LAW OFFICES
BALLARD SPAHR ANDREWS & INGERSOLL, LLP
1735 MARKET STREET, 51ST FLOOR
PHILADELPHIA, PENNSYLVANIA 19103-7599
215-665-8500
FAX: 215-864-8999
WWW.BALLARDSPAHR.COM

BALTIMORE, MD
DENVER, CO
SALT LAKE CITY, UT
VOORHEES, NJ
WASHINGTON, DC
WILMINGTON, DE

JEREMY T. ROSENBLUM
DIRECT DIAL: (215) 864-8505
PERSONAL FAX: (215) 864-9062
E-MAIL: ROSENBLUM@BALLARDSPAHR.COM

December 13, 2005

E-Mail (comments@FDIC.gov)

Robert E. Feldman, Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation
550 17th Street, NW.
Washington, DC 20429

Re: Proposed Rule: Interstate Banking; Federal Interest Rate Authority
RIN 3064-AC95

We very much appreciate the opportunity to comment on the proposed rule identified above and, in particular, the FDIC's proposal to adopt regulations under Section 27 of the Federal Deposit Insurance Act ("Section 27"), 12 U.S.C. § 1831d. We strongly support the adoption of regulations under Section 27. Such regulations will clarify the interest rate authority of state banks and will thereby support Congress' intent, expressed in Section 27, to "prevent discrimination against State-chartered insured depository institutions."

In its preamble to the proposed rule, the FDIC recognized the overwhelming authority for the proposition that Section 27 must be interpreted in *pari materia* with 12 U.S.C. § 85 ("Section 85"). The definition of "interest" as incorporated into Part 331 appropriately addresses the importance of a uniform federal definition of this key term in Section 27. However, we respectfully submit that true parity will not be achieved by Section 27 regulations that merely mirror 12 C.F.R. § 7.4001 ("Section 7.4001"), the OCC's regulation under Section 85. This is because: (1) the OCC has articulated its Section 85 guidance not merely through Section 7.4001 but also through its lending regulations, 12 C.F.R.§§ 7.4008 and 34 (and the accompanying explanatory material); and (2) a recent decision by the U.S. Court of Appeals for the 11th Circuit, *BankWest v. Baker*, 411 F.3d 1289 (11th Cir. 2005), *petition for rehearing en banc pending*, has refused to apply to Section 27 the preemption standards articulated by the U.S. Supreme Court in *Barnett Bank of Marion County v. Nelson*, 517 U.S. 25 (1996), and has accordingly adopted a narrow view of Section 27's preemptive force that threatens to establish widely varying rules for state and national banks.

Relying upon abundant judicial precedent, the OCC has made it clear that state laws that impair significantly the ability of a national bank to exercise its federally created

powers are preempted, whether such impairment is direct or indirect. In the Federal Register release adopting its final preemption rules, the OCC explained as follows:

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

69 FR 1904 (Jan. 14, 2004) (footnote omitted) (emphasis added).

Notably, the OCC did not suggest that *Barnett Bank* is limited to the insurance powers at issue in that case, nor even to the lending, deposit-taking or other powers described in 12 C.F.R. §§ 7.4007, 7.4008, 7.4009 and 34. Rather, preemption extends to the exercise by a national bank of ***any*** of its "Federally authorized powers," ***including*** the power under Section 85 to charge the interest allowed by the laws of the State where the bank is located, subject, of course, to compliance with the related laws that are "material to the determination of the permitted interest."

Due to the fact that the OCC has adopted broad lending preemption regulations, 12 C.F.R. §§ 7.4008(d) and 34.4, it was not necessary for the OCC to separately address how the principles of *Barnett Bank* apply to the related power of national banks to charge the interest allowed by the laws where they are located. We submit, however, that it is essential for the FDIC to do this in the context of its regulations under Section 27. Thus, the FDIC should confirm that *Barnett Bank* applies to a state bank exercising its power under Section 27 in the same manner that it applies to a national bank exercising it Federally authorized powers under 12 U.S.C. §§ 24 (Seventh), 85 and 371.

The necessity of formal recognition of how *Barnett Bank* applies to Section 27 was made manifest earlier this year by the 11th Circuit's divided panel opinion in *BankWest v. Baker*. In *BankWest*, the majority held that Section 27 did not preclude the State of Georgia from prohibiting out-of-state state banks from paying their agents a majority of loan revenues when charging more than 16% interest on small loans. Not only did the majority note that "nothing in § 27(a) regulates separate contracts between out-of-state banks and in-state vendors," 411 F.3d at 1304, it observed that Section 27(a) "does not mention ***any*** collateral activity associated with the loan, such as marketing, advertising, solicitation, or any aspect of the loan procurement process. It does not mention collection practices associated with the loan." *Id.* (underscoring in original; bold italics added)

Thus, *BankWest* has given the states *carte blanche* to restrict, to any extent, marketing, advertising, solicitation, loan procurement and collection practices of state banks – so long as the restrictions do not ***directly*** limit the interest that may be charged. This is so, even where the state statute: (1) only applies to loans at interest rates above a specified level, and the statutory restrictions accordingly are explicitly tied to the lender's exercise of its federally created right to charge the interest authorized by its home state laws; and (2) the bank can have

its loans voided, can be prosecuted for aiding and abetting its agent's violations and can, in practice, be prevented from making loans at disfavored rates altogether.

For example, *BankWest* would permit states to enact statutes providing that no third party may purchase a state bank's mortgage loan or credit card receivable if the borrower is a resident of the state and the rate exceeds a state-established level. It would also permit states to provide that merchants in the state may not accept a credit card that contains an interest rate above a specified level. Likewise, it would allow a state to impose burdensome restrictions on the marketing or collection of mortgage loans with rates above a specified threshold.

While the *BankWest* majority assumed that indirect action against bank agents, rather than direct action against banks themselves, cannot significantly impair the banks' rights and thereby trigger preemption under Section 27 and *Barnett Bank,* nothing in *Barnett Bank* (or in any other decision) limits preemption to state laws that operate directly against protected parties. And last year, in *Engine Manufacturers Ass'n v. S. Coast Air Quality Management Dist.*, 541 U.S. 246 (2004), the Supreme Court unequivocally rejected this kind of thinking: "The manufacturer's right to sell federally approved vehicles is meaningless in the absence of a purchaser's right to buy them." 541 U.S. at 255. By the same token, the right of state banks to export interest charges to out-of-state borrowers, recognized by a unanimous Supreme Court in *Marquette Nat'l Bank v. First of Omaha Serv. Corp.*, 439 U.S. 299 (1978), is meaningless in the absence of their agents' right to provide assistance in return for adequate compensation.

In brushing aside *Barnett Bank*, the *BankWest* majority also relied upon the fact that Act 440, the Georgia statute at issue: (1) allows out-of-state banks to lend to Georgia residents at their home state interest rates if they limit agent compensation to less than a predominant share of loan revenues; and (2) "leaves open other alternatives for out-of-state banks to export their home-state interest rates to Georgia borrowers."[1] 411 F.3d at 1302. In a blistering dissent, Judge Carnes cut right to the fallacy in this argument:

> The reality is that Georgia has acted to strip from out-of-state banks the right that § 27(a) gives them, if those banks structure their business in the way that they think best in light of business considerations and market forces. What Georgia has said is that the out-of-state banks Congress has specifically protected from state usury laws will not be protected by § 27(a) unless those banks quit doing business the way they prefer and start doing business the way the state prefers. And it just so happens that Georgia prefers that out-of-state banks covered by § 27(a) not do business in the way those banks have chosen to do it. What a coincidence. 411 F.3d at 1316-17 (Carnes, J., dissenting).

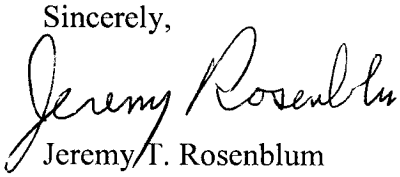
---

[1] The majority opinion suggests that preemption may be unavailable even where the indirect state law limitation on interest rates forecloses any and all options for the bank to make the loan.

We submit that *BankWest v. Baker* threatens irreparable harm to state banks and that the FDIC should expressly reject the reasoning of the case in the explanatory material for the final rule. We further submit that, in light of *BankWest v. Baker*, it is essential for the FDIC to explicitly recognize in its Section 27 regulations the application of *Barnett Bank* in this area, ***whether state limitations on interest charges are direct or indirect***. We would suggest adding a new Section 331.6 to the Section 27 regulations, closely patterned upon 12 C.F.R. § 7.4008(d), in the form attached hereto as Exhibit A.

Thank you for your attention to our views and for the effort you are making to reduce the competitive disadvantages state banks are facing in their interstate operations.

Sincerely,



Jeremy T. Rosenblum

PROPOSED 12 C.F.R. § 331.6

(a) (1) State laws are not applicable to state banks if and to the extent that they directly or indirectly obstruct, impair, or condition a state bank's ability to fully exercise its Federally authorized power to charge throughout the country the interest allowed by the laws of the state where the bank is located (other than laws that are material to the determination of the permitted interest).

(2) A state bank may charge such interest without regard to state law limitations concerning:

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

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

(iii) Loan-to-value ratios;

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

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

(vi) Security property, including leaseholds;

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

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

(ix) Disbursements and repayments; and

(x) Rates of interest on loans (other than the laws of the state where the bank is located incorporated into 12 U.S.C. § 1831d).

(b) State laws that are not preempted. State laws on the following subjects are not inconsistent with the powers of state banks under 12 U.S.C. § 1831d and apply to state banks to the extent that they only incidentally affect the exercise of state banks' of such powers:

Exhibit A

(1) Contracts;

(2) Torts;

(3) Criminal law;[2]

(4) Rights to collect debts;

(5) Acquisition and transfer of property;

(6) Taxation;

(7) Zoning; and

(8) Any other law the effect of which the FDIC determines to be incidental to the exercise by a state bank of its powers under 12 U.S.C. 1831d.

---

2 However, see the distinction drawn by the Supreme Court in *Easton v. Iowa*, 188 U.S. 220, 238 (1903) between "crimes defined and punishable at common law or by the general statutes of a state and crimes and offences cognizable under the authority of the United States" and special laws applicable to banks.

LAW OFFICES
BALLARD SPAHR ANDREWS & INGERSOLL, LLP
1735 MARKET STREET, 51ST FLOOR
PHILADELPHIA, PENNSYLVANIA 19103-7599
215-665-8500
FAX: 215-864-8999
WWW.BALLARDSPAHR.COM

BALTIMORE, MD
DENVER, CO
SALT LAKE CITY, UT
VOORHEES, NJ
WASHINGTON, DC
WILMINGTON, DE

JEREMY T. ROSENBLUM
DIRECT DIAL: (215) 864-8505
PERSONAL FAX: (215) 864-9062
E-MAIL: ROSENBLUM@BALLARDSPAHR.COM

December 13, 2005

E-Mail (comments@FDIC.gov)

Robert E. Feldman, Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation
550 17th Street, NW.
Washington, DC 20429

Re: Proposed Rule: Interstate Banking; Federal Interest Rate Authority
RIN 3064-AC95

As the recipient of OCC Interpretive Letter 822, 1998 OCC Ltr. LEXIS 14 (Feb. 17, 1998) (the "OCC Letter"), I am writing to address proposed 12 C.F.R. § 331.4 ("Section 331.4"). I am concerned that the proposed rule does not accurately reflect the rules laid out in the OCC Letter and, accordingly, may create confusion and/or unintended variances in the rules that apply to state banks and national banks, respectively. Additionally, I believe the adoption of the final rules under Section 27 would be a good occasion to recognize a self-evident fact: When a bank performs one of the three non-ministerial loan functions in a particular host state, that host state necessarily has a sufficient nexus to the loan to justify incorporation of the relevant usury laws of that state – that is, the laws applicable to that state's most favored lender – into Section 27.

My concerns with the existing language of proposed Section 331.4 are as follows:

1. I do not believe that proposed Section 331.4 contains an adequate definition of the three non-ministerial loan functions identified in the OCC Letter. Most importantly, it does not articulate where loan approval occurs if a bank applies non-discretionary underwriting standards to a loan.

2. As currently drafted, proposed Section 331.4 would not allow a state bank to apply its home state interest charges if all three non-ministerial functions occur in a single host state but one or more of these functions occurs outside host state branches – for example, at a back office or the borrower's home. This is not consistent either with the rule in the OCC Letter or the FDIC's description of the rule. In the preamble, the FDIC addresses the situation "where the three non-ministerial functions occur in different states or where some of the non-ministerial

functions occur in an office that is not considered to be the home office or a branch of the bank." 70 Fed. Reg. at 60028-29. It goes onto state that, "[I]n these instances, . . . home state rates may be used." It is correct in saying that the application of home state rates is consistent with GC-11 but incorrect in saying that the application of home state rates is consistent with the current language in proposed Section 331.4(c)(3). 70 Fed. Reg. at 60029.

3. Proposed Section 331.4(c) does not make it sufficiently clear that a bank may have options of whether to use home state or host state rates in many of the cases it describes. This is because the use of the phrase "[m]ay be determined" in subsections (c)(2) and (3) could be read as meaning "might (or might not) be determined."

4. Finally, proposed Section 331.4(c)(3) could be read to imply that performance of a non-ministerial function in a particular host state is insufficient to establish a "clear nexus" to that state. I suggest a formulation that allows a state bank to apply a host state's rates if the bank performs a non-ministerial function in the home state ***or*** there exists a clear nexus to the state. If the FDIC believes it necessary to retain the reference to performance of a non-ministerial function ***and*** a clear nexus, I believe it would be appropriate to state in the regulation (or perhaps the preamble) that the FDIC and OCC have not prejudged the issue whether performance of a non-ministerial function in a particular host state is sufficient by itself to establish a clear nexus to that host state, and that the rule should ***not*** be read to the contrary

Based on the foregoing concerns, I would suggest revising Section 331.4 as follows:

~~(a)~~§ 331.4 Location and interest rate for interstate state bank.

(a) Definitions. For purposes this section, the following terms have the following meanings:

(1) Home state means the state that chartered a state bank.

(2) Host state means a state, other than the home state of a state bank, in which the bank maintains a branch.

(3) Non-ministerial functions are factors to be considered in determining where a loan is made by an interstate state bank. The non-ministerial functions are:

(i) Approval. The decision to extend credit. Approval occurs where the person is located who ~~is charged with making~~applies discretion to make the final ~~judgment~~determination of approval or denial of credit. If, however, a loan is subject to non-discretionary criteria that are applied mechanically, the loan is approved where the decision to apply those criteria to the loan is made.

(ii) Disbursal. The ~~location where the actual physical disbursement of the~~disbursal of loan proceeds~~ of the loan occurs~~, as opposed to the delivery of previously disbursed funds. Disbursal occurs where a bank gives the proceeds of a loan in-person to a customer or credits the borrower's account at a branch. Disbursal does not occur when an escrow agent delivers funds, previously received from a bank, to the borrower. In cases not addressed by this section, identifying where disbursal occurs will require an analysis of the relevant facts and circumstances.

(iii) Extension of credit. The ~~site from which the~~ first communication of final approval of the loan~~ occurs~~.

(b) Location. An interstate state bank is located, for purposes of applying 12 U.S.C. 1831d, in the home state of the state bank and in each host state where the state bank maintains a branch.

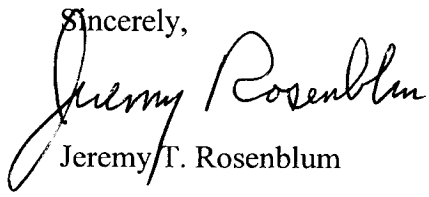
(c) Location in more than one state. If a state bank is located in more than one state, the appropriate interest rate will be determined as follows:

(1) ~~Will be determined by reference to the laws of the state where~~If all three of the non-ministerial functions occur in one or more branches in a single host state, the relevant usury laws of that state will apply;

(2) ~~May be determined by reference to the laws of the home state of the state bank, where~~If all three of the non-ministerial functions do not occur in ~~branches located in different host states or any of the non-ministerial functions occur in a state where the state bank does not maintain a branch; or (3) May be determined by reference to the laws of a host state where a~~one or more branches in a single host state, the bank may always elect to lend on the basis of the relevant usury laws of its home state. Additionally, the bank may elect to lend on the basis of the relevant usury laws of any host state where any non-ministerial function occurs or any host state where, if, based on an assessment of all of the relevant facts and circumstances, the loan has a clear nexus~~ to that host state~~.

Thank you for your consideration of my views.

Sincerely,



Jeremy T. Rosenblum