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Statement of the Shadow Financial Regulatory Committee

On

Predatory Lending and Federal Preemption of State Laws

September 22, 2003

Even before the beginning of the National Banking System in 1863 issues arose concerning the applicability of state laws to national banks. These issues have persisted despite the Supreme Court holding in *McCulloch v. Maryland* that states “have no power...to retard, impede, burden, or in any manner control, the operations of federal instrumentalities.” Over the years disputes that arose were resolved by the Congress, the courts or the Office of the Comptroller of the Currency (OCC). In response to a recent inquiry concerning the Georgia Fair Lending Act (GFLA), however, the OCC has proposed a regulation that attempts to provide broader guidance concerning the applicability of state laws to the activities of national banks.

The Shadow Financial Regulatory Committee applauds this effort, but the Committee recognizes that this is not a simple task. It has long been clear that some state laws do apply to the activities of national banks. For example, a recent court ruling noted that the states retain the power to regulate national banks in areas such as “contracts, debt collection, acquisition and transfer of property, and taxation, zoning, criminal, and tort law.”

Because national banks are now allowed to branch across state lines and to operate on a national basis, the potential effect of state laws on their operations has become a more significant problem. A bank operating in one state must deal with the applicability of that state’s laws. A national bank operating in many states is potentially exposed to the need to comply with several different sets of laws. Uncertainty as to the applicability of these laws to national banks poses more of a problem for their operations and costs than was the case in earlier times.

The OCC's proposed rulemaking would not preempt state laws that do not materially affect the lending, deposit-taking, or other activities of national banks, such as those cited above, or any other law that the OCC determines does not interfere significantly with the powers of national banks.

The Committee believes that this attempt at setting general rules on the applicability of state laws to national banks is appropriate, and raises the broader issue of whether it is time to consider legislation that would define the extent of explicit federal preemption of state laws regarding consumer protection in the financial activities of federally-chartered institutions. The Committee may consider this broader issue at some future meeting. The Committee believes there are benefits of uniform federal law for the costs and operating efficiency of federally-chartered providers of financial services. The Committee also sees benefits from competition in the regulatory process, and sees the OCC action as helpful in preserving effective and beneficial competition. By the same token, the Committee would not favor federal laws that would prevent the various states from creating or allowing institutions that could provide useful services to consumers that may not be within the powers of national banks.

The Committee does have reservations as to one aspect of the OCC proposed rulemaking in response to the GFLA. The proposed regulation would prohibit national banks from making loans "based predominantly on the foreclosure value of the borrower's collateral, rather than on the borrower's repayment ability, including current and expected income, current obligations, employment status, and other relevant financial resources." The Committee believes that in some cases it would be beneficial for banks and borrowers if the bank were able to make loans equal to a fraction of the value of the collateral without the need to do a thorough credit investigation of the borrower. The wording of the proposed regulation might prevent some cases of predatory real estate lending, but it would also prevent transactions, based on real estate or other collateral, that would benefit bank customers.