U.S. House of Representatives
Committee on Financial Services
2129 Rayburn House Office Building
Washington, DC 20515

May 16, 2005

The Honorable Donald E. Powell
Chairman
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

Dear Chairman Powell:

Thank you for holding a public hearing to discuss the Financial Services Roundtable's ("the Roundtable's") recent preemption petition. As the petition points out state banks currently lack the legal certainty to necessary to "restore [the] balance in the dual banking system that Congress sought to achieve in 1997."

Given the current ambiguity, we understand the Roundtable's desire to provide clarity. The issue of parity between national and state-chartered banks is of substantial importance. Unfortunately, the current ambiguity derives directly from the OCC's recent preemption and visitorial rules; and the obvious solution is for the OCC to work in good faith with interested parties to revise them. In short, the OCC caused this problem by overreaching and for the FDIC to follow suit and do the same would compound the problem rather than solve it.

Because the FDIC cannot change the OCC's recent regulations, it cannot provide state banks with the desired clarity. The law is quite clear. The application of state law to the interstate branches of state banks depends on the application of state law to the interstate branches of national banks:

> "The laws of the host state … shall apply to any branch … of an out-of-State State bank *to the same extent* as such laws apply to a branch … of an out-of-State National Bank. *To the extent* host state law is inapplicable to a branch of an out-of-State State bank in such host State … home State law shall apply to such branch."[1]

Hence, the key question in determining whether a state law applies to the interstate branch of a state bank is determining *whether the state law applies to the interstate branch of a national bank.* Unfortunately – in the wake of the OCC's far too sweeping preemption and visitorial rules – no one knows when state laws apply to national banks, so no one knows when state laws apply to the interstate branches of state banks. Because the FDIC has no ability to revise the OCC's regulations to appropriately answer this key question, it has little ability to correct this problem.

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[1] 12 U.S.C. § 1831a(j) (emphasis added).

There are several solutions to this uncertainty problem, the best of which would result from a cooperative effort from all parties. First (as noted above), the OCC could clarify its rules (once we know what state law applies to national bank branches, 12 USC § 1831a(j) defines quite clearly what law applies to the interstate branches of state banks). Second, the relevant parties could sit down and negotiate a *workable* solution that clarifies applicable law and enforcement without facilitating a race to the bottom on consumer protection. Third, courts could begin taking more than a cursory look at the National Bank Act and the OCC's regulations and (upon doing so) provide needed guidance on the scope of National Bank Act preemption. Finally, Congress could act and clarify these issues once and for all (again). Because the petition facilitates none of these solutions, it should be rejected.

The OCC's Recent Regulations Created This Problem

Clearly there is a problem when state banks do not know what state laws apply to their interstate branches. We concur with the Conference of State Bank Supervisors' analysis that this problem derives directly from the OCC's recent preemption rule giving national banks a broad regulatory shield against "state laws that obstruct, impair or condition a national bank's ability to fully exercise its Federally authorized deposit-taking [or lending] powers."[2] It is a domino effect: because no one knows precisely when or whether a particular state law "obstructs, impairs or conditions a national bank's ability to fully exercise its deposit-taking or lending functions," no one knows what state laws apply to national bank branches; and because no one knows what law applies to national bank branches, no one knows what law applies to the interstate branches of state banks.

This problem did not exist between passage of Riegle-Neal and the OCC's promulgating its recent regulations because during that period the OCC followed Riegle-Neal's requirements to make case-by-case "preemption determinations."[3] Under that process, the OCC would review questioned state laws individually, and reach conclusions through an open and transparent process so all interested parties (national *and state* banks) would know whether the National Bank Act preempted a particular state law and could alter their behavior accordingly.

The OCC's recent regulations undermine this transparent process and breed confusion. Because the OCC's regulations now empower national banks to ignore any (unlisted) state laws that "obstruct, impair or condition…" – and courts have thus far broadly deferred to the OCC whenever preemption questions arise – national banks have little incentive to ask for, and the OCC has no incentive to make, formal preemption determinations. National banks can now simply ignore questionable state laws and use the OCC's broad regulations as a safe harbor should litigation ever arise. Hence the current confusion.

The FDIC Is Not In A Position To Solve The OCC's Problem

It is unclear how the FDIC can issue a regulation to address these issues. The Riegle-Neal provision at issue here is entirely self-executing. It neither seeks nor requires federal

[2] 12 C.F.R. §§ 7.4007, 7.4008.
[3] 12 U.S.C. § 43.

regulation as its reach is no more or less than that of the national bank provision from which it follows.

Moreover, an FDIC regulation would do nothing to "fill in the gaps" of the statute. There are no gaps in the provisions: national banks must comply with state consumer protection laws unless they discriminate against national banks or are preempted.[4] If a state law is preempted there are simple mechanisms for letting all interested parties know: either (1) the OCC would issue a case-by-case "preemption determination;" or (2) a court would make a determination and publish its findings for all. There is no ambiguity.

To the extent there is a "gap" in understanding whether a particular state law applies to the interstate branches of state banks, that gap was created by the OCC's misinterpretation of the National Bank Act and its willingness to ignore Riegle-Neal. Unfortunately, no FDIC regulation can change that.

The Petition's Approach Poses Public Policy Problems

While they are a serious effort to address legitimate parity concerns, the solutions offered in the petition would only make the problem worse by extending ambiguity to a new and larger segment of the banking industry, and encourage a race to the bottom among state banks.

Because Riegle-Neal is clear that the law applicable to the interstate branches of state banks is determined by whether that state law applies to national bank branches, and the FDIC has no power to define what laws are applicable to national bank branches, an FDIC regulation could not improve the current situation. Instead of providing greater clarity to state banks, consumers and States, an FDIC regulation could only do harm by extending uncertainty and potentially eliminating the consumer protection laws applicable to others.

While this approach might put state banks on a more even playing field vis-à-vis national banks (ambiguity for all), it would encourage States to join a whole new race to the bottom as institutions moved their charters to less restrictive states to export these (non-existent) consumer protections to the rest of the country. These concerns are heightened by the breadth of some of the petition's legal arguments. For example, the petition attempts to re-define the term "branch" to include a wide array of other banking offices. In addition, it uses an anti-discrimination provision intended to safeguard banks from anti-competitive state laws to justify preemption of state consumer protection laws that are not discriminatory and do not obstruct the business of banking.

While parity is an understandable goal, the right answer cannot be that no state consumer protection laws apply to national or state-chartered institutions and legitimate state authorities have no enforcement rights or responsibilities. Yet that is the direction in which the OCC's ill-advised preemption regulation coupled with this particular approach to achieving parity would take us.

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12 U.S.C. § 36(f).

Going Forward

As noted above, there are several options available for addressing these important concerns:

The most direct solution would be for the OCC to revise its rules and return to the framework created by Congress in Riegle-Neal: eliminate the overly broad "obstruct, impair or condition" language, make explicit what state laws are and are not currently preempted, and publish any future preemption determinations on a case-by-case basis. This system ensures that all the relevant market participants understand what laws apply to national banks and therefore what laws apply to the interstate operations of state chartered banks.

Second, the relevant parties could negotiate a workable solution that: (1) concedes that there are core banking areas where state laws do not apply to national banks and other areas (e.g., consumer protections that do not in any meaningful way impair the business of banking) where they clearly do; (2) establishes a mechanism for informing all the relevant parties when individual laws do not apply and why; and (3) establishes clearly which regulator/regulators (OCC, banking commissioners, attorneys general) are responsible for policing which practices of which institutions.

Third, courts should begin taking more than a cursory look at how the OCC's regulations mesh with the statutory framework. Rather than so readily deferring to the agency under Chevron[5] and Mead,[6] waiting for a problem to arise that is finally too large to ignore, courts should take the time to fully review the National Bank Act, Riegle-Neal and the OCC's regulations and provide real guidance on the scope of National Bank Act preemption.

Finally, Congress could act (again). Last year we introduced, along with several other Members of the House of Representatives, the Preservation of Federalism in Banking Act (H.R. 5251) a bill designed to clarify precisely when and why particular state laws are applicable to national banks. Given the unwillingness of many to come to the table and support this balanced approach, this year we will press again for Congress to act.

We look forward to working with you on this important issue.

BARNEY FRANK

LUIS V. GUTIERREZ

[5] Chevron USA, Inc. v. Natural Resources Defense Counsel, 467 U.S. 837 (1984)

[6] United States v. Mead Corp., 533 U.S. 218 (2001).