19-4271-cv

United States Court of Appeals

for the

Second Circuit

LINDA A. LACEWELL, in her official capacity as Superintendent of the New York State Department of Financial Services,

Plaintiff-Appellee,

– v. –

OFFICE OF THE COMPTROLLER OF THE CURRENCY, JOSEPH M. OTTING, in his official capacity as U.S. Comptroller of the Currency,

Defendants-Appellants.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF OF *AMICUS CURIAE* CONFERENCE OF STATE BANK SUPERVISORS IN SUPPORT OF APPELLEE AND AFFIRMANCE

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INTEREST OF AMICUS CURIAE[1]

Amicus Conference of State Bank Supervisors ("CSBS") is the nationwide organization of state banking and financial regulators from all 50 states, American Samoa, the District of Columbia, Guam, Puerto Rico, and the U.S. Virgin Islands. CSBS's members charter and supervise state banks and license and regulate a wide range of nondepository financial institutions, including mortgage and consumer finance companies and money transmission companies. Since 1902, CSBS has played a crucial role in the preservation of the dual-banking system by representing the collective policy interests of its members at the federal level. It also facilitates regulatory and supervisory coordination and collaboration on a state-to-state and state-to-federal basis. CSBS also serves as the administrator of the Nationwide Multistate Licensing System ("NMLS"), the system of record for state nonbank licensing. Initially developed as state-based licensing platform, NMLS was codified

[1] Both parties have consented to CSBS's filing this brief. Neither party's counsel authored this brief in whole or in part, and no person other than *amicus curiae* made a monetary contribution toward its preparation or submission.

into federal law in the Secure and Fair Enforcement for Mortgage Licensing Act of 2008.

SUMMARY OF ARGUMENT

This Court should affirm the lower court decision and hold that the Office of the Comptroller of the Currency ("OCC") lacks authority to create a special-purpose national bank charter for nondepository financial institutions (the "Fintech Charter Decision").

First, DFS has standing and its claims are constitutionally ripe because the Fintech Charter Decision caused an injury-in-fact to DFS's legally protected interest in the balance of federal and state power in the dual banking system. Because OCC has circumvented the process for active companies to switch to national charters and its approach retroactively deprives states of their supervisory authority, DFS is actually injured even before a charter is granted. Further, additional injury to DFS is certainly impending.

Second, DFS's claims are prudentially ripe because this case presents a purely legal issue—whether engaging in receiving deposits is necessary for national banks—and no additional facts are necessary to

resolve that issue. Moreover, there will be hardship to DFS and other state regulators from withholding review, but no hardship to OCC.

Third, the National Bank Act, Title LXII of the Revised Statutes (codified, at 12 U.S.C. § 21 *et seq*.) ("NBA") cabins OCC's authority to charter national banks for the purpose of carrying on the business of banking. Carrying on the "business of banking" under the NBA unambiguously requires engaging in receiving deposits because other federal banking laws, including the Federal Reserve Act ("FRA"), 12 U.S.C. §§ 221 et. seq., and the Federal Deposit Insurance Act ("FDIA"), 12 U.S.C. §§ 1811 et. seq., require national banks to be depository institutions to lawfully commence the business of banking. Since these laws govern the formation of national banks, they must inform the meaning of the "business of banking" in the NBA chartering provisions.

Fourth, OCC's reliance on the definition of "branch" to define the "business of banking" creates asymmetry between the NBA chartering and location provisions, contravenes the very reason that Congress separated the three functions in the branch definition by adopting "or," and conflicts with judicial precedent and the constitutional basis of the NBA.

ARGUMENT

I. OCC's Disruption of the Dual-Banking System Has Caused Actual Harm to DFS and Other State Banking Regulators, and Additional Harm is Imminent.

A. OCC's regulatory interference with DFS has already caused a particularized injury.

DFS and CSBS's other members have successfully overseen and regulated nonbank companies for more than a century. States generally require nondepository institutions to obtain a license to engage in regulated financial activities, impose product restrictions like limitations on interest rates and finance charges, and regulate business conduct through protections like net worth requirements and restrictions on customer communications. The NBA preempts the application of many of these state consumer protection laws to national banks. *See* 12 U.S.C. §§ 25b, 85; 12 C.F.R. §§7.4001, 7.4002, 7.4007, 7.4008, 34.4.

Additionally, national banks are subject exclusively to the supervisory authority of OCC to enforce any state law not preempted by the NBA and, thus, the powers of the states to supervise national banks for compliance with respect to these laws is itself preempted. *See* 12 U.S.C. § 484; 12 C.F.R. § 7.4000. To enable state-regulated nondepository institutions to take advantage of this broad preemptive framework, OCC

has created the Fintech Charter, thereby improperly extending its regulatory reach into traditional areas of state concern.

The U.S. Supreme Court has long recognized that state bank regulators have a legally protected, quasi-sovereign interest in the balance of federal and state power in the dual-banking system. *See e.g., Hopkins Federal Sav. & Loan Assoc. v. Cleary*, 296 U.S. 315, 337 (1935); *see also Nuesse v. Camp*, 385 F.2d 694, 700 (D.C. Cir. 1967) ("a state official directly concerned in effectuating the state policy has an 'interest' in a legal controversy involving the Comptroller which concerns the nature and protection of the state policy."). A state banking supervisor's ability to "exercise sovereign power over individuals and entities within the relevant jurisdiction" and its "power to create and enforce a legal code" are essential to this balance. *Alfred L. Snapp & Son, Inc. v. Puerto Rico ex rel. Barez*, 458 U.S. 592, 601 (1982); *Hopkins*, 296 U.S. at 340.

The Fintech Charter Decision exceeds OCC's authority under the NBA and upsets this balance of power by invading DFS's long-recognized and legally protectable interests. Because the Fintech Charter Decision, and the tension between federal and state law it triggers, is itself actual injury, DFS has alleged "a judicially cognizable interest in the

preservation of its own sovereignty, and a diminishment of that sovereignty by the alleged [federal] interference." *Bowen v. Public Agencies Opposed to Soc. Sec. Entrapment*, 477 U.S. 41, 51 n.17 (1986).

The Supreme Court recognizes the "special solicitude" to which states are entitled in the standing analysis. *Massachusetts v. EPA*, 549 U.S. 497, 520 (2007). And federal courts have long recognized a state's standing to challenge federal agency action that "interferes with [the state's] ability to enforce its legal code." *See, e.g., Wyoming ex rel. Crank v. United States*, 539 F.3d 1236, 1241-42 (10th Cir. 2008); *Texas v. EEOC*, 827 F.3d 372, 379 (5th Cir. 2016) (a state's "unique position as a sovereign state defending its existing practices and threatened authority" creates standing); *see also Abrams v. Heckler*, 582 F. Supp. 1155, 1159 (S.D.N.Y. 1984) (New York regulators have standing to challenge federal agency rule that would "impede the plaintiffs' ability to protect the interests of those they are charged by statute with protecting.")

Even the District Court decision of the District of Columbia ("*CSBS I*"), upon which OCC so significantly relies, acknowledged that "regulatory interference with a state is indeed a concrete and particularized injury." *CSBS v. OCC*, 313 F. Supp. 3d 285, 296 (D.D.C.

2018). Contrary to OCC's contentions, this regulatory interference has already begun.

For example, the Fintech Charter Decision circumvents existing limitations on the ability of state-regulated entities to convert to a national bank. Under the NBA, an active company can become a national bank only by converting to a national bank charter through the statutory mechanisms established by Congress. *See* 12 U.S.C. § 35.[2] But to be eligible to convert to a national bank charter, an institution must be a state-chartered bank and, thus, "engaged in the business of receiving deposits." *See* 12 C.F.R. § 5.24(c)(2) (OCC conversion regulation incorporating definition of "state bank" in 12 U.S.C. § 214(a)). Permitting otherwise ineligible entities to apply for and effectively convert to a national charter is itself injurious to the interests of state bank regulators.

[2] Only natural persons are permitted to apply to organize a national bank *de novo*, 12 U.S.C. § 21. Thus, OCC's invitation to existing legal entities to substitute their state charter for the Fintech Charter while maintaining their business and corporate identity is effectively an invitation to undergo "conversion" to a national charter.

By circumventing the charter conversion process in this manner, OCC strips from state regulators the protections that come from the NBA prohibition on conversion of an entity subject to a pending supervisory action by a state bank supervisor. 12 U.S.C. § 35. The loss of this protection forces state regulators to face the prospect of retroactive preemption of their supervisory actions. This is because, in other contexts where conversion is permitted irrespective of pending actions, *see* 12 U.S.C. § 3102(f), OCC has taken the position that, upon conditional approval of a national charter, state regulators like DFS lose their authority over even pre-charter conduct occurring when the organization was still state-regulated. *See* Brief of OCC as Amicus Curiae Supporting Plaintiff, at pp. 20, 23-25, *Bank of Tokyo-Mitsubishi UFJ, Ltd. v. Vullo*, No. 1:17-cv-08691 (S.D.N.Y. Mar. 26, 2018), ECF No. 35-1.

Because OCC has historically taken the position that preemption of state law is *retroactive* upon the granting of a national charter to the date that the federal entity was first created, OCC's actions have already divested the states of regulatory and supervisory authority over state-licensed nonbanks even before a national charter is granted. Accordingly, DFS and other state regulators must now exercise their regulatory

authority over nonbanks under the existential threat that state licensees will obtain a Fintech Charter and, as a result, any state supervisory action will be rendered ineffective even with respect to pre-application conduct. Being forced to modify supervisory approaches constitutes an actual injury which, given the retroactive preemptive effect, has already manifested.

B. OCC's regulatory interference is at least certainly impending.

DFS renewed this litigation only after OCC finalized its Fintech Charter Decision and made multiple public statements about the significant progress being made toward issuing charters—including "hundreds" of meetings with interested companies, acknowledgement that the application process was underway for "a number of institutions," and a proclamation that initial charter decisions were expected soon. *See* Appellee's Brief 18-20; *see also* Rachel Witkowski, *Fed not an impediment to fintechs' charter ambitions: OCC's Otting*, American Banker (Jan. 16, 2019), https://www.americanbanker.com/news/fed-not-an-impediment-to-fintechs-charter-ambitions-occs-otting. Notwithstanding its own

public pronouncements regarding the imminence of these charters, OCC now asserts that any injury to DFS is merely "speculative."

But the central and animating purpose of the Fintech Charter is to enable recipients of the charter to escape state regulation through federal preemption. *See* 12 U.S.C. § 484; 12 C.F.R. § 7.4000. Because preemption is the *raison d'etre* of the Fintech Charter, there is a "reasonable probability" that such interference with state regulation will occur and, thus, DFS's injuries are "certainly impending." *See Monsanto Co. v. Geertson Seed Farms*, 561 U.S. 139, 153 (2010).

In arguing the contrary, OCC contends that DFS's harm is dependent on the specific *nature* and *geography* of the chartered entities—DFS will never be harmed if *none* of the chartered entities operate within a substantive area subject to DFS's regulation or supervision, or have any nexus to New York. *See* Brief of Defs.-Appellants ("OCC Br.") at 22. These assertions strain credulity.

First, it is well-settled that the relevant inquiry here is the "*risk* of future injury, rather than its ultimate realization." *New York v. U.S. Dep't of Commerce*, 351 F. Supp. 3d 502, 575 (S.D.N.Y. 2019) (citing *Davis*

v. FEC, 554 U.S. 724 (2008)) (emphasis in original). Additionally, injury can be established "even if several steps on the causal chain still stand between a defendant's conduct and the plaintiff's injury . . ." *New York*, 351 at 576; *see also Rothstein v. UBS AG*, 708 F.3d 82, 92 (2d Cir. 2013). Moreover, DFS need not establish that its harm is "literally certain." *Clapper v. Amnesty Int'l USA*, 568 U.S. 398, 414 n.5 (2013). Rather, "reasonable probability" of harm is sufficient. *Monsanto Co. v. Geertson Seed Farms*, 561 U.S. 139, 153 (2010).

Because of (1) the Fintech Charter's distinct appeal to companies operating nationwide, which will be the most affected by preemption of state law, and (2) the wide variety of nonbank financial activities regulated by DFS and New York law,[3] DFS has readily established a "reasonable probability" that OCC's Fintech Charter program will impede its interests.

[3] Like other states, New York licenses, supervises, or otherwise regulates nonbanks engaged in payday lending, mortgage lending, check cashing, payment processing, sales financing, student loan servicing, virtual currency business and more. *See*, *e.g.*, New York State Licensing Requirements, *NMLS Resource Center*, https://nationwidelicensingsystem.org/slr/Pages/DynamicLicenses.aspx?StateID=NY.

C. DFS's Claims are Prudentially Ripe.

The District Court acted well within its discretion in declining to invoke the doctrine of prudential ripeness to postpone consideration of the merits of DFS's challenge.

As DFS explains in its principal brief, this dispute presents a purely legal issue. Additional facts—such as the identity of the company seeking a charter, its business model, or the geographic scope of its operations—are not relevant to this discrete legal question. DFS has challenged OCC's authority to issue Fintech Charters to *any* nondepository institution. Moreover, OCC's position regarding its own authority to issue Fintech Charters has fully crystallized and no outstanding interpretive questions remain.

OCC has not explained what additional facts are needed to evaluate the *merits* of the claim before the court. Rather, OCC focuses solely on the purported need for facts to establish whether DFS has suffered *injury*. OCC Br. 27-28. This misconstrues the proper focus of the fitness prong. *See, e.g.*, *Awad v. Ziriax*, 670 F.3d 1111, 1124-25 (10th Cir. 2012) (courts must "focus[] on whether determination of *the merits* . . . requires

facts that may not yet be sufficiently developed.") (emphasis added) (citations omitted).

Nor can OCC establish hardship sufficient to justify further postponing review. OCC has not cited *any* institutional interest in postponement, because there is none. To the contrary, as the District Court noted, the narrow legal issue here should be answered "before a fintech company wastes its and OCC's time and money . . ." (J.A. 250).

On the other hand, state bank supervisors, including DFS, would face substantial hardship if review is withheld. The general interference with the states' quasi-sovereign interests, as well as the interference with DFS's ability to establish and enforce nondepository financial regulations under the threat of federal encroachment by OCC, weigh in favor of prompt resolution. Moreover, as described herein, OCC's attempt to circumvent statutory conversion limitations and assertion of retroactive preemption of state law are present detriments that will color the states' approach to nondepository supervision so long as the possibility of the Fintech Charter is held out as a lawful option.

Finally, there will not be sufficient timely notice of applications to afford DFS "ample opportunity" to challenge those applications. An applicant is only required to place notice in the newspaper in the area of its main office, and OCC has authority to waive any of its own notice requirements. *See* 12 C.F.R. § 5.8(f). Even if a state regulator could successfully monitor all newspapers across the country, the published information is likely to be insufficient to determine whether the application is for a Fintech Charter or to identify the applicant as a particular nonbank licensee.

II. Carrying on the "business of banking" under the NBA unambiguously requires engaging in receiving deposits.

OCC's interpretation of the "business of banking" is invalid because carrying on the "business of banking" under the NBA unambiguously requires engaging in receiving deposits in light of the conditions placed on the formation of national banks by other federal banking laws.

A. The FRA and FDIA govern the formation of national banks, and both unequivocally require that national banks receive deposits.

The term "business of banking," as used in the NBA chartering provisions, cannot be considered in isolation. In addition to the NBA, Congress has enacted several laws that were landmarks in the development of the present federal banking structure—most notably, the FRA and FDIA.[4] These enactments are as foundational to the structure of the national banking system as the NBA itself. Failing to give these other federal banking laws due consideration in construing the meaning of the "business of banking" would upend the statutory scheme established by Congress over the past 150 years.

Like the NBA, the FRA and the FDIA place conditions on the formation and operation of national banks and thus govern whether a

[4] Although not addressed in detail herein, the definition of "bank" in the Bank Holding Company Act (BHCA) requires engaging in receiving deposits. 12 U.S.C. § 1841(c). Thus, the "business of banking" must require the same, in order to give full effect to the BHCA and the NBA's joint regulatory scheme. *See Indep. Bankers Ass'n of Am. v. Conover*, No. 8401403-CIV-J-12, 1985 U.S. Dist. Lexis 22529, *33 (M.D. Fla. Feb. 15, 1985). *See also Whitney Nat'l Bank v. Bank of New Orleans & Trust*, 379 U.S. 411, 417-26 (1965) (the NBA and BHCA should be interpreted in harmony and OCC cannot grant charters that would violate the BHCA's terms or clearly intended policies).

national bank may lawfully commence business. The FRA requires that national banks become members of the Federal Reserve System ("FRS"), and such banks must be "insured banks" upon commencing business. *See* 12 U.S.C. § 222. To become an "insured bank," a bank must apply to the Federal Deposit Insurance Corporation ("FDIC") for deposit insurance, *see* 12 U.S.C. § 1815(a), and, of course, must be eligible for deposit insurance by engaging in "the business of receiving deposits other than trust funds" as defined under the FDIA and FDIC regulations. *See* 12 C.F.R. § 303.14.

Failure to become a FRS member or FDIC-insured bank results in the forfeiture of the rights, privileges, and franchises conferred with a national bank charter. *See e.g.,* 12 U.S.C. § 501a. These provisions of the FRA and FDIA must be read *in pari materia* with the NBA chartering provisions, given the high degree of integration between these laws. *See e.g., Branch v. Smith*, 538 U.S. 254, 281 (2003); *see also Brown v. Gardner*, 513 U.S. 115, 118 (1994) ("Ambiguity is a creature not of definitional possibilities but of statutory context").

Many national bank powers, rights and privileges actually derive from the FRA itself. *See e.g.*, 12 U.S.C. § 371 (power to originate mortgage

loans). All of the powers of national banks must, at the point of formation, be "consistent with the purposes of the [FDIA]." *See* 12 U.S.C. § 1816(7). OCC's chartering regulation itself cites this provision of the FDIA as part of the statutory authority for its promulgation. *See* 12 C.F.R. § 5.20(a) (citing 12 U.S.C. §§ 1814(b), 1816).

When enacted, the FRA and FDIA unambiguously required that national banks operate as depository institutions just like the NBA before them. While the NBA had required national banks to engage in receiving deposits in order to engage in issuing and circulating national bank notes, the FRA requires national banks to engage in receiving deposits in order to become members of the FRS, which issues and circulates federal reserve notes. *Cf*. Act of June 3, 1864, ch. 106, § 39, 13 Stat. 99, 111 (requiring that a national bank's notes "be receivable, at par, on deposit" in order to be issued and circulated by the national bank) with Act of Dec. 23, 1913, ch. 6, § 16 (codified at 12 U.S.C. § 411) ("The [Federal Reserve] notes . . . shall be receivable by all national and member banks . . .); H.R. Rep. No. 63-69, at 54-55 (1913) (explaining that, through this and other provisions of the FRA, "it is required that every bank in the system shall receive the notes on deposit at par.").

The requirement that all FRS members operate as depository institutions was reinforced when Congress amended the FRA to establish a system of federal deposit insurance in the Banking Acts of 1933 and 1935 and, in doing so, requiring all national banks and member banks to obtain deposit insurance. *See* Act of June 16, 1933, ch. 89, § 8, 48 Stat. 162, 179; Act of Aug. 23, 1935, ch. 614, § 101, 49 Stat. 685, 688, 691. Although the deposit insurance provisions of the Banking Acts were subsequently incorporated into an independent act with the enactment of the Federal Deposit Insurance Act of 1950, Pub. L. 81–797, 64 Stat. 873, the deposit insurance mandate was maintained in the FRA. *See* 12 U.S.C. § 222. Thus, since the enactment of the FRA and the FDIA, national banks have been required to become FRS members and FDIC-insured banks. Accordingly, just like the NBA at the time of its enactment, the FRA and FDIA have always unambiguously required national banks to engage in receiving deposits in order to carry on the business of banking.

B. Section 222 was intended to function, and has always functioned, as a deposit-insurance mandate.

OCC's claim that Section 222 has never functioned, and was not intended to function, as a deposit insurance mandate is contrary to the legislative history and misreads a statute it does not administer. OCC Br. 48-49. OCC argues that Section 222 merely requires national banks located in newly admitted states (*e.g.*, Alaska) to become FRS members and automatically grants deposit insurance to such banks rather than continuing to require them to submit a separate application. *Id*. However, legislative history reveals the contrary—Section 222 imposes a deposit-insurance mandate.

The FRS membership and FDIC insurance mandates in Section 222 were enacted at the request of the Board of Governors of the Federal Reserve System ("FRB"). In proposing statutory language that ultimately would be codified in Section 222, the FRB explained this provision as a continuation of the deposit-insurance mandate that had applied to national banks since the inception of federal deposit insurance. *See* 96 Cong. Rec. 9744-9745 (July 10, 1950) ("[u]nder present law, all national

banks . . . are required to be members of the Federal Reserve System and, as such members, to be insured banks").

The fact that deposit insurance was, at that time, automatically granted to national banks upon their becoming members of the FRS, rather than through a separate application, does not imply that that Section 222 did not function as a deposit-insurance requirement. First, that Congress automatically granted the status of insured bank to national banks confirms Congress' viewed national banks as always, by their nature, engaged in the business of receiving deposits. Second, if FDIC insurance were not required as a condition of FRS membership, it would make little sense for Congress to require the termination of a bank's insured-bank status if it ceased being a FRS member. *See* 12 U.S.C. § 1818(o).

Finally, when Congress revised the FDIA in 1989 and 1991 to require national banks to submit a separate application for deposit insurance, rather than obtain it automatically, the FRB continued to interpret Section 222 as an independent deposit insurance requirement—and Congress rejected the Comptroller's urging to repeal that requirement. *See Economic Growth and Regulatory Paperwork*

Reduction Act: Hearing on S. 650 Before the S. Comm. on Banking, 104th Cong., 91-92 (1995) (testimony of Comptroller indicating that the FRB interprets Section 222 to "require a national bank both to become a member of the Federal Reserve and to be insured by FDIC" and advocating for its repeal to allow for the chartering of uninsured national banks). Thus, OCC's current interpretation of Section 222 not only conflicts with the FRB's interpretation of a statute FRB is charged with administering but disregards OCC's own failed efforts to eliminate this requirement.

Next, OCC argues that Section 222 does not function as an independent deposit insurance requirement because this statute requires a national bank to become FDIC-insured only if OCC determines it is eligible for deposit insurance. OCC Br. 49-50. But OCC does not have the authority to make a final determination whether or not a national bank is "engaged in the business of receiving deposits, other than trust funds," under the FDIA, because that determination is solely the FDIC's prerogative. *See* 12 U.S.C. §§ 1815(a)(6), 1818(p).

Were it otherwise, OCC could permit national banks to forego deposit insurance because, in OCC's view, none of the bank's liabilities

are "deposits" as defined in the FDIA. FDIC has the exclusive authority to define what constitutes a "deposit" under FDIA. *See* 12 U.S.C. § 1813(l)(5). OCC cannot authorize national banks to forego applying for deposit insurance by adopting interpretations of the meaning of "deposit" under the FDIA that conflict with FDIC's interpretations of that term. Thus, Section 222 cannot be read as requiring deposit insurance *only if* OCC itself determines the bank would be engaged in receiving deposits.

C. National trust companies and bankers' banks are chartered for specified and distinct business purposes other than the banking business, and have no bearing on the application of Section 222 to institutions commencing the business of banking.

OCC claims that Section 222 does not impose a deposit-insurance mandate for institutions chartered by OCC to carry on the "business of banking" because OCC charters national trust companies, which are FRS members but not FDIC-insured. OCC Br. 48-49. But Section 222 does not apply to national trust companies because they are not chartered to carry on the banking business; rather, they are chartered to carry on the *trust* business and therefore are categorically ineligible for deposit insurance.

When Section 222 was enacted, OCC did not have the authority to charter national trust companies. Although Congress had previously considered granting OCC the authority to charter national trust companies, *see Suggested Plan For Monetary Legislation, Submitted To The National Monetary Commission by Hon. Nelson W. Aldrich*, S. Doc. No. 784, p. 27 (January 11, 1911), it ultimately decided, with the enactment of the FRA in 1913, to instead extend fiduciary powers to national banks by permitting them to apply for a permit to exercise those powers in addition to the normal banking powers conferred with their charter. *See* Act of Dec. 23, 1913, ch 6, § 11(k) (*codified at* 12 U.S.C. § 92a); 12 C.F.R. § 5.26.

Thus, a national bank could not engage in fiduciary activities pursuant to its authority to engage in the business of banking. In fact, a national bank is prohibited under its banking powers from taking certain actions mandated in the exercise of trust powers. *Compare Texas & Pac. Ry. Co. v. Pottorff*, 291 U.S. 245 (1934) (national banks do not have the authority to pledge assets to secure deposits) *with* 12 U.S.C. § 92a(d) (mandating pledge of assets to secure trust funds). Conversely, national banks cannot engage in banking activities through the exercise of

fiduciary powers because the grant of fiduciary powers prohibits (i) engaging in receiving deposits other than trust funds and (ii) engaging in non-fiduciary banking activities more broadly. *See* 12 U.S.C. § 92a(c)-(d).

Because the trust business and banking business are of a distinct and separate nature under the NBA, OCC did not have the power to charter national trust companies until Congress expressly granted OCC that authority in the Financial Institutions Regulatory and Interest Rate Control Act of 1978 ("FIRIRCA"), Pub. L. 95-630, 92 Stat. 3641 (amending 12 U.S.C. § 27(a)). *See National State Bank of Elizabeth v. Smith*, No. 76-1479, 1977 U.S. Dist. LEXIS 18184 (D.N.J. Sept. 16, 1977). The powers conferred in the grant of a national trust company charter derive from the grant of fiduciary powers in Section 92a, rather than the grant of banking powers in Section 24 (Seventh). *See National State Bank v. Smith*, 591 F.2d 223, 231-32 (3d Cir. 1979). Accordingly, a national trust company lacks the power to engage, and is prohibited from engaging, in receiving deposits other than trust funds. *See* 12 U.S.C. § 92a(d). Thus, national trust companies are categorically ineligible for deposit insurance and do not carry on the business to which the Section

222 deposit-insurance mandate was intended to apply—namely, the banking business.

Importantly, the fact that national trust companies are not required to obtain deposit insurance by Section 222 does not imply that OCC is authorized to determine whether an institution it charters is eligible for deposit insurance. Given the nature of a trust company's business, OCC need not determine whether or not such a company is engaged in receiving deposits other than trust funds. Thus, other than national trust companies and national bankers' banks,[5] all institutions chartered by OCC are organized to carry on the business of banking and, thus, must engage in receiving deposits and be FDIC-insured banks.

[5] OCC has previously relied on its authority to exempt bankers' banks from statutory obligations applicable to national banks, *see* 12 U.S.C. § 27(b)(2), to waive the FDIC insurance requirement for bankers' banks. *See* Comptroller's Manual for Corporate Activities, Policies and Procedures, Vol. 1, p. 40 (January 1992). All other institutions chartered by OCC, regardless of the label they are given, must be FDIC-insured. *See e.g., id.* at p. 14 ("Credit card banks are required to be FDIC-insured.").

III. OCC's reliance on the definition of "branch" to define the "business of banking" is unreasonable.

OCC acknowledges that it based its "business of banking" definition on 12 U.S.C. § 36(j)'s definition of a bank "branch," *i.e.*, offices located apart from a national bank's main office "at which deposits are received, or checks paid, or money lent." In reality, Section 36(j) does not support OCC's position but directly contradicts it.

Section 36 was enacted in the McFadden Act of 1927, Pub. L. 69-639, § 7, 44 Stat. 1228, to enable national banks to establish "branches" with the prior approval of OCC. Prior to the McFadden Act, national banks were not permitted to establish branches because they lacked the implied power to do so under 12 U.S.C. § 24 and were expressly prohibited from doing so by 12 U.S.C. § 81, which restricted the "general business" of a national bank to its main office. *See Lowry National Bank,* 29 Op. Att'y Gen. 81 (1911). Through the McFadden Act, Congress amended Section 81 to permit the "general business" of a national bank to be conducted not only in its main office but also at any branch established in accordance with Section 36.

The overriding purpose of the McFadden Act was to establish "competitive equality" between state and national banks with respect to restrictions on geographic expansion, while deferring to the states to establish the extent of such restrictions. *First Nat'l Bank v. Walker Bank & Trust Co.*, 385 U.S. 252 (1966). The McFadden Act accomplished these twin aims by permitting national banks to open branch offices only to the same extent as is expressly authorized for state banks under state law. *See* 12 U.S.C. § 36(c). To preserve this deference to state standards, Congress identified the three functions that are the "routine and traditional bank services normally provided at the bank's main office," *Indep. Bankers Asso. v. Smith*, 534 F.2d 921, 943 (D.C. Cir. 1976), and provided that any office apart from the main office that engages in these functions (either in isolation or in combination) is a branch office subject to state law restrictions incorporated by Section 36.

It is unreasonable to define the term "business of banking" as *any* of the three functions listed in the branch definition. First, Congress listed these three functions in the disjunctive to prevent OCC from deeming any of the listed functions as not essential to the banking business. Second, OCC's interpretation contradicts the meaning

historically ascribed to the three functions and would result in asymmetry between the NBA chartering and location provisions. Third, this interpretation conflicts with OCC and judicial precedent recognizing that all three functions are essential to the banking business—receiving deposits most of all.

A. The disjunction in the branch definition was intended to prevent OCC from identifying any one of the functions as not essential to the general business of national banks.

In 1911, *Lowry* held that a national bank could not establish branch offices to conduct a general banking business. 29 Op. Att'y Gen. 81. A subsequent Attorney General opinion, however, sought to limit the scope of the *Lowrey* opinion, concluding that receiving deposits and cashing checks were not within the "general business" of national banks. 34 Op. Att'y Gen. 1 (1923). Based on this opinion, OCC adopted regulations to allow for the establishment of "additional offices" on an intra-city basis (described as "mere tellers' windows") to engage in receiving deposits or paying checks. *See* Annual Report of the Comptroller of the Currency, 12, 153-155 (1923).

The Supreme Court subsequently rejected these tellers' windows and overruled the 1923 opinion to the extent it diverged from *Lowry*. *See First Nat'l Bank v. Missouri*, 263 U.S. 640, 658 n.1 (1924). Shortly thereafter, however, OCC announced it would not rescind the tellers' windows regulation because it believed solely receiving deposits or cashing checks did not amount to a general banking business. *See* Fed. Res. Bull. Vol. 10, No. 4, pp. 285-286 (April 1924); *see also* 66 Cong. Rec. 1577 (January 9, 1925).

Because OCC's views allowed for "unlimited branching," Congress subsequently intervened by enacting the McFadden Act. *See Clarke v. Sec. Indus. Ass'n*, 479 U.S. 388, 402 (1987). Legislative history reveals that Congress defined branch in functional terms as a direct response to OCC's extant regulation. *See Consolidation of National Banking Associations, etc.: Hearing on H.R. 6855 Before the H. Comm. on Banking and Currency*, 68th Cong., 3 (1924) (original version of the McFadden Act defining "branch" as any additional office "at which deposits are received or checks cashed").

Furthermore, Congress listed the functions of branch in the disjunctive to prevent OCC from circumventing state law branching

restrictions—as it had done in allowing for tellers' windows—by identifying certain functions as purely ministerial and therefore not subject to the restrictions on the location of the "general business" of national banks. *See* 66 Cong. Rec. 1628 (January 10, 1925) (Rep. Stevenson explaining that the definition of branch is intended to "take away from the comptroller the right to say that banks can maintain offices at which they can pay checks and receive deposits"); *accord* 67 Cong. Rec. 2860 (January 27, 1926). It is illogical to assert that, by listing the functions in the disjunctive, Congress intended, on the one hand, to prevent OCC from classifying any one of the listed functions as not part of the "general business" of national banks and, on the other hand, to enable OCC to classify any of the listed functions as not essential to the "business of banking."

B. OCC's interpretation gives a meaning to the core functions in the chartering context that entirely contradicts the meaning given to those functions in the branching context.

Sections 36 and 81 restrict the location at which the three functions listed in the definition of branch may be conducted. As is evident from the use of the passive voice to refer to these three functions, these sections

do not confer the power to engage in these functions; they merely refer to the powers granted elsewhere in the NBA. *See e.g.*, 12 U.S.C. § 24(Seventh).

Because the branch definition does not enable the exercise of the activities listed therein, the meaning historically ascribed to the three functions in determining where they may take place is significantly more circumscribed than the meaning ascribed to the correlative banking powers in determining what activities can take place at all. Whereas, in the latter inquiry, many activities will be found to be incidental to the enumerated banking powers, in the former inquiry, these same activities have been found not to be within the scope of the functions listed in the branch definition. *See e.g.,* 1999 OCC Ltr. LEXIS 42, *28-29 (July 9, 1999) (listing OCC interpretations finding that "money" is not "lent" by engaging in various loan origination and loan approval functions); 12 C.F.R. §§ 7.1004-.1005.

In fact, OCC and courts have long recognized that having the power to receive deposits is necessary for money to be lent or checks to be paid within the meaning of the branch definition. Specifically, for a national bank to engage in the functions of lending money or paying checks, it

must be able to offer deposit accounts through which loan proceeds can be disbursed and from which checks can be drawn. *See Smith*, 534 F.2d at 943; *see also* 1985 OCC Ltr. LEXIS 4, *4 (May 24, 1985) ("the passage of funds represents the essence of each "branching" service enumerated by section 36(f)."). And to offer deposit accounts, a national bank, of course, must possess and exercise the power to receive deposits.

For instance, with respect to "paying checks," OCC has long held that "[t]he term 'checks paid,' within the meaning of the definition of a 'branch' refers to withdrawals from a deposit account at the bank." 1999 OCC QJ LEXIS 45, *6 (Sept. 29, 1998); *see also Smith*, 534 F.2d at 944. As a result, the term refers to the payment of checks drawn on the bank to which the check is presented, not the cashing of checks drawn on other banks. *See id*; 12 C.F.R. § 7.4004(a) (equating paying checks with "paying withdrawals").

Similarly, OCC's regulations provide that "'money' is deemed to be 'lent' only at the place, if any, where the borrower in-person receives loan proceeds *directly* from bank funds." 12 C.F.R. § 7.1003 (emphasis added); *see also* 1996 OCC Ltr. LEXIS 32, *10-11 (Mar. 6, 1996). Accordingly, for a national bank to engage in lending money as used in the branch

definition, it must itself offer accounts through which it can disburse loan proceeds directly to borrowers.

Thus, engaging in "paying checks" or "lending money" requires offering deposit accounts, and, by extension, exercising the power to receive deposits. OCC's reliance on the disjunction in the branch definition to assert that an institution can engage in lending money or paying checks without engaging in receiving deposits therefore contradicts its interpretations regarding the interrelation of these functions. It is illogical for OCC to give these functions contradictory meanings in implementing the NBA provisions governing where an activity take place, as opposed to the NBA provisions governing what activities can take place at all.

Far from creating symmetry, OCC's interpretation results in the scope and interrelation of the core functions being defined entirely differently for the purposes of the NBA location and chartering provisions. Even if OCC were permitted to start anew and adopt entirely contradictory meanings of these functions, there is then no textual basis left for incorporating the "or" from the branch definition. This is

particularly baseless since doing so undermines the reason that Congress listed those functions in the disjunctive.

C. OCC's definition of the business of banking is inconsistent with precedent and the constitutional basis of the NBA.

Neither *Clarke* nor any other precedent supports OCC's interpretation. *Clarke* suggested that the "general business" that a national bank itself transacts must encompass all three core banking functions, including receiving deposits. *Clarke,* 479 U.S. at 405 (quoting *Lowry*, 29 Op. Att'y Gen. at 87-88) ("a bank office that carries on a 'general banking business' is . . . one that 'competes in *all branches of the banking business*.'") (emphasis added). In briefing the case, OCC likewise stated that "the phrases 'general business of each national bank()' or 'general banking business,' plainly refer to *those activities* that are *essential attributes* of a bank's role as a provider of *depository and related banking services*." 1986 WL 728049 (U.S.), Reply Brief of the Federal Petitioner, *5-6 (emphasis added).

The "core banking functions" moniker actually derived, not from the briefings or the lower court opinions, but from OCC's interpretation of the phrase "banking business" in 12 U.S.C. § 36(l). In that interpretation,

OCC defined the phrase "banking business" as necessarily including all three core banking functions. *See* 1985 OCC QJ LEXIS 812, at *21-22 ("the [NBA] essentially reduces the business of banking, in perhaps its simplest form, to accepting deposits, making loans, and paying checks,"); *see also Dep't of Banking & Consumer Fin. v. Clarke*, 809 F.2d 266, 268 (5th Cir. 1987). Thus, to the extent that the phrase "general business" has any bearing on the meaning of the "business of banking," it is clearly established that the "general business" of a national bank itself must encompass all three core banking functions, receiving deposits most of all given that, as explained above, the exercise of this power is necessary to engage in the other two functions.

This conclusion is consistent with the conception of the banking business upon which the authority of the federal government to create national banks is based. *See Farmers' & Mechanics' Nat'l Bank v. Dearing*, 91 U.S. 29, 33 (1875) (upholding constitutionality of the NBA based on constitutional authority recognized in *McCulloch v. Maryland*, 17 U.S. 316 (1819) and *Osborne v. Bank of the United States*, 22 U.S. 738 (1824)). *McCulloch* and *Osborne* upheld this authority by "considering the bank as created by Congress as an entity with all the functions and

attributes conferred upon it," rather than by "rest[ing] the determination as to such power upon a separation of the particular functions from the other attributes and functions of the bank and ascertain[ing] the existence of the implied authority to confer them by considering them as segregated, that is, by disregarding their relation to the bank as component parts of its operations, . . .". *First Nat'l Bank v. Fellows*, 244 U.S. 416, 424 (1917).

In defining a bank by separating and isolating banking functions and treating each as a sufficient, but not necessary, condition to be engaged in banking, OCC's interpretation contradicts the constitutional basis upon which the NBA rests. Instead, to keep the NBA within its constitutional mooring it must be held that engaging in receiving deposits is a necessary condition to be engaged in the banking business. Because the power to receive deposits bears an indispensable relation to the other two functions and the banking business more generally, this holding properly considers the national bank charter as creating "an entity with all the functions and attributes conferred upon it." *Id*.

CONCLUSION

For the reasons set forth above, this Court should affirm the District Court's judgment.

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CERTIFICATE OF COMPLIANCE

Pursuant to Rule 32(a) of the Federal Rules of Appellate Procedure, I hereby certify that this brief contains [6,981] words and complies with the typeface requirements and length limits of Rule 32(a)(5)-(7) and Second Circuit Local Rule 32.1.

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