the Application by Zions First National Bank, OCC Conditional Approval No. 262, Dec. 11, 1997, 1997 OCC Ltr. LEXIS 127, at *5-*6 (explaining that the OCC’s existing regulation on operating subsidiaries – 12 C.F.R. § 5.34 – permitted operating subsidiaries to engage in activities that were *not* permissible for national banks); 65 Fed. Reg. 3157, 3160 (Jan. 20, 2000) (proposing to amend Section 5.34, “because the GLBA makes clear that an operating subsidiary may engage *only in activities that are permissible for the parent bank to engage in directly*”) (emphasis added); 65 Fed. Reg. 12905, 12911 (Mar. 10, 2000) (adopting amended Section 5.34(e), which provides that “[a] national bank may conduct in an operating subsidiary activities that are permissible for a national bank to engage in directly”).

Section 5.34 of the OCC's regulations similarly does *not* support the OCC's claim that it has authority to preempt state laws that apply to the activities of operating subsidiaries. Section 5.34 contains no mention of any intent to preclude the states from regulating the activities of operating subsidiaries.

Section 7.4006 of the OCC's regulations does mention state law, because it provides that "State laws apply to national bank operating subsidiaries to the same extent that those laws apply to the parent national bank." However, when the OCC adopted Section 7.4006 in 2001, the OCC declared that its new regulation would *not* preempt state law of its own force. The OCC said that Section 7.4006 "itself *does not effect* preemption of any State law; it reflects the conclusion we believe a Federal court would reach, even in the absence of the regulation, pursuant to the Supremacy Clause and applicable Federal judicial precedent." 66 Fed. Reg. 34784, 34790 (July 2, 2001) (emphasis added). Based on this disclaimer, the OCC claimed that it was *not* required to comply with Executive Order 13132, which, as discussed below in Part C, requires the OCC to follow detailed procedures before adopting any rule that has "federalism implications."

Given the OCC's assurance that Section 7.4006 "does not effect preemption of any State law," Section 7.4006 does not provide any legal basis for extending to operating subsidiaries the preemption of state law that would be created by the OCC's proposed amendments to Section 7.4000. In addition, CSBS maintains that the OCC did *not* satisfy the requirements of E.O. 13132 when the OCC adopted Section 7.4006. The OCC violated Section 6(c)(1) of E.O. 13132, because it did *not* "consult[] with State and local officials *early in the process* of developing the proposed [Section 7.4006]." See 64 Fed. Reg. at 43258 (emphasis added). The OCC acknowledged that it "brought the proposal [for Section 7.4006] to the attention of [CSBS]" only at the time that the proposal was published for comment by members of the public. 66 Fed. Reg. at 34790. Thus, the OCC did not notify CSBS until *after* the OCC had already decided on the proposed text of Section 7.4006. Moreover, the OCC subsequently *refused* to modify its proposal for Section 7.4006, even though "[a] number of commenters" – including CSBS and state banking departments – "were opposed to the provision." 66 Fed. Reg. at 34788-89, 34790. The OCC's belated notice, the OCC's failure to meet with CSBS and state banking officials to discuss Section 7.4006 *before* it was issued in proposed form, and the OCC's refusal to modify Section 7.4006 in light of adverse comments submitted by CSBS and state banking officials demonstrate that the OCC did *not* satisfy its obligation under E.O. 13132 to consult with CSBS and its members "early in the process of developing" Section 7.4006. Accordingly, any reliance by the OCC on Section 7.4006 as a legal basis for expanding either visitorial authority or preempting state law would be a clear violation of E.O. 13132.

The OCC's attempt to rely on Section 7.4006 is also contrary to governing statutes and judicial precedents. The limitations on "visitorial powers" under Section 484 apply only to "national bank[s]." Section 484 is currently codified as part of the Federal Reserve Act ("FRA"), and the terms used in Section 484 are therefore governed by the FRA's definitional sections, 12 U.S.C. §§ 221 & 221a. As those sections and related provisions of the federal banking laws make clear, a "national bank" is an institution that (i) has filed articles of association and an organization certificate with the OCC, pursuant to 12 U.S.C. §§ 21-24 & 26;

(ii) has received from the OCC a certificate of authority to carry on a “banking business,” pursuant to 12 U.S.C. §§ 24 & 27; and (iii) is entitled to become a member of the Federal Reserve System under 12 U.S.C. §§ 282 & 287. Operating subsidiaries do *not* qualify as “national banks” under Sections 221 and 221a, because they are chartered as *nonbank* corporations under *state* law, they do *not* receive certificates of authority from the OCC to carry on a “banking business,” and they *cannot* become a member of the Federal Reserve System. Accordingly, operating subsidiaries *cannot* rely on any preemptive authority that the OCC may lawfully exercise with respect to “national bank[s]” under Section 484.

The foregoing conclusion is further supported by Section 221a(b), which defines “affiliate” to include “any corporation” which controls or *is controlled by* a national bank. Thus, operating subsidiaries are “affiliates” of their parent banks for purposes of the FRA – including Section 484 – and have a separate corporate status from their parent banks. The FRA makes this point absolutely clear in 12 U.S.C. §§ 371c & 371c-1, which govern transactions between member banks and their “affiliates.” For purposes *only* of those two sections, operating subsidiaries of national banks are *specifically exempted* from being treated as “affiliates” of their parent banks, unless the *Federal Reserve Board* determines otherwise. See 12 U.S.C. §§ 371c(b)(2)(A) & 371c-1(d)(1).

The OCC’s argument ignores the careful distinction that Section 221a draws between a “national bank” and its “affiliates,” a distinction that includes *all* subsidiaries controlled by the bank. The OCC’s assertion that Section 484 applies to operating subsidiaries must therefore be rejected in light of well-established principles of statutory construction. See, e.g., *American Textile Mfrs. Institute, Inc. v. Donovan*, 452 U.S. 490, 513 (1981) (rejecting a proposed interpretation that would render one provision of the statute “nugatory, thereby offending the well-settled rule that all parts of a statute, if possible, are to be given effect”); *Bd. of Governors v. Investment Co. Institute*, 450 U.S. 46, 58-59 n.24 (1981) (holding that the term “bank,” as used in 12 U.S.C. §§ 24 (Seventh) & 378, “cannot be read to include within its prohibition separate organizations related by ownership with a bank,” because (i) “the structure of the [Glass-Steagall] Act reveals a congressional intent to treat banks separately from their affiliates,” and (ii) “the reading of the Act urged by respondent would render § 20 meaningless”); *Independent Ins. Agents of America, Inc. v. Hawke*, 211 F.3d 638, 644-45 (D.C. Cir. 2000).

It is very significant that Section 481 – also part of the FRA– authorizes the OCC to examine “affiliates” of a national bank “as shall be necessary to disclose fully the relations between such bank and such affiliates and the effect of such relations on the affairs of such bank.” In view of the definition of “affiliates” in Section 221a(b), the OCC’s examination authority under Section 481 clearly extends to operating subsidiaries of national banks. By contrast, the limitations on “visitorial powers” established by Section 484 apply only to “national bank[s].” Since Congress has expressly included the term “affiliates” in Section 481 and *failed* to include that term in Section 484, the only reasonable construction is that the limitations on “visitorial powers” under Section 484 do *not* extend to operating subsidiaries and other “affiliates” of national banks. See *Chicago v. Environmental Defense Fund*, 511 U.S. 328, 338 (1994) (holding that it is “generally presumed that Congress acts intentionally and purposely” when “it includes particular language in one section of a statute but omits it in another”)

(quoting *Keene Corp. v. United States*, 508 U.S. 200, 208 (1993)). Accordingly, state officials are free to exercise all “visitorial powers” over operating subsidiaries that they possess under applicable state laws.¹³

13 In adopting Section 7.4006 in 2001, the OCC attempted to rely on a similar rule promulgated by the Office of Thrift Supervision (“OTS”) with regard to operating subsidiaries of federal thrifts. The OCC noted that a federal district court and a state appellate court had upheld the OTS’ claim that its rule preempted the authority of states to regulate operating subsidiaries of federal thrifts. 66 Fed. Reg. at 34789. CSBS does *not* concede the legality of the OTS’ operating subsidiary rule or the correctness of the two court decisions upholding that rule. In any event, the OCC cannot defend its claim of “exclusive visitorial authority” over operating subsidiaries of national banks by referring to the OTS’ regulatory authority under the Home Owners’ Loan Act of 1933, 12 U.S.C. § 1461 et seq. (“HOLA”). The courts have repeatedly held that the scope of federal preemption created by HOLA is far broader than that established by the NBA. For example, in *People v. Coast Federal Savings & Loan Ass’n*, 98 F. Supp. 311 (S.D. Cal. 1951), the court held that HOLA “preempted the field” with regard to “the creation, operation and supervision of federal savings and loan associations,” and that HOLA empowered the OTS’ predecessor agency to issue “comprehensive rules and regulations concerning the powers and operations of every Federal savings and loan association from its cradle to its corporate grave.” *Id.* at 318, 316. The court also declared that the preemptive reach of HOLA was far greater than that of the NBA:

‘[A] building and loan association organized under [HOLA] is not a national bank and the powers and duties of the two materially differ.’ *As to national banks, Congress expressly left open a field of state regulation and the application of state laws; but as to federal savings and loan associations, Congress made plenary, preemptive delegation to the [OTS’ predecessor] to organize, incorporate, supervise and regulate, leaving no field for state supervision.*

Id. at 319 (emphasis added) (citing, inter alia, *Luckett*). The sharp distinction made in *Coast Federal* as to the different preemptive scopes of HOLA and the NBA is highly significant, because subsequent cases have relied on the “cradle to grave” language of *Coast Federal* in affirming sweeping exercises of preemptive power by the OTS and its predecessor. See, e.g., 458 U.S. 141, 144-45 (1982); *Conference of Federal Savings & Loan Ass’ns v. Stein*, 604 F.2d 1256, 1260 (9th Cir. 1979), *aff’d mem.*, 445 U.S. 921 (1980); *Bank of America v. City and County of San Francisco*, 309 F.3d 551 (9th Cir. 2002) (slip op. at 11). In the latter case, the Ninth Circuit applied a “field preemption” analysis under HOLA but followed a much narrower “conflict preemption” analysis under the NBA. See *id.* (slip op. at 11-26).

Section 5(a) of HOLA, 12 U.S.C. § 1464(a), grants broad authority to the OTS to regulate federal thrifts based on what it determines to be the “best practices” for thrift institutions. In contrast, as shown by the discussion in Part C below with regard to 12 U.S.C. § 93a, the OCC does *not* possess any similar power to issue preemptive rules. The courts have recognized this clear difference between the scope of authority granted to the OTS and the much more circumscribed power conferred on the OCC. See *North Arlington National Bank v. Kearny*

The OCC's interpretation of Section 484 is also contrary to a recent federal district court decision, which *rejected* the OCC's argument that operating subsidiaries of national banks are "indistinguishable" from their parent bank and therefore fall within the "exclusive jurisdiction" of the OCC. In *Minnesota v. Fleet Mortgage Corp.*, 181 F. Supp. 2d 995, 999-1001 (D. Minn. 2001), the court determined that an operating subsidiary engaged in mortgage lending was *not* a "bank" for purposes of Section 133 of GLBA, 113 Stat. 1383 (reprinted in 15 U.S.C.A. § 41 note). Based on that finding, the district court held that (i) the OCC did *not* have "exclusive jurisdiction" to enforce laws applicable to the operating subsidiary, and (ii) the operating subsidiary was therefore subject to the shared enforcement jurisdiction of the FTC and the states with respect to violations of the FTC's Telemarketing Sales Rule ("TSR"). In rejecting the OCC's claim of "exclusive jurisdiction," the court held:

The OCC's insistence that it must have exclusive jurisdiction over [operating] subsidiaries in order to avoid having its authority 'restricted' is not persuasive. . . . Congress simply chose *not* to provide exclusivity to the OCC in the GLBA. *There is no direct authority establishing exclusive jurisdiction over national bank operating subsidiaries*, and . . . there is no compelling reason to believe that allowing [the FTC and the states to exercise] concurrent jurisdiction would 'produce a result demonstrably at odds with the intentions of [Congress]'.

Id. at 1001-02 (emphasis added; citations and footnotes omitted). The court held that Section 133(a) of GLBA – which incorporates the definition of "bank" contained in Section 3 of the Federal Deposit Insurance Act ("FDIA"), 12 U.S.C. § 1813 – was "unambiguous" and "simply does not include subsidiaries of banks." The court also concluded that an operating subsidiary "fits precisely into the category of entities described by the language of § 133 as an entity controlled by a bank that is *not itself a bank* according to the prescribed definition." *Id.* at 1000 (emphasis added).

The definitions of "bank" and "affiliate" in Section 221a of the FRA are substantively identical to the definitions of the same terms in Section 3 of the FDIA. Compare 12 U.S.C. § 221a with *id.* §§ 1813(a)(1)(A) & (w)(6) (incorporating the definition of "affiliate" set forth in *id.* § 1841(k)). Thus, the holding in *Fleet Mortgage* as to the meaning of "bank" in Section 3 of

Federal Savings & Loan Ass'n, 187 F.2d 564, 565-66 (3d Cir.) (holding that (i) Section 5(a) gave the OTS' predecessor "authority to make policy" allowing federal thrifts to branch without regard to state law, and (ii) the NBA could *not* be used as an "analogy" in determining the scope of authority granted under HOLA, because of "the historical reasons back of the establishment of national banks and the altogether different type of administrative control exerted over them"), *cert. denied*, 342 U.S. 816 (1951); *Long*, 630 F.2d at 989 (stating that "federal regulation of federal savings and loan associations . . . is distinct from the supervision of national banks by the [OCC] and . . . federal savings and loan associations do not have the lengthy history of dual regulation that characterizes the national banking system"). Accordingly, the OTS' operating subsidiary rule does *not* provide any persuasive legal basis, by analogy or otherwise, for the OCC's claim of "exclusive visitorial authority" over operating subsidiaries of national banks.

the FDIA directly refutes the OCC's claim that it can treat operating subsidiaries in the same manner as "national banks" for purposes of Sections 221a and 484 of the FRA. The OCC accordingly has no authority under Section 484 to prevent state officials from exercising all "visitorial powers" that they possess over operating subsidiaries under applicable state laws.¹⁴

The OCC's proposed application of Section 7.4000 to operating subsidiaries also contravenes fundamental principles of state corporate law, which establish a strict separation between subsidiaries and their parent companies. The OCC's assertion that it can ignore the legal separation principles established by state corporate law is refuted by numerous Supreme Court decisions, in which the Court has insisted on interpreting federal statutes in harmony with established doctrines of state corporate law. For example, in *United States v. Bestfoods*, 524 U.S. 51 (1998), the Supreme Court held that a parent corporation can be held liable for its subsidiary's alleged violation of a federal pollution law ("CERCLA") *only if* federal authorities succeed in "piercing the corporate veil" between the parent and the subsidiary based on *principles of state corporate law*. The Supreme Court's decision in *Bestfoods*, which defined CERCLA liability based on corporate separation principles established by state law, is consistent with other decisions in which the Supreme Court has *refused* to interpret federal statutes in a manner that conflicts with fundamental tenets of state corporate law.¹⁵

The federal banking laws do *not* contain any expression of congressional intent to obliterate the "bedrock principle" of state corporate law that establishes a clear separation between a parent corporation and its subsidiaries. On the contrary, as shown above, Congress expressly recognized the distinct corporate status of a national bank and each of its "affiliates" (*including* its operating subsidiaries) in 12 U.S.C. §§ 221a, 1813(a)(1)(A) & (w)(6). Congress chose to qualify the separate status of operating subsidiaries only in one area, by providing *specific exemptions* that apply *only* to the affiliate transaction rules in 12 U.S.C. §§ 371c & 371c-1. Congress did not include any such qualification in Section 484, and therefore the limitations on "visitorial powers" under that statute cannot be applied to operating subsidiaries or other

¹⁴ A recent federal district court decision in California concluded that an operating subsidiary of a national bank had shown "probable success on the merits" with respect to its claims that the NBA preempted a state agency's authority to (i) prohibit the subsidiary from engaging in real estate lending in California, or (ii) exercise "visitorial powers" over the subsidiary. *Wells Fargo Bank, N.A. v. Boutris*, 2003 U.S. Dist. LEXIS 4192, at *19-*20 (E.D. Cal., Mar. 10, 2003). CSBS notes that no final decision has been rendered and the case continues to be litigated. In addition, for the reasons set forth in this letter, CSBS maintains that the preliminary *Boutris* decision is clearly erroneous and should *not* be followed by the OCC in determining whether to adopt the proposed amendments to Section 7.4000.

¹⁵ E.g., *CTS Corp. v. Dynamics Corp. of America*, 481 U.S. 69, 85 (1987) (refusing to construe a federal statute governing tender offers in a manner that "would pre-empt a variety of state corporate laws of hitherto unquestioned validity"); *Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 479 (1977) (rejecting an interpretation of "the federal securities laws [that] would overlap and quite possibly interfere with state corporate law").

“affiliates” of national banks.

Moreover, the OCC has itself relied on state-law principles of corporate separation in presenting legislative proposals to Congress. During congressional hearings on GLBA, the OCC invoked the corporate separation doctrine (including the judicial reluctance to “pierce the corporate veil”) as support for its argument that Congress should *not* be concerned about the possibility that “banks would end up being liable for the debts of their subsidiaries – beyond their own investment and loans.” Based on these representations by the OCC, Congress clearly understood that national banks and their subsidiaries *are* separate and distinct corporate entities. H.R. Rep. No. 106-74 (1999) (pt. 1), at 101. Accordingly, there is simply no congressional mandate that would allow the OCC to disregard the separate corporate status of operating subsidiaries and treat them as “national banks” for purposes of Section 484. Furthermore, according to the *Bestfoods* decision, “piercing the corporate veil” between the national bank and its operating subsidiaries could place significant subsidiary liability on national banks, of which the ramifications to both the financial system and FDIC insurance fund could be drastic.

The OCC’s proposal to assert exclusive “visitorial powers” over operating subsidiaries would deprive the states of their authority to license, examine and regulate the activities of *state-chartered* corporations. Indeed, by claiming that the OCC has exclusive “visitorial powers” over national banks’ operating subsidiaries, the proposed amendments to Section 7.4000 would bar the states from inspecting, examining, licensing or exercising any regulatory supervision over those entities they are expected to create and charter. This clearly disregards any previously accepted fundamental powers of corporate regulation. Contrary to the OCC’s proposal, the courts have repeatedly struck down similar attempts to rely on federal agency rules as a basis for infringing – *without* congressional authorization – upon the states’ power to regulate the internal affairs and business operations of state-chartered corporations. For example, in *Santa Fe v. Green*, 430 U.S. at 479, the Supreme Court rejected the respondents’ broad interpretation of Rule 10b-5 of the Securities and Exchange Commission (“SEC”), because “[a]bsent a clear indication of congressional intent, we are reluctant to federalize the substantial portion of the law of corporations that deals with transactions in securities, particularly where established state policies of corporate regulation would be overridden.” Similarly, in *Business Roundtable v. SEC*, 905 F.2d 406 (D.C. Cir. 1990), the court invalidated Rule 19c-4 of the SEC, because that rule would “overturn or at least impinge severely on the tradition of state regulation of corporate law” and “nothing in the statute and legislative history suggests so broad a [congressional] purpose.” *Id.* at 412, 415.

The courts have consistently upheld the authority of the states “to create corporations, to prescribe their powers, and to define the rights that are acquired by purchasing their shares.” *CTS Corp.*, 481 U.S. at 91. “[T]he powers of corporations . . . are such and such only as are conferred upon them by the acts of the legislatures of the several States under which they are organized.” *Oregon Railway & Navigation Co. v. Oregonian Railway Co.*, 130 U.S. 1, 20 (1889). The OCC’s proposal to extend Section 7.4000 to operating subsidiaries would override these fundamental powers of corporate regulation that are reserved to the states under our federal system. The proposal would effectively “federalize” state-chartered operating subsidiaries by placing them within the sole supervisory control of the OCC, based on the OCC’s assertion of

“exclusive visitorial authority” over such subsidiaries. 63 Fed. Reg. at 6369. The Supreme Court has held that the federal government intrudes upon state sovereignty and exceeds the boundaries of its authority under the Tenth Amendment when it attempts to convert state-chartered corporations into creatures of federal law without the permission of the chartering states.¹⁶ The OCC’s proposal to extend Section 7.4000 to operating subsidiaries of national banks must therefore be withdrawn, because any regulation embodying that proposal would raise extremely serious constitutional issues under the Tenth Amendment.

B. The OCC Must Make Several Changes in Its Proposed Revisions to Section 5.33.

1. Opportunity for Public Comment and Hearing

Proposed Section 5.33(f) would exempt applications by national banks to merge with their nonbank affiliates from the procedural requirements of 12 C.F.R. §§ 5.10 & 5.11, unless the OCC determines that the “application presents significant and novel policy, supervisory or legal issues. Sections 5.10 and 5.11 permit members of the public to submit comments and request hearings on merger applications involving national banks. Thus, the proposed terms of Section 5.33(f) would *deny* to members of the public any ability to participate in the application process for mergers between national banks and their nonbank affiliates *unless* the OCC exercised its discretion to allow such participation in individual cases.

CSBS strongly urges the OCC to remove this exemption from Section 5.33(f). As the OCC recognized in its Notice of Proposed Rulemaking, 63 Fed. Reg. at 6364-65, national banks did *not* have authority to merge with nonbank organizations of any type before Congress enacted 12 U.S.C. § 215a-3 at the end of 2000. Section 215a-3 provides authority for national banks to merge with their “nonbank subsidiaries or affiliates,” subject to important qualifications discussed below. Mergers between national banks and nonbank affiliates are therefore unprecedented, and such transactions are likely to raise many important legal and policy issues implicating bank supervision, bank safety and soundness, and the general public interest.

Accordingly, members of the public must be afforded the opportunity to submit comments and request hearings with respect to all mergers between national banks and nonbank affiliates authorized under Section 215a-3. The OCC has not articulated any persuasive rationale for excluding the public from participating in these unprecedented transactions of great potential significance.

¹⁶ *Hopkins Federal Savings & Loan Ass’n v. Cleary*, 296 U.S. 315 (1935) (striking down Section 5(i) of the Home Owners’ Loan Act of 1933, because it permitted state-chartered savings institutions to convert to federal charters without state permission); *Chicago Title & Trust Co. v. 4136 Wilcox Bldg. Corp.*, 302 U.S. 120 (1937) (holding that Section 77B of the federal Bankruptcy Act did not authorize the filing of a bankruptcy petition on behalf of a corporation whose charter had expired under state law, because such any such filing would create “an intrusion by the Federal Government on the powers of the State” and would create serious problems under the Tenth Amendment as construed in *Hopkins*).

2. Requirement for FDIC Approval under Section 1828(c)(1)(A)

Section 215a-3(b)(1) states that nothing contained in that section “shall be construed . . . to affect the applicability of [12 U.S.C. §] 1828” to mergers between national banks and their nonbank affiliates. Under Section 1828(c)(1)(A), an “insured depository institution” may *not* “merge or consolidate with any noninsured bank or institution” *unless* the bank receives “the prior written approval” of the FDIC. Section 1828(c)(1)(A) would clearly apply to any merger between an FDIC-insured national bank and its nonbank affiliate. The national bank would be an “insured depository institution” under Section 1813(c)(2), and the nonbank affiliate would be a “noninsured . . . institution” for purposes of Section 1828(c)(1)(A). The FDI Act defines “depository institution” to include “any bank or savings association,” under Section 1813(c)(1). The use of the broader term “institution” in Section 1828(c)(1)(A) therefore clearly indicates the intent of Congress to regulate mergers between insured banks and noninsured entities that were *not* “depository institutions.” In addition, proposed Section 5.33(g)(4)(v) refers to a nonbank affiliate as an “institution participating in the merger.” Therefore, the OCC appears to recognize that a nonbank affiliate would be treated as a “noninsured . . . institution” under Section 1828(c).

Accordingly, the OCC must revise Section 5.33 by specifying that a proposed merger between an insured national bank and its nonbank affiliate must receive the prior written approval of the FDIC. Any omission of this requirement from Section 5.33 would not be in keeping with Section 215a-3(b)(1), and it could also potentially mislead national banks and their nonbank affiliates as to their responsibilities under Section 1828(c).

3. Required Changes to Section 5.33(g)(4)(v)

Proposed Section 5.33(g)(4)(v) provides that, upon the consummation of a merger between a national bank and a nonbank affiliate that results in a national bank, “[t]he corporate existence of each institution participating in the merger shall be continued in the resulting national bank, and all the rights, franchises, property, appointments, liabilities, and other interests of the participating institutions shall be transferred to the resulting national bank, as set forth in 12 U.S.C. 215a(a), (e), and (f), in the same manner and to the same extent as in a merger between a national bank and a state bank under 12 U.S.C. 215a(a), as if the nonbank affiliate were a state bank.” This statement is technically correct, but it omits a very important qualification. This qualification is contained in Section 215a-3(b)(2), which provides that “[n]othing in this section shall be construed . . . to grant a national banks any power or authority that is not permissible for a national bank under other applicable provisions of law.” In view of this explicit congressional limitation, the OCC must change Section 5.33(g)(4)(v) to provide that a national bank resulting from a merger with a nonbank affiliate may not exercise any power or engage in any activity that would not be permissible for a national bank under applicable provisions of federal law *other than* Section 215a-3.

The statutory limitation on the powers of national banks resulting from mergers under Section 215a-3 is consistent with judicial interpretations of Sections 215 and 215a. Those sections govern consolidations and mergers between state banks and national banks in which the

resulting bank is a national bank. The courts have made clear that the resulting national bank in each such transaction has authority to exercise only those powers that a national bank is permitted to exercise under applicable provisions of federal law. For example, in *Fidelity-Baltimore National Bank v. United States*, 328 F.2d 953 (4th Cir.), *cert. denied*, 379 U.S. 823 (1964), the court reviewed a transaction in which a state bank and a national bank consolidated into a national bank pursuant to Section 215. The court pointed out that

[Section 215 requires] that the resulting corporation shall operate under the charter of the national bank. Pursuant to that requirement, *the state charter is necessarily abandoned, and it is plain that the resulting national bank may not thereafter conduct its business in violation of federal law* though in accordance with what state banks may do under state law. Though the consolidated national bank succeeds under the statute to all of the state created rights of the state bank constituent, state laws subsequently adopted may neither enlarge nor detract from such rights. In the nature of things, *the consolidated national bank could not remain subject to state regulation which was incompatible with federal requirements.*

328 F.2d at 956-57 (emphasis added). The court further explained that Section 215 permits the “absorption of the state institution with all its assets, by the national bank, which succeeds to all the rights, property, franchises, interests and powers of the state institution, *so far as the exercise of them is permitted by federal legislation.*” *Id.* at 959 (emphasis added).

Similarly, in *Commissioner v. Morris Trust*, 367 F.2d 794 (4th Cir. 1966), the court held that a state bank was required to divest its state-authorized insurance agency business before it could merge with and into a national bank under Section 215a. Given the restrictions on the insurance activities of national banks set forth in 12 U.S.C. § 92, the national bank resulting from the merger was prohibited under federal law from continuing to carry on the state bank’s insurance business. Accordingly, the court explained, the state bank’s insurance department was a substantial impediment to the accomplishment of the merger, for a national bank is prohibited from operating an insurance department except in towns having a population of not more than 5,000. *To avoid a violation of the national banking laws, therefore, and to accomplish the merger under [the surviving bank’s] national charter, it was prerequisite that [the state bank] rid itself of its insurance business.*

367 F.2d at 795 (emphasis added; footnote omitted).

Thus, judicial interpretations of Section 215 and 215a make clear that a national bank resulting from a merger under Section 215a-3 may *not* engage in any activities that would be impermissible for a national banks under applicable provisions of federal law. The OCC may not have ignore this restriction and thereby enlarge the congressionally-authorized powers of national banks. It is well established that national banks, being creatures of federal law, may only exercise the powers that are granted to them by Congress. E.g., *Texas & Pacific Railway Co. v. Pottorff*, 291 U.S. 245, 253-54 (1934); *St. Louis*, 263 U.S. at 656-59. In addition, the OCC may not unilaterally expand the powers of national banks pursuant to its general

rulemaking authority under 12 U.S.C. § 93a. Section 93a only permits the OCC to issue regulations “to carry out the responsibilities of [its] office.” When Section 93a was enacted in 1982, Congress made clear that the OCC’s rulemaking authority thereunder

... is only available to carry out the responsibilities of the [OCC] and *carries with it no new authority to confer on national banks powers which they do not have under existing substantive law*. To give national banks authority under this rulemaking provision that they do not possess under existing substantive law would not be carrying out the responsibilities of the [OCC] since *only Congress can define those responsibilities so as to confer powers on national banks*.¹⁷

Based on the terms and legislative history of Section 93a, a federal appellate court has stated that Section 93a “grants no new substantive powers to [national] *banks*,” and Section 93a therefore does not allow the OCC to “authorize activities that run afoul of federal laws governing the activities of national banks.” *CSBS v. Conover*, 710 F.2d 878, 885 (D.C. Cir. 1983) (emphasis in original).

In view of the foregoing authorities, the OCC must change Section 5.33(g)(4)(v) to provide that the resulting national bank may not exercise any power or engage in an activity that would not be permissible for a national bank under applicable provisions of federal law *other than* Section 215a-3. This is a very important qualification for at least two reasons. First, it is conceivable that a national bank might elect to merge with a financial subsidiary. As noted above in Part B(4), financial subsidiaries are permitted, under 12 U.S.C. § 24a, to engage in certain activities that are *not* permissible for national banks. It would be entirely contrary to the purposes of GLBA if the OCC interpreted Section 215a-3 to permit a national bank to acquire impermissible powers simply by merging with its financial subsidiary.

Second, GLBA permits the FRB and the Treasury Department to authorize by joint action, beginning in November 2004, financial subsidiaries of national banks to engage in merchant banking activities. See 12 U.S.C. § 1843(k)(7)(B). Any such grant of merchant banking authority would permit financial subsidiaries of national banks to acquire controlling interests in nonfinancial companies, with the potential result that such nonfinancial companies could arguably be deemed “affiliates” of national banks. See *id.* § 1843(k)(4)(H). Again, it would violate GLBA’s policy of maintaining the separation of banking and commerce if the OCC interpreted Section 215a-3 to permit a national bank to engage in unrestricted commercial activities by merging with a nonfinancial company that was controlled by its financial subsidiary.

¹⁷ 126 Cong. Rec. 6902 (1980) (remarks of Sen. Proxmire, Senate floor manager for the 1982 legislation). See also H.R. Rep. No. 96-842 (Conf. Rep.), at 83, reprinted in 1980 U.S. Code Cong. & Ad. News 298, 313 (stating that Section 93a “carries no authority to permit otherwise impermissible activities of national banks with specific reference to the provisions of the McFadden Act and the Glass-Steagall Act”); 126 Cong. Rec. 6971 (1980) (identical statement by Rep. St Germain, House floor manager for the 1982 legislation).

4. Required Changes to Section 5.33(g)(5)(v)

Proposed Section 5.33(g)(4)(v) provides that, upon consummation of a merger between an uninsured national bank and a nonbank affiliate that results in a nonbank company, “[t]he corporate existence of each entity participating in the merger shall be continued in the resulting nonbank affiliate, and all the rights, franchises, property, appointments, liabilities and other interests of the participating national bank shall be transferred to the resulting nonbank affiliate as set forth in 12 U.S.C. 214b, in the same manner and to the same extent as in a merger between a national bank and a state bank under 12 U.S.C. 214a, as if the nonbank affiliate were a state bank.” This statement is technically correct as far as it goes, but it omits three very important qualifications. First, the resulting nonbank company is not a national bank and therefore may not exercise any powers or engage in any activities based on authority granted to national banks under federal law. Second, the resulting nonbank company may exercise only those powers and engage in only those activities that are permissible for nonbank companies under applicable state laws, and it may not conduct any business for which a bank charter is required under either federal or state law. Third, the resulting nonbank company must comply with all licensing requirements, supervisory directives and other regulations prescribed by applicable state laws.

When a national bank merges into a state bank pursuant to Section 214a, Section 214b provides that the “franchise” of the disappearing national bank “shall automatically terminate . . . and the resulting State bank shall be considered the same business and corporate entity as the national banking association, although as to rights, powers and duties the resulting bank is a State bank.” Thus, Section 214b makes clear that the resulting state bank in a merger under Section 214a gives up any “rights, powers and duties” that the disappearing national bank may have possessed under its federal “franchise.” Section 214b further requires the resulting bank to derive all authority for its business activities from its status as a state bank organized under state law. In the Notice of Proposed Rulemaking, the OCC apparently recognized the legal importance of Section 214b in applying the provisions of Section 215a-3. The OCC stated that, when an uninsured national bank merges into a nonbank affiliate under Section 215a-3, the disappearing national bank must “surrender its national charter but [may] continue conducting lines of business that are authorized for the nonbank affiliate.” 68 Fed. Reg. at 6366. This conclusion is further mandated by 12 U.S.C. §§ 21-24 & 26-27, which prohibit any association from carrying on the “business of banking” under authority of the NBA unless the organizers have filed the required organization certificate and the OCC has issued a certificate of authority allowing the association to commence the “business of banking.”

Given these clear statutory commands, the OCC must revise Section 5.33(g)(5)(v) to stipulate that the resulting nonbank company may not exercise any powers or engage in any activities based on authority that the disappearing national bank possessed under federal law. In addition, Section 5.33(g)(5)(v) must specify that the resulting nonbank company may not engage in any activity which is impermissible for a nonbank company under applicable state law, or for which a bank charter is required under applicable federal or state law. For example, 12 U.S.C. § 378(a)(2) prohibits any person from engaging in “the business of receiving deposits subject to check or to repayment upon presentation of a pass book, certificate of deposit, or other evidence of debt, or upon request of the depositor,” unless that person has received a valid charter to

engage in a deposit-taking business from the federal government or a state or territorial government. Most states have enacted similar laws prohibiting persons from engaging in the business of accepting deposits or acting as a fiduciary unless such persons have obtained the requisite banking charter under federal or state law. Since, as the OCC has acknowledged, a merger under Section 5.33(g)(5) requires the disappearing national bank to “surrender its charter” (68 Fed. Reg. at 6366), the surviving nonbank company no longer has any authority, power or status to conduct business as a “bank” under either federal or state law.

Finally, Section 5.33(g)(5) must provide that the resulting nonbank company is required to comply with all restrictions on permitted activities, licensing requirements, supervisory directives and other regulations prescribed by applicable state laws. As discussed above in Part A(4), it is an “established doctrine” of our federal system that “the powers of [state-chartered] corporations are such and such only as are conferred upon them by the acts of the legislatures of the several States under which they are organized. . . . [S]uch a corporation can exercise no power or authority which is not granted to it by the charter under which it exists, or by some other act of the legislature which granted that charter.” *Oregon Railway & Navigation Co.*, 130 U.S. at 20, 21. In addition, there is no question that each state “is legitimately concerned with safeguarding the interests of its own people in business dealings with corporations not of its own chartering but who do business within its borders.” *Union Brokerage Co. v. Jensen*, 322 U.S. 202, 208 (1944). As a consequence, “a State may impose non-discriminatory regulations on those engaged in foreign commerce ‘for the purpose of ensuring the public safety and convenience; . . . a license fee no larger in amount than is reasonably required to defray the expense of administering the regulations may be demanded.’” *Id.* at 211-12 (citation omitted). Accordingly, the OCC’s regulations governing mergers under Section 5.33(g)(5) must inform nonbank companies resulting from such mergers that they are obligated to comply with all applicable state laws and regulations.

C. The OCC Must Comply with Executive Order 13132 in Determining Whether to Adopt Its Proposed Rules, Because Those Rules Have Important “Federalism Implications”.

Although the OCC noted that the proposed rulemaking *may* have Federalism implications, the proposed amendments to Sections 7.4000 and 5.33 have *significant* “federalism implications” and therefore require the OCC to comply with Executive Order 13132, 64 Fed. Reg. 43255 (Aug. 10, 1999). The OCC is therefore required to follow all applicable procedures of E.O. 13132 before issuing a final rule. For example, Section 3(d) provides that “in determining whether to establish uniform national standards, [an agency shall] consult with appropriate State and local officials as to the need for national standards and any alternatives that would limit the scope of national standards or otherwise preserve State prerogatives and authority.” *Id.* at 43256. In addition, under Section 4(d), “[w]hen an agency foresees the possibility of a conflict between State law and Federally protected interests within its area of regulatory responsibility, the agency shall consult, to the extent practicable, with appropriate State and local officials to avoid such a conflict.” Similarly, Section 6(c) provides that “no agency shall promulgate any regulation that has federalism implications and that preempts State

law unless the agency . . . consulted with State and local officials *early in the process of developing the proposed regulation.*” 68 Fed. Reg. at 43258 (emphasis added).¹⁸

CSBS maintains that the OCC has *not* satisfied its obligations to consult with the responsible state officials concerning this proposed rule or National City’s request for preemption of the Georgia Fair Lending Act. The OCC did not notify CSBS or state officials about its proposed rule until the day it was released to the public. In addition, although OCC officials recently met with CSBS staff at our request to discuss this proposal, the OCC has not initiated any consultations with CSBS or state officials (based on discussions with the state banking department heads) to discuss the serious adverse effects of a promulgating a similar rule as proposed. CSBS calls upon the OCC to postpone any decision on promulgating a final rule until the OCC has fully complied with its responsibilities under E.O. 13132.

¹⁸ If the OCC approves National City’s request, its approval would establish a decisional rule applicable to all national banks (and operating subsidiaries thereof) doing business in Georgia. Accordingly, whether the OCC chooses to designate such an approval as a “rule” or an “order,” the OCC’s action would clearly constitute a “regulation” within the scope of Section 6(c) of E.O. 13132. See *Ford Motor Co. v. FTC*, 673 F.2d 1008, 1009 (9th Cir. 1981) (holding that a federal agency must issue regulations in accordance with the “rulemaking” procedures specified in 5 U.S.C. § 553, if the agency “seeks to change the law and establish rules of widespread application”), *cert. denied*, 459 U.S. 999 (1982).

CSBS commends the OCC's ongoing efforts to improve the national bank charter. However, we hope that you will consider the public policy issues and concerns that we have raised in this letter. CSBS stands ready to meet with you and your staff in an effort to resolve these issues.

Best personal regards,

A handwritten signature in black ink that reads "Neil Milner". The signature is written in a cursive, flowing style.

Neil A. Milner, CAE
President and CEO