HEARING ON "LICENSE TO BANK: EXAMINING THE LEGAL FRAMEWORK GOVERNING WHO CAN LEND AND PROCESS PAYMENTS IN THE FINTECH AGE," SEPTEMBER 29, 2020, BEFORE THE TASK FORCE ON FINANCIAL TECHNOLOGY, COMMITTEE ON FINANCIAL SERVICES, U.S. HOUSE OF REPRESENTATIVES

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Thank you for inviting me to participate in this very important hearing. My testimony today criticizes recent attempts by the Office of the Comptroller of the Currency (OCC) and the Federal Deposit Insurance Corporation (FDIC) to confer banking powers and privileges on nonbanks and commercial firms without requiring those companies to comply with the regulations that govern banks and bank holding companies. For the reasons stated below, I believe that the OCC's and FDIC's initiatives are unlawful and contrary to the public interest. They represent a dangerous form of regulatory arbitrage because they allow nonbanks and commercial firms to evade fundamental principles incorporated in our federal statutory framework for banking institutions. I urge Congress to use its legislative and oversight powers to block OCC's and FDIC's initiatives or persuade the agencies to rescind them.

In July 2018, the OCC announced its intention to approve national bank charters for nondepository fintech firms that provide lending or payment services but do not accept deposits. The New York Department of Financial Services (NYDFS) promptly filed a lawsuit to challenge the OCC's action. In May 2019, a federal district court held that the OCC lacked authority to grant national bank charters to financial institutions that do not accept deposits. The OCC has appealed that decision to the U.S. Court of Appeals for the Second Circuit.[1]

Despite the district court's decision, Acting Comptroller of the Currency Brian Brooks stated in August 2020 that the OCC was ready to "start processing applications for [national bank] charters from payments companies . . . . These could include financial technology firms like PayPal or cryptocurrency exchanges like Coinbase, his former employer." Big technology firms responded with great enthusiasm to the OCC's willingness to approve national bank charters for nondepository providers of payment services. For example, "Financial Innovation Now – a group that represents Amazon, Apple, Google, Intuit, PayPal, Square and Stripe – praised Brooks' 'leadership and vision' in a statement."[2]

In March 2020, the FDIC issued a proposed rule that would allow all types of commercial firms – including the largest technology firms – to acquire FDIC-insured industrial banks and industrial loan companies (collectively "ILCs").[3] If implemented, that rule could have an even greater impact than the OCC's nondepository fintech national bank charter and could transform our financial system and economy. Unlike the OCC's nondepository fintech charter, the FDIC's proposed ILC rule would permit Big Tech giants and other commercial firms to own FDIC-

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[1] *Vullo v. OCC*, 378 F.Supp.3d 271 (S.D.N.Y. 2019), *appeal pending sub nom. Lacewell v. OCC*, No. 19-4271-cv (2d Cir.). Morgan Ricks, Lev Menand, Joseph Sommer, and I served as the drafting committee for an amicus brief filed by 33 banking law scholars in the Second Circuit in support of the NYDFS and in opposition to the OCC. Parts I(A), I(B), and I(C) of my testimony are adapted from that brief, which is available at https://justmoney.org/wp-content/uploads/2020/08/19-4271-Amicus-Brief-of-Banking-Law-Scholars.pdf.

[2] Victoria Guida, "Top regulator pushes ahead with plan to reshape banking, sparking clash with states," *Politico* (Aug. 31, 2020), available at https://www.politico.com/news/2020/08/31/currency-comptroller-reshape-banking-406393 (summarizing Brooks' statement and quoting Financial Innovation Now's statement).

[3] FDIC notice of proposed rulemaking, "Parent Companies of Industrial Banks and Industrial Loan Companies," 85 Fed. Reg. 17771 (Mar. 31, 2020) [hereinafter "FDIC Proposed ILC Rule"]. On April 10, 2020, I filed a comment letter (available at https://www.fdic.gov/regulations/laws/federal/2020/2020-parent-companies-of-industrial-banks-3064-af31-c-002.pdf) opposing the FDIC's proposed rule. I subsequently published an article based on that comment letter. Arthur E. Wilmarth, Jr., "The FDIC Should Not Permit Commercial Firms to Acquire Industrial Banks," 39 *Banking & Financial Services Policy Report* No. 5 (May 2020, at 1-17, available at http://ssrn.com/abstract=3613022 [hereinafter Wilmarth, "Industrial Banks"].

insured, deposit-taking institutions. The proposed ILC rule would also enable commercial owners of ILCs to avoid the limitations and obligations that apply to parent companies of FDIC-insured banks under the Bank Holding Company Act.

In addition, FDIC-insured ILCs have presumptive access to discount window loans, payment and settlement services, and other facilities and benefits offered by the Federal Reserve System (Fed) to depository institutions. In contrast, as discussed below in Part I(B), it is doubtful whether the OCC's nondepository fintech national banks could gain access to the Fed's services and facilities.

The OCC has made two attempts to confer the privileges of national banks on nonbank firms. In June 2020, the OCC adopted a rule declaring that national banks may transfer their federal preemptive immunity from state usury laws to nonbanks that are purchasers, assignees, or transferees of their loans. The OCC's usury preemption transfer rule will shield nonbank purchasers, assignees, and other transferees from all state usury laws except for the laws of the state where the national bank that transferred the loans is "located."[4] Most national banks "locate" their lending operations in states that have few or no usury limits. Accordingly, the OCC's rule effectively provides blanket immunity from state usury laws to all persons who acquire loans from national banks.

In July 2020, the OCC issued a proposed rule that would (1) allow national banks to form lending "partnerships" with nonbank lenders, (2) treat national banks as the "true lenders" for loans produced such "partnerships" if the banks are named as the lenders in the loan agreements

[4] OCC final rule, "Permissible Interest on Loans That Are Sold, Assigned or Otherwise Transferred," 85 Fed. Reg. 33530 (June 2, 2020) [hereinafter OCC Usury Preemption Transfer Rule]. The OCC's rule provides parallel treatment for loans that are sold, assigned or transferred by federal savings associations to nonbanks. I filed a comment letter opposing that rule as proposed in November 2019. Arthur E. Wilmarth, Jr., Comment Letter in Opposition to the OCC's Proposed Valid-When-Made Rule" (Jan. 17, 2020), available at http://ssrn.com/abstract=3523939 [hereinafter Wilmarth Usury Preemption Transfer Comment Letter].

or fund the loans, and (3) permit national banks to maintain their status as "true lenders" even if the banks sell their entire interest in loans to their nonbank "partners" *one day after the loans are made*. The OCC's proposed "true lender" rule would allow national banks to establish "rent-a-charter" schemes with predatory nonbank lenders. Under "rent-a-charter" schemes, banks earn fees by transferring their federal preemptive immunity from state usury laws and other state laws to their nonbank "partners," while the nonbank "partners" assume all or virtually all of the economic benefits and risks of the loans originated through those schemes.[5]

In July 2020, the FDIC adopted a rule allowing FDIC-insured state banks to transfer their federal preemptive immunity from state usury laws to purchasers, assignees, and transferees of their loans. The FDIC's rule is intended to give FDIC-insured state banks the same ability to transfer their preemptive immunity from state usury laws that national banks possess under the OCC's usury preemption transfer rule.[6] The FDIC has not yet proposed a regulation similar to the OCC's "true lender" rule.

Part I of this testimony shows that the OCC's nondepository fintech national bank charter and the FDIC's proposed ILC rule are contrary to federal statutes and policies governing banks and bank holding companies. Part II demonstrates that the OCC's and FDIC's attempts to confer on nonbanks the benefits that banks receive through federal preemption violate federal laws and undermine important public policies. I urge Congress to exercise its legislative and oversight

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[5] OCC notice of proposed rulemaking, "National Banks and Federal Savings Associations as Lenders," 85 Fed. Reg. 44223 (July 22, 2020) [hereinafter OCC Proposed "True Lender" Rule]. The OCC's proposed rule would provide parallel treatment for federal savings associations that form lending "partnerships" with nonbanks. On August 11, 2020, I filed a comment letter opposing the OCC's proposed rule. Arthur E. Wilmarth, Jr., Comment Letter in Opposition to the OCC's "True Lender" Rule (Aug. 11, 2020), available at http://ssrn.com/abstract=3673421 [hereinafter Wilmarth "True Lender" Comment Letter].

[6] FDIC final rule, "Federal Interest Rate Authority," 85 Fed. Reg. 44146 (July 22, 2020) [hereinafter FDIC Usury Preemption Transfer Rule]. On January 17, 2020, I filed a comment letter (available at https://www.fdic.gov/regulations/laws/federal/2019/2019-federal-interest-rate-authority-3064-af21-c-008.pdf) opposing that rule as proposed in November 2019.

powers to overturn the OCC's and FDIC's unauthorized and misguided actions or to persuade the agencies to rescind them.

I. The OCC's Nondepository Fintech Charter and the FDIC's Proposed ILC Rule Violate Federal Laws and Undermine the Separation of Banking and Commerce

As shown below, several federal banking laws prohibit the OCC from granting national bank charters to financial institutions that do not accept deposits. In addition, the OCC's nondepository fintech national bank charter and the FDIC's proposed ILC rule undermine fundamental policies established by federal banking statutes, including the separation of banking and commerce, the avoidance of undue risks to financial stability, the prevention of serious threats to competition, and the protection of consumers and communities.

A. The National Bank Act Requires National Banks to Accept Deposits in Order to Conduct the "Business of Banking"

Congress passed the National Bank Act of 1864 (NBA) to establish a uniform national currency in the form of bank notes issued by national banks.[7] The NBA also helped the federal government to finance the Civil War by requiring national banks to purchase and hold government bonds as liquidity reserves for their liabilities created by bank notes and deposits.[8] The NBA required each national bank to hold federal government bonds and other "lawful money of the United States" in an amount equal to a specified percentage of "its notes in circulation and its deposits."[9]

Since 1864, deposit-taking has been an essential part of the "business of banking" conducted by national banks. Since 1864, the NBA has authorized the OCC to issue national

[7] *See* Bray Hammond, *Banks and Politics in America, from the Revolution to the Civil War* 723-27 (1957); Edward L. Symons, Jr., "The Business of Banking in Historical Perspective," 51 *George Washington Law Review* 676, 699 (1983).
[8] Hammond, *supra* note 7, at 724, 731-32; Symons, *supra* note 7, at 699.
[9] Act of June 3, 1864, ch. 106, § 31, 13 Stat. 108; *see also id.* § 16, 13 Stat. 104 (requiring each national bank to deposit a minimum amount of federal government bonds with the U.S. Treasury).

bank charters only if the OCC determines that each proposed national bank "is lawfully entitled to commence the business of banking."[10] Since 1864, the NBA has defined "the business of banking" to include the activities of "receiving deposits," making loans, paying ("discounting") negotiable instruments and other evidences of debt, buying and selling "bullion" and foreign exchange, and obtaining and issuing circulating bank notes, along with "all such incidental powers as shall be necessary to carry on the business of banking."[11] Since 1864, the NBA has required every national bank to identify in its organization certificate "[t]he place where its operations of discount and deposit are to be carried on."[12]

The NBA's designation of deposit-taking as a crucial aspect of "the business of banking" reflects the fundamental role of bank deposits in our monetary system and economy. Banks increase our nation's money supply by issuing deposits. Banks use deposits as a funding device for extending loans and purchasing investment securities.[13] Bank customers use deposits as a vehicle for savings and for making payments to others. Under federal law, only banks and other chartered depository institutions are allowed to issue deposits.[14]

Thus, banks perform essential functions through their issuance of deposits. Bank deposits expand our money supply and support our economy by funding loans and investments, promoting savings, and facilitating payments by businesses and consumers to other persons.[15]

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[10] 12 U.S.C. § 27(a) (derived from § 18 of the NBA of 1864, 13 Stat. 104-05).

[11] 12 U.S.C. § 24 (Seventh) (derived from § 8 of the NBA of 1864, 13 Stat. 101-02). As discussed below in Part I(B), the function of issuing a national currency in the form of circulating notes was transferred from national banks to the Federal Reserve System after 1913.

[12] 12 U.S.C. § 22 (Second) (derived from §6 (Second) of the NBA of 1864, 13 Stat. 101).

[13] *United States v. Philadelphia National Bank*, 374 U.S. 321, 326 (1963) ("Commercial banks are unique among financial institutions in that they alone are permitted by law to accept demand deposits. This distinctive power gives commercial banking a key role in the national economy. For banks do not merely deal in but are actually a source of, money and credit; when a bank makes a loan by crediting the borrower's demand deposit account, it augments the Nation's credit supply."); *see also* Milton Friedman, "The Euro-Dollar Market: Some First Principles," 7 *Review* 16 (Fed. Res. Bank of St. Louis, July 1971).

[14] 12 U.S.C. § 378(a).

[15] *See* E. Gerald Corrigan, "Are Banks Special? A Revisitation" (Fed. Res. Bank of Minneapolis, Mar. 1, 2000), available at https://www.minneapolisfed.org/article/2000/are-banks-special; John L. Douglas, "The Role of a

Federal courts have repeatedly identified deposit-taking as an "essential" element of the "business of banking" authorized by the NBA and other federal statutes.[16] The power to accept deposits is a special privilege conferred by federal and state governments on banks and other depository institutions through a demanding chartering process. That special privilege also warrants the comprehensive regime of regulation and supervision that federal and state governments impose on banks and other depository institutions.[17]

In 1975, the OCC took an unprecedented step by approving a national bank charter for a special-purpose trust company. That trust company that did not accept deposits other than trust funds and did not exercise any other non-fiduciary powers. A district court invalidated the OCC's special-purpose trust charter, holding that it violated the NBA's requirement that all national banks must engage in the "business of banking."[18] In response to that court decision, Congress amended Section 27(a) of the NBA in 1978. That 1978 amendment allowed the OCC

Banking System in Nation-Building," 60 *Maine Law Review* 511, 513-19 (2008); *see also* Morgan Ricks, "Money as Infrastructure," 2018 *Columbia Business Law Review* 757, 758-72 (describing the "competing paradigms" that view banks as "monetary institutions" or as "financial intermediaries," and explaining why those paradigms are "not strictly incompatible" and "coexist in uneasy tension").

[16] *Mercantile National Bank v. New York*, 121 U.S. 138, 156 (1887) (The "business of banking" under the NBA includes "receiving deposits payable on demand"); *In re Prudence Co*., 79 F.2d 77, 79 (2d Cir.), *cert. denied*, 296 U.S. 646 (1935) ("[T]he power to receive deposits . . . is generally recognized as the essential characteristic of a banking business."); *Gamble v. Daniel*, 39 F.2d 447, 450 (8th Cit. 1930) (In 1910, Congress recognized that "the ordinary conception of a bank was of a business which was based primarily on the receipt of deposits (general or special), which deposits were used by the bank for loans, discounts, buying and selling commercial paper, and other business purposes.").

[17] *Philadelphia National Bank*, 374 U.S. at 326-27 ("[A]mong [the roles played by banks], the creation of additional money and credit, the management of the checking-account system, and the furnishing of short-term business loans would appear to be the most important. For the proper discharge of these functions is indispensable to a healthy national economy. . . . It is therefore not surprising that commercial banking in the United States is subject to a variety of governmental controls, state and federal."); *Noble State Bank v. Haskell*, 219 U.S. 104, 112-13 (1911) (holding that the "public interest[]" in "mak[ing] the currency of checks secure" is "sufficient to warrant the state in taking the whole business of banking under its control"); S. Rep. No. 1482, 89th Cong., 2nd Sess. 5 (1966) (justifying Congress's decision to grant extensive enforcement powers to federal banking agencies by explaining that the "banking system is a fundamental part of our monetary system and the Nation's $130 billion of demand deposits represents the principal element in the Nation's money supply").

[18] *National State Bank v. Smith*, 1977 U.S. Dist. LEXIS 18184 (D.N.J., Sept. 16, 1977). As provided in 12 U.S.C. § 1815(a)(1), trust funds are not "deposits." In contrast to deposits, trust funds do not augment the nation's money supply. Trust funds must be held in segregated accounts established in accordance with customers' trust instruments and federal and state fiduciary laws. Unlike deposits, trust funds cannot be used by a bank or trust company to make loans or investments for its own account. *See* 12 U.S.C. § 92a(a)-(d); 12 C.F.R. §§ 9.8-9.13, 9.18.

to approve national bank charters for special-purpose, nondepository trust companies.[19] Based on that narrowly-tailored provision, a federal appellate court upheld the OCC's special-purpose trust company charter.[20]

Congress's 1978 amendment to Section 27(a) confirms that the NBA does not authorize the OCC to approve nondepository charters for national banks *other than* special-purpose trust companies.[21] If the OCC possessed a general power to charter nondepository national banks, the 1978 amendment to Section 27(a) would have been redundant and unnecessary surplusage. Under two well-established canons of statutory construction – the canon against surplusage and the associated canon of *expressio unius est exclusio alterius* (the naming of one thing excludes other similar things), the OCC's claim of a general authority to charter nondepository national banks is indefensible.[22]

The OCC rests its claim of authority to charter nondepository national banks on Section 36 of the NBA. However, Section 36 was not added to the NBA until 1927 – more than 60 years after the NBA's enactment. Section 36 deals only with the authority of national banks to establish *branches*. Section 36 says nothing about the chartering of *banks*, and it does not refer to "the business of banking." The OCC did not assert any chartering authority under Section 36

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[19] The 1978 amendment to Section 27(a) provides that a national bank "is not illegally constituted solely because its operations are . . . limited to those of a trust company and activities related thereto." Pub. L. 95-630, § 1504, 92 Stat. 3713 (1978) (codified as amended at 12 U.S.C. § 27(a)).
[20] *National State Bank v. Smith*, 591 F.2d 223, 231-32 (3d Cir. 1979).
[21] *See Vullo v. OCC*, 378 F.Supp.3d at 294-95.
[22] *See Independent. Ins. Agents of America v. Hawke*, 211 F.3d. 638, 641-45 (D.C. Cir. 2000) (holding that the NBA's specific authorization for national banks to sell insurance in towns with populations of 5,000 or less precluded the OCC from allowing national banks to sell crop insurance in larger communities); *American Land Title Ass'n v. Clarke*, 968 F.2d 150, 155-57 (2d Cir. 1992) (determining on similar grounds that the OCC could not permit national banks to sell title insurance in larger communities), *cert. denied*, 508 U.S. 971 (1993); *see also Vullo*, 378 F.Supp.3d at 295 (concluding, based in part on the 1978 amendment to Section 27(a), that Congress "understood the NBA's original use of the 'business of banking' phrase to require deposit-receiving, such that a non-depository institution (or class of such institutions) is not considered eligible to be granted a federal charter to commence the 'business of banking' absent a statutory amendment to the contrary").

until 2003, and the OCC did not take any definitive steps to implement that asserted authority until 2016.[23]

Section 36 defines a "branch" as a location "at which deposits are received, or checks paid, or money lent."[24] Based on the disjunctive word "or" in Section 36, the OCC argues that it can charter national banks that engage in lending or payment activities but do not accept deposits. However, a branch is a *subset* of a national bank, and Section 36 merely authorizes a branch to exercise a subset of "the business of banking." The fact that a national bank may lawfully establish a subsidiary *branch* without accepting deposits has no bearing on whether the OCC may lawfully charter a *bank* that does not accept deposits.

In contrast to Section 36, Section 24 (Seventh) of the NBA uses the conjunctive word "and" when it identifies the activities – including "receiving deposits" – that are part of "the business of banking." The activities specified in Section 24 (Seventh) include *all three* of the functions listed in Section 36. Viewed in combination with Section 22 (Second) – which requires every national bank to identify "[t]he place where its operations of discount and deposit are to be carried on" – as well as Section 27(a) – which forbids the OCC from chartering banks that are not "lawfully entitled to commence the business of banking" – Section 24 (Seventh) plainly bars the OCC from chartering nondepository national banks *other than* special-purpose trust companies.[25]

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[23] *See Vullo*, 378 F.Supp.3d at 279, 288-90, 295-96 ("The Court finds that a delay of that length" in asserting chartering authority under Section 36 "provides substantial grounds to cast doubt on OCC's interpretation" of Section 36).
[24] 12 U.S.C. § 36.
[25] *See Vullo v. OCC*, 378 F.Supp.3d at 297-98 ("receiving deposits is an indispensable part of the 'business of banking' as used by Congress in the original phrase that now appears in Section 27 and Section 24 (Seventh)"); *see also* Symons, *supra* note 7, at 721 and 721-22 note 239 (discussing "the critical importance of the deposit-taking power to the determination of an entity as a bank").

As the district court pointed out in *Vullo*, the OCC's nondepository fintech charter could have a major "impact . . . on at least 'a significant portion' of the national economy" by causing a "dramatic disruption of federal-state relationships in the banking industry." The OCC's fintech charter threatens to preempt a broad array of state financial regulations (including state licensing and supervisory standards) and other state consumer protection laws (including state usury laws), which currently apply to nonbank providers of lending and payment services.[26] In addition, the OCC could conceivably assert that fintech "banks" are exempt from state privacy and data protection laws.[27] Thus, the OCC's fintech charter threatens to abrogate the longstanding federal policy of allowing states to regulate nonbank firms that provide lending, payment, and other financial services within their borders.[28]

The OCC's fintech charter would severely undermine the states' authority to enforce laws that protect their residents against abusive, deceptive, and exploitative practices by nonbank providers of lending and payment services. As the NYDFS pointed out in its Complaint in *Vullo*, "preemption of state law governing mortgage lenders and servicers" by the OCC and the Office of Thrift Supervision during the 1990s and 2000s "was a root cause of the global financial collapse," combined with the failures by federal regulators to protect consumers against predatory lending and foreclosure practices.[29] Congress should not allow the OCC to repeat its

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[26] *Vullo*, 378 F.Supp.3d at 286-88, 296 (citing and quoting the NYDFS' Complaint, ¶¶ 3, 11-12, 35, 43-49).
[27] As discussed in Part II(B), the OCC has authority to issue regulations or orders preempting state consumer financial laws if those state laws would "prevent or significantly interfere" with the federally-authorized powers of national banks. *See* 12 U.S.C. § 25b(b)(1)(B). If the OCC issues national bank charters to nondepository fintech firms, the OCC could potentially issue preemptive rules or orders claiming that state privacy or data protection laws "prevent or significantly interfere" with the lending and payment activities of those firms.
[28] *See, e.g.*, 12 U.S.C. §§ 5551-5552; *Meade v. Avant of Colorado LLC*, 307 F.Supp.2d 1134 (D. Colo. 2018); *West Virginia v. CashCall*, 605 F.Supp.2d 781 (S.D. W. Va. 2009).
[29] NYDFS Complaint in *Vullo*, ¶ 12; *see also* S. Rep. No. 111-176, at 11-18, 175-76 (2010); Kathleen Engel & Patricia A. McCoy, *The Subprime Virus: Reckless Credit, Regulatory Failure, and Next Steps* 157-226 (Oxford University Press, 2011); Lev Menand, "Too Big to Supervise: The Rise of Financial Conglomerates and the Decline of Discretionary Oversight in Banking," 103 *Cornell Law Review* 1527, 1529-32, 1551-74 (2018); Arthur E. Wilmarth, Jr., "The Dodd-Frank Act's Expansion of State Authority to Protect Consumers of Financial Services," 36

disastrous pattern of preemptive overreach and regulatory laxity that contributed to the catastrophic events of 2007-09.

The OCC's fintech chartering initiative offers federal corporate charters to a wide range of nonbank firms that provide lending and payment services. Big Tech giants like Alphabet (Google), Amazon, Apple, Facebook, and Microsoft could potentially operate under OCC charters if they decide to establish significant lending or payment programs. Currently, Big Tech giants and other nonbank firms must operate under state corporate charters and must comply with state corporate governance laws. The OCC's attempt to expand its federal chartering authority beyond deposit-taking national banks is untenable in view of numerous court decisions that have *refused* to construe federal statutes in a manner that would override "established state policies of corporate regulation" absent clear evidence of congressional intent.[30] As shown above, Congress has never expressed an intent to allow the OCC to grant national bank charters to nondepository firms *except for* special-purpose trust companies.

B. The Federal Reserve Act Confirms That National Banks Must Operate as Depository Institutions

Congress enacted the Federal Reserve Act of 1913 (FRA) to establish the Federal Reserve System (Fed) as the nation's new monetary authority. Congress directed the Fed to establish a "sound" and "flexible" national currency in the form of Federal Reserve notes. Federal Reserve notes gradually replaced the "bond-secured note[s]" issued by national banks under the NBA.[31] Congress also instructed the Fed to clear and pay (at par) checks drawn by

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Journal of Corporation Law 893, 897-919 (2011) [hereinafter Wilmarth, "Dodd-Frank"], available at http://ssrn.com/abstract=1891970.

[30] *Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 478-80 (1977); *accord, e.g.*, *Business Roundtable v. SEC*, 905 F.2d 406, 411-17 (D.C. Cir. 1990); *Field v. Trump*, 850 F.2d 938, 947 (2d Cir. 1988), *cert. denied*, 489 U.S. 1012 (1989); *Panter v. Marshall Field & Co*., 646 F.2d 271, 289 (7th Cir.), *cert. denied*, 454 U.S. 1092 (1981).

[31] H.R. Rep. No. 63-69, at 16-19, 22-26 (1913); *see also First Agricultural Bank v. State Tax Comm'n*, 399 U.S. 339, 355-56 (1968) (Marshall, J., dissenting) (explaining that national banks "ceased" issuing bank notes by 1935).

depositors on national banks and state banks that were members of the Fed (state member banks). The Fed's duty to clear and pay checks reflected the fact that bank deposits had become a major component of the U.S. money supply by 1913.[32]

The FRA provides that Federal Reserve notes must be "receivable by all national and [state] member banks."[33] Congress included that mandate to ensure that Federal Reserve notes would be "payable . . . to any [member] bank for deposit purposes," thereby making each member bank a "quasi-redemption" facility for those notes.[34] The duty of all Fed member banks to receive Federal Reserve notes as deposits demonstrated Congress's understanding that all national banks were depository institutions.

Since 1913, the FRA has required every national bank to become a member bank of the Federal Reserve System and to purchase stock in its respective regional Federal Reserve Bank. National banks that do not fulfill those commitments must forfeit their charters.[35] The FRA's provisions requiring national banks to become member banks, to buy stock in their Federal Reserve Banks, and to accept Federal Reserve notes as deposits were crucial elements of the FRA's design for an effective monetary system and national currency.[36] Congress recognized that "the Federal Reserve System could not function without national banks, which are required to be members therein, 12 U.S.C. § 222, and in that sense they are part and parcel of the establishment and effectuation of the national fiscal and monetary policies."[37]

Congress formally abolished the power of national banks to issue bank notes in 1994. Pub. L. 103-325, §§ 602(e)-(g), 108 Stat. 2291-94 (1994).

[32] Act of Dec. 23, 1913 § 16, 38 Stat. 268 (codified as amended at 12 U.S.C. § 360); *see also* H.R. Rep. No 63-69, at 55-56.

[33] Act of Dec. 23, 1913, § 16, 38 Stat. 265 (codified as amended at 12 U.S.C. § 411).

[34] H.R. Rep. No. 63-69, at 26, 54-55 (1913).

[35] Act of Dec. 23, 1913, § 2, 38 Stat. 252-53 (codified as amended at 12 U.S.C. §§222, 282, 501a).

[36] H.R. Rep. No. 63-69, at 16-19, 31-37, 39-41 (1913); *see also Federal Reserve System: Purposes and Functions* 3-6, 9, 12-17, 35, 38-44 (10th ed. 2016) [hereinafter *Fed Purposes and Functions*].

[37] *First Agricultural National Bank*, 392 U.S. at 357 (Marshall, J., dissenting).

Deposits held by national banks and other federally-regulated depository institutions play important roles in the Fed's implementation of monetary policy. National banks and other depository institutions must maintain reserves against their deposits in accordance with the Fed's regulations.[38] Bank reserve requirements are one of the "primary means through which the [Federal Reserve] System implements monetary policy."[39] Other standard mechanisms for implementing the Fed's monetary policy (including open-market operations and discount window lending) also operate through the Fed's relationships and transactions with national banks and other depository institutions.[40]

The Fed frequently conducts monetary policy by adjusting its target for the federal funds rate – the interest rate at which depository institutions borrow from and lend to each other overnight in the federal funds market. To influence the federal funds rate, the Fed changes the rate of interest that it pays on reserve balances maintained by depository institutions in excess of their required reserves.[41] Thus, the Fed relies on national banks and other depository institutions to perform a vitally important function as a "transmission belt for monetary policy."[42]

National banks and other depository institutions enjoy a privileged relationship with the Fed, and they receive highly beneficial services from the Fed. The Fed provides loans to depository institutions through the discount window. The Fed also permits depository institutions to establish master accounts that give them direct access to the Fed's real-time payment system (Fedwire) and its securities custody and settlement services.[43]

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[38] Act of Dec. 23, 1913, § 19, 38 Stat. 270 (codified as amended at 12 U.S.C. § 461).
[39] *Committee for Monetary Reform v. Board of Governors*, 765 F.2d 538, 539 (D.C. Cir. 1985).
[40] *Fed Purposes and Functions*, *supra* note 36, at 17, 38-44.
[41] *Id.* at 23, 38-40, 50-51; Ricks, *supra* note 15, at 786-90.
[42] Corrigan *supra* note 15; *see also Fed Purposes and Functions*, *supra* note 36, at 17 (explaining that depository institutions perform "important roles in the Federal Reserve System's core functions"); Ricks, *supra* note 15, at 772-801 (describing the changing roles that banks have played in the Fed's implementation of monetary policy before and after 2008).
[43] *Fed Purposes and Functions*, *supra* note 36, at 40-46, 130-34.

As shown above, the FRA embodies Congress's clear understanding that national banks must be depository institutions to fulfill their intended functions within the Federal Reserve System. Consequently, the OCC's nondepository fintech national bank charter creates massive conflicts with the FRA's design. Financial firms that receive fintech charters could potentially argue that they have the automatic right to become Fed member banks, and that they are eligible for all the benefits and services that the Fed provides to depository member banks.[44] The Fed has not yet expressed any position on whether it would be willing to recognize the OCC's nondepository fintech "banks" as Fed member banks.[45]

If nondepository fintech "banks" obtained recognition as Fed member banks, they would immediately qualify for loans from the Fed's discount window. Such an outcome would destroy the vital distinction established by Congress between the broad support that the Fed provides to depository institutions through the discount window and the much more limited assistance that the Fed can offer to nondepository firms. Under Section 13(3) of the FRA, as amended in 2010, "nondepository institutions" may receive loans from the Fed only (1) in "unusual and exigent circumstances," (2) pursuant to a program or facility creating "broad-based eligibility" for nondepository borrowers that are "not insolvent," and (3) with the approval of a supermajority of the Federal Reserve Board and the Secretary of the Treasury.[46] Allowing nondepository fintech national banks to obtain loans through the discount window would seriously undermine Congress's intention to impose significant procedural and substantive limitations on the Fed's authority to provide loans to nondepository firms.

[44] *See* 12 U.S.C. § 222 (requiring all national banks to become Fed member banks); *id.* § 301 (requiring the Fed to carry out its duties under the FRA "fairly and impartially and without discrimination in favor of or against any member bank or banks").
[45] *See* Guida, *supra* note 2.
[46] 12 U.S.C. § 343; *see also Fed Purposes and Functions*, *supra* note 36, at 64.

If nondepository fintech national banks achieved the status of Fed member banks, they could establish master accounts that provide access to the Fed's payment services (including Fedwire) as well as the Fed's custody and settlement services. Fedwire provides real-time payments and guaranteed finality – important privileges that are currently available only to depository institutions. Depository institutions can also obtain intraday overdraft credit from the Fed.[47] Granting nondepository fintech national banks access to the Fed's payment and settlement services and overdraft credit would violate Congress's intent that only depository institutions should receive the benefits and services authorized by the FRA.

Obtaining access to the Fed's benefits and services would give nondepository fintech "banks" major advantages over nonbank competitors that could not obtain fintech charters. Allowing nondepository fintech "banks" to obtain and exploit such competitive advantages would be contrary to the public policies embodied in the NBA and FRA. In addition, as explained below in Part I(D), the OCC's fintech charter would allow fintech "banks" to evade a number of important regulatory requirements and public interest safeguards that apply to FDIC-insured depository institutions and their parent companies.

The OCC's nondepository national bank charter would also permit Big Tech giants and other technology firms to influence our monetary and economic policies. National banks and other Fed member banks elect six of the nine directors of each Federal Reserve Bank. Half of the directors elected by member banks participate in selecting the presidents of the twelve Federal Reserve Banks. Five of those presidents serve as voting members of the Federal Open Market Committee (FOMC), which establishes the Fed's monetary policy. The other seven presidents attend the FOMC's meetings and participate in its discussions.[48] If the OCC's

[47] *Fed Purposes and Functions*, *supra* note 36, at 131-34, 146-48.
[48] *See* 12 U.S.C. §§ 304, 341 (Fifth); *Fed Purposes and Functions*, *supra* note 36, at 12-17.

nondepository "fintech" banks were recognized as Fed member banks, they could influence the FOMC's deliberations and decisions on monetary policy through their selection of directors and presidents of Federal Reserve Banks. Allowing Big Tech giants and other technology firms to play such a role would contradict the FRA's fundamental policies.

C. The Federal Deposit Insurance Act Requires National Banks to Obtain Federal Deposit Insurance

The Banking Acts of 1933 and 1935 established a federal deposit insurance program and created the FDIC to administer that program. The 1933 and 1935 Acts mandated that all national banks must become members of the FDIC.[49] Similarly, the Federal Deposit Insurance Act of 1950 (FDI Act) required every national bank "engaged in the business of receiving deposits other than trust funds" to obtain deposit insurance.[50] National banks that fail to obtain deposit insurance must forfeit their charters.[51]

The OCC's claim of plenary authority to charter nondepository national banks is completely unfounded, given Congress's explicit mandate that national banks must obtain deposit insurance. The only national banks that currently operate without deposit insurance are nondepository, special-purpose trust companies.[52] As explained in Part I(A), those institutions are expressly permitted by Congress's 1978 amendment to Section 27(a) of the NBA.

The statutory requirement that all *other* national banks must obtain deposit insurance is consistent with Congress's understanding that deposit-taking is an essential element of the

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[49] Act of June 16, 1933, § 8, 48 Stat. 162, 168-70; Act of Aug. 23, 1935, § 101, 49 Stat. 684, 687.
[50] Act of Sept. 21, 1950, § 4, 64 Stat. 873, 875. The only national banks that were exempted from the deposit insurance mandate were "national nonmember banks" located in U.S. territories. Act of Sept. 21, 1950, §§ 3(e), 4(b), 64 Stat. 874, 875-76. When Alaska and Hawaii were admitted as states in 1958 and 1959, Congress amended 12 U.S.C. § 222 to confirm that national banks located in those former territories must become Fed member banks and obtain FDIC insurance, just like the national banks located in the other 48 states. Act of July 7, 1958, § 19, 72 Stat. 350; Act of Mar. 18, 1959, § 17, 73 Stat. 12.
[51] 12 U.S.C. §§ 222, 501a.
[52] *See* OCC Proposed Rule, "Receiverships for Uninsured National Banks," 81 Fed. Reg. 62835 (2016) ("There are only a small number of uninsured national banks in operation today. … [A]ll of these institutions are trust banks.").

"business of banking" under both the NBA and the FRA. As shown above in Parts I(A) and I(B), Congress has identified deposit-taking as the crucial and dispositive function that distinguishes banks from nonbanks. Indeed, Section 21(a)(2) of the Banking Act of 1933 imposes criminal penalties on any person who engages in "the business of receiving deposits" without being chartered and regulated as a depository institution.[53]

D. The OCC's Fintech Charter and the FDIC's Proposed ILC Rule Pose Serious Threats to the Bank Holding Company Act's Policy of Separating Banking and Commerce

1. The BHC Act's Mandate for Separating Banking and Commerce

The BHC Act regulates all "companies" that control "banks."[54] The original BHC Act of 1956 applied to companies that controlled two or more banks. In 1970, Congress expanded the BHC Act's scope to include all companies that control a single bank.[55]

Section 4 of the BHC Act prohibits banks from controlling commercial firms, and it also bars commercial firms from controlling banks. Section 4 embodies our nation's "longstanding policy of separating banking from commerce."[56] The BHC Act prohibits affiliations between banks and commercial firms because those affiliations pose significant dangers, including (1) undue concentrations of economic and financial power, (2) conflicts of interest that destroy the ability of banks to act objectively in providing loans and other services, and (3) unacceptable risks to the federal "safety net" for banks, including the FDIC's deposit insurance fund, the Fed's

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[53] 12 U.S.C. § 378(a).
[54] 12 U.S.C. § 1841(b) & (c).
[55] *See* Arthur E. Wilmarth, Jr., "Wal-Mart and the Separation of Banking and Commerce," 39 *Connecticut Law Review* 1539, 1566-69 (2007), available at http://ssrn.com/abstract=984103 [hereinafter Wilmarth, "Wal-Mart"].
[56] 12 U.S.C. § 1843; *see* S. Rep. No. 91-1084, at 2-4 (1970) (quote at 3); S. Rep. No. 100-19, at 2 (1987) ("At the foundation of American financial law is a longstanding tradition of separating banking and commerce.").

discount window, the Fed's guarantees for interbank payments made on Fedwire, and the Fed's overdraft credit facility for depository institutions.[57]

The 1970 amendments to the BHC Act changed the definition of "bank" to include financial institutions that both accepted demand (business checking) deposits and made commercial loans. In 1980, the OCC began to charter "nonbank banks" – national banks that refrained from either accepting demand deposits or making commercial loans. By omitting one of those functions, nonbank banks enabled their parent companies to evade regulation under the BHC Act. The OCC allowed many commercial firms to acquire "nonbank banks," thereby threatening the BHC Act's policy of separating banking and commerce.[58]

In 1987, Congress closed the "nonbank bank loophole" and strongly criticized the OCC's efforts to undermine the BHC Act. Congress amended the definition of "bank" under the BHC Act to include all FDIC-insured banks (as well as any other banks that accept demand deposits and make commercial loans), subject to narrowly-defined exceptions.[59] The Senate committee report on the 1987 legislation declared that "[n]onbank banks undermine the principle of separating banking and commerce, a policy that has long been the keystone of our banking system." The report also explained that Congress was closing the nonbank bank loophole to

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[57] S. Rep. No. 91-1084, at 2-4 (1970); S. Rep. No. 100-19, at 2, 8-10 (1987); Wilmarth, "Wal-Mart," *supra* note 55, at 1566-71.

[58] *Independent Bankers Ass'n of America v. Conover*, 1985 U.S. Dist. LEXIS 22529, at *2 -*6 (M.D. Fla. Feb. 15, 1985); S. Rep. No. 100-19, at 5-7 (1987).

[59] The BHC Act's definition of "bank," as amended in 1987, includes exemptions for state-chartered ILCs, special-purpose trust companies, and limited-purpose credit card banks (which cannot maintain any checking accounts or accept any time deposits smaller than $100,000 and may only provide business credit card loans to small firms), as well as thrift institutions and credit unions (which are subject to separate regulatory regimes). *See* Pub. L. No. 100-86, § 101(a), 101 Stat. 552, 555-56 (codified as amended at 12 U.S.C. § 1841(c)); S. Rep. No. 100-19, at 11, 29-31 (1987). For discussions of the exemptions in the BHC Act for special-purpose trust companies and state-chartered ILCs, *see infra* notes 61, 63-70 and accompanying text.

"minimize the concentration of financial and economic resources" and improve "the safety and soundness of our financial system."[60]

2. The OCC's Fintech Charter Would Allow Technology Firms to Evade the BHC Act's Prohibition Against Combinations of Banking and Commerce

The OCC's nondepository fintech national bank charter represents the latest attempt by the OCC to evade the BHC Act and undermine the separation of banking and commerce. Congress made clear in 1987 that the OCC had no authority to create new types of national bank charters that would allow combinations of banking and commerce. As discussed above, the 1987 amendments to the BHC Act shut down the "nonbank bank loophole." In addition, while the 1987 amendments exempted nondepository, special-purpose trust companies from the BHC Act's definition of "bank," the 1987 amendments also stipulated that special-purpose trust companies would lose that exemption if they received discount window loans or payment services from the Fed.[61]

Parent companies of the OCC's nondepository fintech national banks would escape regulation under the BHC Act. Fintech national banks would not be FDIC-insured institutions, and they would not accept demand deposits. Consequently, fintech national banks would not be treated as "banks" under the BHC Act. Big Tech giants and other commercial firms could acquire nondepository fintech national banks and avoid any regulation under the BHC Act.

As discussed above in Part I(B), fintech national banks could offer lending and payment services and could potentially claim all of the privileges provided to national banks under the FRA – including access to the Fed's discount window loans, payment and settlement services, guarantees for payments made on Fedwire, and overdraft credit. If fintech national banks

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[60] S. Rep. No. 100-19, at 2, 6-10 (1987) (quote at 8).
[61] *See* 12 U.S.C. § 1841(c)(2)(D)(iv); S. Rep. No. 100-19, at 29 (1987).

achieved status as Fed member banks, ownership of those banks by Big Tech giants and other commercial enterprises would expose major components of the federal safety net to the risks posed by their unregulated parent companies. That outcome would severely compromise the BHC Act's fundamental principle of separating banking and commerce to protect the federal safety net from risks and losses generated by commercial firms.

In addition to avoiding the BHC Act's prohibition on commercial ownership of banks, fintech national banks and their owners would evade a number of other important regulatory requirements and public interest safeguards that apply to FDIC-insured depository institutions and their parent companies. For example, FDIC-insured depository institutions and their parent companies must comply with (1) capital requirements and other safety and soundness standards for depository institutions pursuant to 12 U.S.C. §§ 1831p-1 and 3901-07; (2) prompt corrective action rules for depository institutions under 12 U.S.C. § 1831*o*; (3) "source of strength" commitments for parent companies under 12 U.S.C. § 1831*o*-1; (4) capital requirements for parent companies under 12 U.S.C. § 5371; (5) the FDIC's conservatorship and receivership powers over FDIC-insured depository institutions under 12 U.S.C. §§ 1821-23; and (6) duties of depository institutions under the Community Reinvestment Act, 12 U.S.C. §§ 3901-08.

The OCC's nondepository fintech "banks" would not be subject to any of the foregoing regulatory requirements and public interest safeguards because they would not be FDIC-insured depository institutions.[62] Thus, the OCC's fintech national bank charters would allow Big Tech firms and other commercial enterprises to engage in unconscionable regulatory arbitrage. Congress should prevent the OCC from issuing such charters.

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[62] *See* OCC, *Exploring Special Purpose National Bank Charters for Fintech Companies* (Dec. 2016), at 6-7, 12, available at https://www.occ.gov/publications-and-resources/publications/banker-education/files/exploring-special-purpose-nat-bank-charters-fintech-companies.html.

3. The FDIC's Proposed ILC Rule Poses a Grave Threat to the Separation of Banking and Commerce

The FDIC's proposed ILC rule poses an even more dangerous threat to the BHC Act's policy of separating banking and commerce. Unlike the OCC's nondepository fintech national banks, ILCs are FDIC-insured, state-chartered institutions that are authorized to accept all types of deposits except for demand (business checking) accounts. The ILC charter is the only vehicle that arguably allows commercial firms to own FDIC-insured depository institutions without violating the BHC Act.[63]

The FDIC's Proposed ILC Rule states that "the industrial bank exemption in the [BHC Act] . . . provides an avenue for commercial firms to own or control a bank."[64] However, there is no evidence indicating that Congress intended or expected that the 1987 exemption for ILCs would lead to widespread acquisitions of ILCs by large commercial firms. In 1987, ILCs were small, locally-focused institutions that offered deposit and credit services to lower- and middle-income consumers. ILCs held only $4.2 billion of assets in 1987, and the largest ILC had less than $420 million of assets. A 1993 report from the Congressional Research Service (CRS) stated that ILCs played only a "minor" role in the U.S. financial system.[65]

In July 2005, Walmart, the largest U.S. retailer, applied to acquire an FDIC-insured, Utah-chartered ILC. Walmart's application triggered vigorous public opposition as well as extensive debates about the desirability of allowing large commercial firms to own ILCs. During one of the FDIC's public hearings on Walmart's application in April 2006, Senator Jake Garn (R-UT) – the sponsor of the 1987 exemption for ILCs – stated that "it was never my intent, as the

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[63] *See* 12 U.S.C. § 1841(c)(2)(H); Wilmarth, "Wal-Mart," *supra* note 55, at 1549-53, 1572-73.
[64] 85 Fed. Reg. at 17772.
[65] In 1992, U.S. banks and trust companies held total assets of $3.5 trillion – 500 times larger than the $7 billion of assets held by ILCs. Wilmarth, "Industrial Banks," *supra* note 3, at 2 (quoting the 1993 CRS report).

author of this particular section, that any of these industrial banks be involved in retail [commercial] operations."[66]

In response to the strong public opposition against Walmart's application, the FDIC imposed a six-month moratorium on acquisitions of ILCs by commercial firms in July 2006. In its moratorium notice, the FDIC observed that the "evolution" of the "ILC industry" was occurring "in ways that may not have been anticipated at the time [Senator Garn's exemption] was enacted in 1987." In January 2007, the FDIC extended its moratorium for an additional year. In the FDIC's moratorium extension notice, the agency pointed out that "business plans" for ILCs owned by commercial firms "differ substantially from the consumer lending focus of the original industrial banks."[67]

Walmart withdrew its ILC application in March 2007, due to the FDIC's extended moratorium and continued public hostility toward Walmart's application. The magnitude of the public outcry against Walmart's proposed ILC – which included statements of opposition from many members of Congress – supported Senator Garn's view that Walmart's application went far beyond the intended scope of the exemption he sponsored in 1987.[68]

Senator Garn's exemption was included in the Competitive Equality Banking Act of 1987 (CEBA). As discussed above in Part I(D)(1), CEBA reaffirmed and strengthened Congress's policy of separating banking and commerce by closing the nonbank bank loophole. During the floor debates on CEBA, members of Congress argued that the nonbank bank loophole should be

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[66] *Id.* at 2-3 (quoting Sen. Garn's statement on April 10, 2006, during one of the FDIC's three public hearings on Walmart's application).
[67] *Id.* at 3 (quoting FDIC rulemaking notices issued in Aug. 2006 and Feb. 2007).
[68] *Id.*

closed to preserve the separation of banking and commerce and ensure parity of regulatory treatment for all companies that control FDIC-insured banks.[69]

It is highly unlikely that Congress passed CEBA to *reaffirm and strengthen* the policy of separating banking and commerce by closing the nonbank bank loophole and, at the same time, intended to *undermine and weaken the same policy* by adopting Senator Garn's exemption for ILCs. The improbability of such a self-contradicting purpose is heightened by the absence of any evidence indicating a congressional belief that Senator Garn's exemption could be used to break down the barrier between banking and commerce. In 1999 – twelve years after CEBA – Congress again reinforced the policy of separating banking and commerce by passing a statute that prohibited further acquisitions of FDIC-insured savings associations by commercial firms. In view of Congress's powerful expressions of support for the policy of separating banking and commerce in 1987 and 1999, the unexplained text of Senator Garn's exemption should *not* be applied in a way that undermines that policy.[70]

Consequently, the FDIC's policy toward ILCs should adhere to Congress's strongly articulated purpose of separating banking and commerce. The appropriate policy would be for the FDIC to allow acquisitions of ILCs by companies engaged in financial activities but *not* by firms engaged in commercial activities. The FDIC followed that policy when (1) it did not approve Walmart's application, (2) it imposed a moratorium on acquisitions of ILCs by commercial firms between June 2006 and January 2008, and (3) it did not approve any

[69] *Id.* (summarizing floor statements by 11 Senators and House members).
[70] *Id.*; *see also* Wilmarth, "Wal-Mart," *supra* note 55, at 1569-73, 1584-86 (discussing Congress's passage of CEBA and the 1999 law that prohibited further acquisitions of thrifts by commercial firms); *Kanikal v. Attorney General*, 776 F.3d 146 (3d Cir. 2015) (refusing to interpret the literal text of one federal statute to override the clearly intended purpose of another federal law because the second law's legislative history confirmed Congress's strong intent that the second law's policy should be given priority). In the course of its opinion in *Kanikal*, the Third Circuit stated, "In resolving ambiguity, we must allow ourselves some recognition of the existence of sheer inadvertence in the legislative process." 776 F.3d at 152-53 & note 5 (quoting *Cass v. United States*, 417 U.S. 72, 83 (1974)).

acquisitions of ILCs by commercial firms between the expiration of its moratorium in 2008 and March 2020. Unfortunately, on March 18, 2020 – one day after the FDIC issued its proposed ILC rule – the FDIC approved deposit insurance applications for ILCs owned by Square and Nelnet. Square and Nelnet engage in a combination of financial and nonfinancial activities and would not qualify for status as bank holding companies under the BHC Act.[71]

The FDIC's issuance of the proposed ILC rule and its approvals of Square's and Nelnet's applications represent a fundamental and unwelcome change in the FDIC's policy toward ILCs. If adopted, the proposed ILC rule would encourage many other technology and commercial firms to acquire FDIC-insured ILCs.

For example, Rakuten recently renewed its application to acquire an FDIC-insured ILC in Utah. Rakuten is a large Japanese company involved in ecommerce, technology and other commercial activities. Rakuten's global website states that it conducts "over 70 businesses across e-commerce, digital content, communications and fintech," ranging from "new open platforms for e-commerce, to experiments with drones, chatbots, deep learning and AI." Rakuten's website also declares that "we challenge the status quo" and "embrace new and disruptive ideas."[72] If Rakuten acquires an FDIC-insured ILC, other Big Tech giants will almost certainly follow its example.

The FDIC should deny – or Congress should prevent – further acquisitions of ILCs by commercial firms. Further acquisitions would (i) severely undermine our longstanding policy of separating banking and commerce, (ii) create toxic conflicts of interest and pose serious threats

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[71] Wilmarth, "Industrial Banks," *supra* note 3, at 1, 3-4 (also noting that Congress imposed a three-year moratorium on acquisitions of ILCs between July 2010 and July 2013).

[72] *Id.* at 1-2 (quoting statements on Rakuten's global website under the headings "About Us" and "Leadership"), available at https://global.rakuten.com/corp/about/); Jon Prior, "Rakuten refiles with FDIC for ILC charter," *American Banker* (May 29, 2020).

to competition and consumer welfare, (iii) threaten to inflict large losses on the federal "safety net" for financial institutions during future systemic crises, and (iv) pose grave dangers to the stability of our financial system and the health of our general economy. Further acquisitions would contravene the public interest factors that the FDIC is required to consider under the FDI Act because those acquisitions would create (a) increased risks to the federal deposit insurance fund, (b) harmful impacts on communities and their residents, (c) adverse effects on competition, and (d) greater risks to the stability of the U.S. banking and financial systems.[73]

Commercial ownership of ILCs would pose serious threats to the stability of our financial system and our economy. The federal government bailed out several large corporate owners of ILCs during the financial crisis of 2007-09, including CIT Group, GE Capital, GMAC, Goldman Sachs, Merrill Lynch, and Morgan Stanley. Those bailouts illustrate the systemic dangers that are likely to arise when large nonbank corporations acquire ILCs and combine the operations of those ILCs with their other activities.[74]

Widespread ownership of ILCs by commercial firms would greatly increase the likelihood of contagious spillovers of risks and losses between the financial system and the general economy. During future financial crises and economic downturns, federal agencies would face intense pressures to rescue large commercial owners of ILCs to ensure the stability of our financial system and the health of our economy. For example, the German technology firm Wirecard was planning to pursue an acquisition of Deutsche Bank shortly before the revelation

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[73] *See* Wilmarth, "Industrial Banks," *supra* note 3, at 2-13; *see also infra* note 79 and accompanying text (discussing the public interest factors that the FDIC must consider under the FDI Act). The FDIC's issuance of its proposed ILC rule also violated the Administrative Procedure Act because the FDIC did not provide the public with adequate notice of – and an opportunity to comment on – the agency's change in policy toward acquisitions of ILCs by commercial firms and its factual, legal, and policy reasons for making that change. *Id.* at 2, 13-14.
[74] *Id.* at 6-8.

of Wirecard's massive accounting fraud led to the firm's collapse in June 2020.[75] Imagine the systemic crisis that could have occurred if Wirecard had acquired Deutsche Bank before its accounting fraud became known to regulators and the public.

FDIC-insured ILCs have full access to the federal "safety net," including deposit insurance, Fed discount window loans, and the Fed's payment and settlement services. That access would give significant competitive advantages to commercial firms that acquire ILCs. In addition to the low-cost funding provided by ILC deposits and discount window loans, commercial owners would receive implicit "catastrophe insurance" in the form of expected federal support during future systemic crises. Allowing commercial firms to own ILCs would create a highly skewed playing field favoring big enterprises that could afford to acquire ILCs and handicapping smaller firms that could not.[76]

The financial industry and many commercial sectors of our economy (including the information technology industry) already display very high levels of concentration and are dominated by a small number of giant firms. That domination enable big incumbent firms to capture unjustified super-profits by using their market power to impose unfair prices on customers and suppliers, by acquiring or crowding out smaller firms, and by deterring entry by new firms.[77] Allow Big Tech giants and other large commercial firms to acquire ILCs would give them an additional competitive edge, thereby further impairing competition and harming customers and suppliers in many lines of commerce.

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[75] *See* Olaf Storbeck, "Wirecard: the frantic final months of a fraudulent operation," *Financial Times* (Aug. 25, 2020), available at https://www.ft.com/content/6a660a5f-4e8c-41d5-b129-ad5bf9782256; Olaf Storbeck & Dan McCrum, "Wirecard's deceit went beyond its fraudulent Asian operations," *Financial Times* (Sept. 22, 2020), available at https://www.ft.com/content/04c77d71-c2ff-4340-8cf9-ee9c55b800e0; *see also* Todd H. Baker, "The Fall of Wirecard," *CLS Blue Sky Blog* (July 8, 2020), available at https://clsbluesky.law.columbia.edu/2020/07/08/the-fall-of-wirecard/.

[76] Wilmarth, "Industrial Banks," *supra* note 3, at 8-9; Wilmarth, "Wal-Mart," *supra* note 55, at 1588-93, 1621.

[77] *See* Thomas Philippon, *The Great Reversal: How America Gave Up on Free Markets* (2019); Timothy Wu, *The Curse of Bigness: Antitrust in the New Gilded Age* (2018).

4. Acquisitions of ILCs and Fintech "Banks" by Commercial Firms Would Inflict Serious Harm on Our Economy and Society

Acquisitions of ILCs and nondepository fintech national banks by Big Tech giants and other commercial firms would transform our financial system and economy in ways that are likely to impose significant harm on taxpayers, consumers, and communities. Big Tech firms already enjoy technological superiority over banks in the fields of automation, artificial intelligence, data management, and mobile payments. The rapid growth of Alibaba, Ant Financial, and Tencent in China's financial system indicate that Big Tech firms could potentially dominate major segments of our financial industry if those firms are allowed to establish "in-house banks" and exploit their technological advantages. Financial regulators around the world are just beginning to grapple with a wide array of public policy issues raised by the potential entry of Big Tech firms into the banking industry. Those issues include concerns about unfair competition, limits on sharing of customer data, protection of privacy rights in customer financial and health information, as well as operational and systemic risks created by ownership of banks by large technology firms.[78]

The FDIC and OCC should not be allowed to preempt the ongoing consideration of these vitally important issues by allowing Big Tech giants to acquire ILCs and nondepository fintech "banks." Those acquisitions would create intense pressure on Congress to remove all of the BHC Act's restrictions on joint ownership of banks and commercial firms. Big Tech giants would not be satisfied with making "toehold" acquisitions of ILCs or fintech "banks." They would want to establish a stronger competitive presence in the financial industry by acquiring large full-service banks. Conversely, big banks would push Congress to create a "level playing

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[78] *See* Kathryn Petralia, Thomas Philippon, Tara Rice & Nicholas Véron, *Banking Disrupted? Financial Intermediation in an Era of Transformational Technology* 25-38, 44-82 (Geneva Reports on the World Economy 22, 2019), available at https://www.cimb.ch/uploads/1/1/5/4/115414161/banking_disrupted_geneva22-1.pdf.

field" by allowing banks to acquire technology firms. Allowing Big Tech firms to acquire ILCs and fintech national "banks" would almost certainly lead to large-scale combinations between giant technology firms and megabanks. Those combinations would magnify the excessive levels of concentration, the lack of effective competition, the "too big to fail" status, and the unhealthy political influence that our technology giants and megabanks already possess and exploit. Those outcomes would violate the public interest factors that the FDIC and other bank regulators must consider under the FDI Act.[79]

As shown above, Big Tech giants and other commercial firms that acquire ILCs or fintech "banks" would not be regulated by the Fed under the BHC Act. The FDIC and the OCC could not exercise the type of consolidated, comprehensive supervision over commercial owners of ILCs and fintech "banks" that the Fed currently exercises over bank holding companies under the BHC Act. For example, the FDIC and OCC could not conduct unlimited, full-scope examinations of commercial parent companies and their nonbank subsidiaries. In addition, the FDIC and OCC could not impose consolidated capital requirements and liquidity requirements on commercial parent companies, nor could they require those companies to undergo stress tests and resolution planning exercises that large bank holding companies must complete.[80]

The Wirecard debacle illustrates the great danger of allowing the FDIC and OCC to regulate ILCs or fintech "banks" without possessing comprehensive, consolidated supervisory authority over those institutions' parent companies and other nonbank affiliates. Felix Hufeld, president of BaFin (Germany's financial regulatory agency) told the Bundestag (Germany's

[79] Wilmarth, "Industrial Banks," *supra* note 3, at 9-13. The public interest factors that regulators must consider under the FDI Act include (a) risks to the federal deposit insurance fund, (b) the "convenience and needs" of communities and their residents, (c) adverse effects on competition, and (d) risks to the stability of the U.S. banking and financial systems. *See id.* at 12-13 (discussing 12 U.S.C. §§ 1815, 1816, 1817(j)(7), and 1828(c)(5)).
[80] *See id.* at 10-11; *see also* 12 U.S.C. §§ 5365, 5371.

federal legislature) that BaFin failed to uncover Wirecard's massive accounting fraud because BaFin lacked authority to supervise Wirecard and its complex international network of nonbank subsidiaries. Hufeld said that BaFin's "ability to act was limited because Wirecard was classified as a technology company rather than a financial services provider, and so was not fully under BaFin's purview. The agency only oversaw Wirecard Bank," a deposit-taking bank that Wirecard owned.[81]

Even if Congress decided to give the FDIC and OCC consolidated supervisory authority over commercial owners of ILCs and fintech "banks," that authority would *not* remove the grave threats posed by the resulting commercial-financial conglomerates. Any federal banking agency would face enormous logistical challenges in attempting to oversee complex and highly diversified commercial-financial conglomerates, including the need to hire personnel with expertise in many different commercial sectors of the U.S. economy. The catastrophic failures of federal financial agencies to regulate large bank holding companies as well as "shadow bank" financial conglomerates prior to the financial crisis of 2007-09 should persuade us that federal regulators would have an even *lower* probability of success in regulating highly diversified commercial-financial conglomerates.[82]

Big Tech giants and other large commercial owners of ILCs and fintech "banks" would inevitably be considered "too big to fail" by both regulators and market participants. Their "too big to fail" status, their extensive lobbying resources, and their political influence would also make them "too big to discipline adequately." Thus, any attempt to establish an effective system

[81] Guy Chazan & Olaf Storbeck, "Head of German financial watchdog defends agency's Wirecard role," *Financial Times* (July 1, 2020) (summarizing Hufeld's statement), available at https://www.ft.com/content/fd2e1442-d35c-412e-a7a5-aa4d5b52e629; *see also* Baker, *supra* note 75; Matthew Vincent, Jim Brunsden & Olaf Storbeck, "EU watchdog to probe German regulators after Wirecard collapse," *Financial Times* (July 15, 2020), available at https://www.ft.com/content/7b711f0e-0e2d-4639-94db-0c26b4073e78.
[82] Wilmarth, "Industrial Banks," *supra* note 3, at 4-7, 11-12; *see also supra* note 29, *infra* note 134 and accompanying text (discussing regulatory failures that contributed to the financial crisis of 2007-09).

of consolidated supervision for commercial-financial conglomerates would almost certainly fail. The unfeasibility of consolidated supervision for large commercial-financial conglomerates provides a further compelling reason for prohibiting their existence.[83]

II. The OCC's and FDIC's Usury Preemption Transfer and "True Lender" Rules Violate Federal Laws and Threaten to Impose Severe Injuries on Consumers and Small Businesses

A. Federal Laws Prohibit the OCC and FDIC from Extending the Scope of Federal Preemption to Benefit Nonbanks

1. The OCC's and FDIC's Usury Preemption Transfer Rules Are Unlawful

Since 1864, Section 85 of the NBA has specified the "interest" that a national bank may "take, receive, reserve, and charge" on its loans. The "interest" allowed to a national bank under Section 85 is governed by the usury laws of the state in which the bank is "located." Section 85 confers on each national bank a preemptive immunity from state usury laws except for the usury laws of the state in which that bank is "located."[84]

The OCC lacked authority to issue its usury preemption transfer rule, which purports to extend the preemption provided to national banks under Section 85 to reach third-party purchasers, assignees, and transferees of loans made by national banks.[85] Section 85's explicit terms make clear that the power to charge "interest" thereunder is granted *only* to national banks and does *not* extend to purchasers, assignees, or transferees of loans made by national banks. Less than a decade after Congress enacted the NBA, the Supreme Court held that Section 85 was intended "to allow *to National associations* the rate allowed by the State to natural persons

[83] Wilmarth, "Industrial Banks," *supra* note 3, at 11-12; Wilmarth, "Wal-Mart," *supra* note 55, at 1617-21.
[84] Act of June 3, 1864, § 30, 13 Stat. 108 (codified as amended at 12 U.S.C. § 85); *see also Marquette National Bank v. First of Omaha Serv. Corp.*, 439 U.S. 299 (1978).
[85] OCC Usury Preemption Transfer Rule, *supra* note 4.

generally, and a higher rate, if State banks of issue were authorized to charge a higher rate."[86] A century later, the Supreme Court's *Marquette* decision stated that Section 85 provides the terms on which "a *national bank* may charge interest."[87] The Court explained that its *Marquette* decision – which allowed a national bank to "export" to borrowers in other states the interest rate allowed by the state in which the bank was "located" – did *not* apply to the bank's nondepository subsidiary or to other parties with which the bank had contractual relationships.[88]

In 1980, Congress enacted two statutes, 12 U.S.C. §§ 1463(g)(1) and 1831d, which were designed to give federal savings associations and FDIC-insured, state-chartered depository institutions "parity, or competitive equality" with national banks in terms of the "interest" they can charge on their loans.[89] Congress also intended that Sections 1463(g) and 1831d would "provide federally-insured credit institutions with the same 'most-favored-lender' status enjoyed by national banks."[90] The preemptive immunity granted by Sections 1463(g) and 1831d applies *only* to "interest" lawfully charged by federal savings associations and FDIC-insured, state-chartered depository institutions. The preemptive scope of those statutes is the same as Section 85, which applies *only* to "interest" lawfully charged by national banks.[91]

Sections 1463(g) and 1831d were enacted as part of Section 521 of the Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDMCA).[92] Like Section 85,

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[86] *Tiffany v. National Bank of Missouri*, 85 U.S. (18 Wall.) 409, 413 (1873) (emphasis added).
[87] *Marquette National Bank*, 439 U.S. at 308 (emphasis added).
[88] See *Marquette*, 439 U.S. at 307-08 ("There is no allegation in petitioners' complaints that either Omaha Service Corp. or the Minnesota merchants and banks participating in the BankAmericard program are themselves extending credit in violation of Minn. Stat. § 48.185 (1978), and we therefore have no occasion to determine the application of the National Bank Act in such a case.").
[89] *Greenwood Trust Co. v. Massachusetts*, 971 F.2d 818, 827 (1st Cir. 1992) (quoting 126 Cong. Rec. 6900 (1980) (remarks of Sen. Proxmire)), *cert. denied*, 506 U.S. 1052 (1993); *accord, Garvey Properties/762 v. First Financial Savings & Loan Ass'n*, 845 F.2d 519, 520-22 (5th Cir. 1988).
[90] *Garvey Properties*, 845 F.2d at 521.
[91] See *In re Community Bank of N. Va.*, 418 F.3d 277, 296 (3d Cir. 2005) (Sections 85 and 1831d "apply only to national banks and state chartered banks, not to non-bank purchasers of second mortgage loans").
[92] Pub. L. No. 96-221, § 521, 94 Stat. 132, 164.

Sections 1463(g) and 1831d do *not* include any reference to the right of a federally-chartered or federally-insured depository institution to transfer its preemptive immunity from state usury laws to purchasers, assignees, and other transferees of its loans.

In contrast, 12 U.S.C. § 1735f-7a – enacted as part of Section 501 of DIDMCA – preempts state usury laws from applying to originations and "credit sales" of first-lien residential mortgages that qualify as "federally related mortgage loans" under 12 U.S.C. § 1735f-5(b). Congress intended that the preemption provided by Section 501 would apply to *both* originations *and* sales of qualifying first-lien residential mortgages. Congress wanted to "facilitate a national housing policy and the functioning of a national secondary market in mortgage lending."[93] Congress therefore made clear that qualifying first-lien residential mortgages made by "eligible lenders" would continue to receive the benefit of Section 501's preemption of state usury laws if those mortgages were subsequently sold to investors who were not "eligible lenders."[94]

Thus, the preemption authorized by Section 501 of DIMCA applies to sales of qualifying first-lien residential mortgages and covers purchasers of those mortgages. In contrast, the preemption authorized by Section 521 of DIDMCA, which enacted Sections 1463(g) and 1831d, does *not* refer to "sales" of loans or to purchasers of loans. The Supreme Court has repeatedly held that Congress is presumed to act "intentionally and purposely" when "it includes particular language in one section of a statute but omits it in another section of the same Act."[95] That presumption is especially strong when the two statues were enacted "simultaneously" by the

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[93] *Smith v. Fidelity Consumer Discount Co.*, 898 F.2d 907, 911 (3d Cir. 1990) (quoting S. Rep. No. 96-368, at 19 (1979)).
[94] ***See*** S. Rep. No. 96-368, at 19 (1979) ("[I]t is the committee's intent that loans originated under this usury exemption will not be subject to claims of usury even if they are later sold to an investor who is not exempt under this section.").
[95] *Barnon v. Sigmon Coal Co.*., 534 U.S. 438, 452 (2002) (quoting *Russelo v. United States*, 464 U.S. 16, 23 (1983)); *accord*, *INS v. Cardoza-Fonseca*, 480 U.S. 421, 432 (1987).

"same Congress," as Sections 501 and 521 of DIDMCA were in 1980.[96] It must therefore be presumed that Congress acted "intentionally and purposefully" when it did *not* make any reference to "sales" of loans or purchasers of loans in Section 521 of DIDMCA.

The absence of any reference to "sales" of loans in Section 521 of DIDMCA supports the conclusion that the preemption provided to national banks by 12 U.S.C. 85 – the historical model for Section 521 – also does *not* extend to purchasers of loans.[97] That conclusion is further bolstered by the Alternative Mortgage Transactions Parity Act, 12 U.S.C. §§ 3801-06 (AMTPA), which was enacted only two years after DIDMCA. Under 12 U.S.C. § 3803, "housing creditors" (including state-chartered, non-depository lenders) can "make, purchase, and enforce alternative mortgage transactions" in accordance with AMTPA, regardless of contrary state laws. Thus, the scope of AMTPA's preemption expressly extends to purchasers of qualifying alternative mortgages, in the same way that the preemptive scope of Section 501 of DIDMCA includes purchasers of qualifying first-lien residential mortgages. Section 501 of DIDMCA and AMTPA show that Congress knew how to make its intention clear when it wanted to extend preemptive immunity to purchasers of loans.

The preemption standards for national banks under 12 U.S.C.§ 25b – which Congress adopted in 2010 – reinforce the conclusion that Sections 85 does *not* provide preemptive immunity for purchasers, assignees, and other transferees of loans made by national banks. Sections 25b(b)(2), (e), and (h)(2) provide that state laws apply to subsidiaries, affiliates, and agents of national banks to the same extent as they apply to any other person subject to those

[96] *Cardoza-Fonseca*, 480 U.S. at 432.
[97] See *Greenwood Trust*, 971 F.2d at 827 ("The historical record clearly requires a court to read the parallel provisions of [DIDMCA] and the [National] Bank Act *in pari materia*."); *accord*, *In re Community Bank of N. Va.*, 418 F.3d at 295-96 ("[T]he language of the two statutes [– Sections 1831d and 85 –] should ordinarily be interpreted in the same way.").

state laws – *unless* the subsidiary, affiliate, or agent is itself chartered as a national bank.[98] Similarly, state laws apply to subsidiaries, affiliates, and agents of federal savings associations pursuant to 12 U.S.C. § 1465(a), which establishes equivalent preemption standards for federal thrifts.

The foregoing provisions of Section 25b overruled several court decisions prior to 2010 that extended the NBA's preemptive scope to cover nonbank subsidiaries and agents of national banks.[99] In light of Section 25b's express *denial* of NBA preemption to nonbank subsidiaries, affiliates, and agents of national banks, the OCC's usury preemption transfer rule violated congressional intent by purporting to extend the preemptive scope of Sections 85 and 1463(g) to reach purchasers and assignees of loans. Purchasers and assignees of loans are counterparties to contracts with national banks and federal thrifts, just as agents are and most subsidiaries and affiliates are. Purchasers and assignees of loans cannot claim any entitlement to a preemptive immunity that Congress has expressly *denied* to other types of contract counterparties that have *closer* relationships with national banks and federal thrifts.

Section 25b(f) provides additional evidence of Congress's intent *not* to extend preemption of state usury laws beyond national banks. Section 25b(f) preserves only "the authority conferred by section 85 . . . for the charging of interest *by a national bank*" from the limitations on preemption established by Section 25b (emphasis added). Federal savings associations are subject to the same limited scope of preemption under 12 U.S.C. § 1465(a).

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[98] *See* S. Rep. No. 111-176, at 176 (2010) (Under Dodd-Frank, "State law applies to State-chartered nondepository institution subsidiaries, affiliates, and agents of national banks, other than entities that are themselves chartered as national banks."); Wilmarth, "Dodd-Frank," *supra* note 29, at 934-35.

[99] See *Mississippi Dept. of Finance v. Pikco Finance, Inc.*, 97 So.3d 1203, 1209 n.7 (Miss. 2012) (recognizing that Dodd-Frank overruled the preemptive ruling of *Watters v. Wachovia Bank, N.A.*, 550 U.S. 1 (2007), with respect to operating subsidiaries of national banks); *Phillips v. Bank of America, N.A.*, 186 Cal.Rptr.3d 434, 444 (Cal. App. 2015) (same); Wilmarth, *supra* note 29, at 934-35 (discussing *Watters* and other decisions whose preemptive rulings concerning subsidiaries and agents of national banks were overruled by Dodd-Frank).

Like Sections 85, 1463(g), and 1831d, Section 25b(f) does *not* refer to purchasers, assignees, or other transferees of loans made by national banks.

When the OCC proposed its usury preemption transfer rule, the OCC acknowledged that its assertion of preemptive immunity for purchasers, assignees, and other transferees of loans made by national banks and federal thrifts was *not* based on any language "expressly stated" in Sections 85 and 1463(g).[100] The OCC also recognized that its rule was contrary to the decision of the Second Circuit Court of Appeals in *Madden v. Midland Funding*. The Second Circuit held in *Madden* that any extension of Section 85's preemption to cover debt collectors who purchased loans from national banks would be an "overly broad application" of the NBA. The Second Circuit concluded that such an outcome "would create an end-run around usury laws for non-national bank entities that are not acting on behalf of a national bank."[101]

The OCC argues that its usury preemption transfer rule is supported by the "common-law [principles of] valid-when-made and the assignability of contracts," which it derives from court decisions dating back to the 19th century. According to the OCC, it is "not citing these tenets as independent authority for this rulemaking but rather as tenets of common law that inform its reasonable interpretation of section 85."[102]

The OCC cannot rely on common-law principles from federal court decisions to expand the preemptive scope of federal statutes. The Supreme Court has made clear since 1938 that "[t]here is no federal general common law."[103] The Supreme Court has repeatedly held that "cases in which judicial creation of a special federal [common law] rule would be justified . . .

[100] OCC, Notice of proposed rulemaking, "Permissible Interest on Loans That Are Sold, Assigned, or Otherwise Transferred," 84 Fed. Reg. 64229, 64230 (Nov. 21, 2019).
[101] *Madden v. Midland Funding, LLC*, 786 F.3d 246, 251-52 (2d Cir. 2015), *cert. denied*, 136 S. Ct. 2505 (2016). The OCC's usury preemption transfer rule is designed to overrule *Madden*. *See* 85 Fed. Reg. at 33531-33.
[102] OCC Usury Preemption Transfer Rule, *supra* note 4, at 33532 (citing, inter alia, *Nichols v. Fearson*, 32 U.S. (7 Pet.) 103 (1833), and *Gaither v. Farmers & Mechanics Bank of Georgetown*, 26 U.S. (1 Pet.) 37 (1828)).
[103] *O'Melveny & Myers v. FDIC*, 512 U.S. 79, 83 (1994) (quoting *Erie R. Co. v. Tompkins*, 304 U.S. 64, 78 (1938)).

are . . . 'few and restricted.'"[104] The Supreme Court has twice struck down attempts by the FDIC to expand the scope of preemption under the FDI Act by invoking federal common-law rules.

In its 1997 *Atherton* decision, the Supreme Court held that a "federal common law" duty of ordinary care for bank directors and officers did not expand the preemptive scope of 12 U.S.C. § 1821(k). Section 1821(k) imposes liability on directors and officers of FDIC-insured banks for gross negligence. However, the statute is silent on the question of whether the FDIC can hold bank directors and officers liable for simple negligence in cases where applicable state laws do not impose a duty of ordinary care. The FDIC claimed that it could impose liability for simple negligence based on a "federal common law" rule dating from the 19th century, even if applicable state laws denied liability for simple negligence. The Supreme Court rejected the FDIC's claim and held that "state law, not federal common law, provides the applicable rules for decision," except where Section 1821(k) preempted state law by stipulating a gross negligence standard. The Court pointed out that "federally chartered banks are subject to state law," and "a federal charter by itself shows no conflict, threat, or need for 'federal common law.'"[105]

In its 1993 *O'Melveny & Myers* decision, the Court rejected a similar preemption claim by the FDIC. The FDIC asserted that a law firm should be held liable for negligence and breach of fiduciary duty based on its alleged malpractice in representing a failed thrift institution. The FDIC argued, based on a "federal common-law rule," that the law firm could not defend itself by imputing the knowledge of corporate officers to the thrift or to the FDIC as the thrift's receiver. Again, Section 1821 was silent about any imputation of knowledge from corporate officers to their institution and the FDIC. However, applicable state laws did impute the knowledge of

[104] *Atherton v. FDIC*, 519 U.S. 213, 218 (1997) (quoting *O'Melveny & Myers*, 512 U.S. at 87) (quoting *Wheeldin v. Wheeler*, 373 U.S. 647, 651 (1963)).
[105] *Atherton*, 519 U.S. at 218-26.

those officers to both the thrift and the FDIC. After reviewing the "comprehensive and detailed" provisions of Section 1821, the Supreme Court determined that "matters left unaddressed in such a scheme are presumably left to the disposition provided by state law." The Court held that Section 1821 "places the FDIC in the shoes of the insolvent S&L, to work out its claims under state law, except where some provision in the extensive framework of [Section 1821] provides otherwise. *To create additional 'federal common-law' exceptions is not to 'supplement' this scheme, but to alter it.*"[106]

The OCC's reliance on common-law "tenets" to expand the preemptive scope of 12 U.S.C. §§ 85 and 1463(g) is invalid for the same reasons that the Supreme Court rejected the FDIC's reliance on "federal common law rules" in *Atherton* and *O'Melveny & Myers*. The OCC's usury preemption transfer rule applies to transactions between private parties (national banks and purchasers, assignees, and transferees of their loans). The OCC's rule does not implicate the rights, liabilities, or duties of the United States or its agencies, officials, or contractors, and it also does not involve U.S. foreign relations or admiralty matters. The Supreme Court has held that application of a federal common-law rule is *not* justified when "private parties," including national banks, are involved in a dispute relating to a "private transaction" that "does not touch the rights and duties of the United States."[107]

Consequently, the OCC cannot rely on common-law "tenets" to expand the preemptive scope of 12 U.S.C. 85 and 1463(g). In determining whether federal statutes preempt state authority in a traditional field of state regulation, such as consumer protection, federal courts "start with the assumption that the historic police powers of the States were not to be superseded

[106] *O'Melveny & Myers*, 512 U.S. at 85-88 (emphasis added).
[107] *Bank of America National Trust & Savings Ass'n v. Parnell*, 352 U.S. 29, 33-34 (1956); *see also Atherton*, 519 U.S. at 226.

by the Federal Act unless that was the clear and manifest purpose of Congress."[108] Courts have held that "compelling evidence of [Congress's] intention to preempt" is required" before they will conclude that a federal statute preempts state consumer protection laws.[109]

There is no "compelling evidence" of any "clear and manifest purpose of Congress" to extend the scope of usury preemption under Sections 85 and 1463(g) to reach purchasers, assignees, and other transferees of loans made by national banks and federal thrifts. On the contrary, as shown above, the express terms of Sections 85 and 1463(g) apply only to "interest" that is lawfully "charge[d]" by national banks and federal thrifts. When Congress wanted to extend usury preemption to reach purchasers of mortgage loans under DIDMCA and AMTPA, Congress made its intention crystal clear.

When the FDIC proposed its own usury preemption transfer rule, it acknowledged that 12 U.S.C. § 1831d "is patterned after section 85 and receives the same interpretation as section 85."[110] Accordingly, the FDIC's authority to preempt state usury laws under Section 1831d is no broader than the OCC's authority under Section 85 and does *not* extend to third parties that acquire bank loans. The OCC's and FDIC's usury preemption transfer rules plainly exceed their statutory authority, and both rules are invalid.[111]

2. The OCC's Proposed "True Lender" Rule Is Unlawful and Would Enable National Banks to Form "Rent-a-Charter" Schemes with Predatory Nonbank Lenders

Under the OCC's proposed "true lender" rule, a national bank or thrift would be deemed to "make" a loan if the institution, "as of the date of origination," is either "named as the lender

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[108] *Wyeth v. Levine*, 555 U.S. 555, 565 (2009) (quoting *Medtronic v. Lohr*, 518 U.S. 470, 485 (1996)).
[109] *Lusnak v. Bank of America, N.A.*, 883 F.3d 1185, 1188, 1191-94 (9th Cir.), *cert. denied*, 139 S. Ct. 567 (2018) (quoting *Aguayo v. U.S. Bank*, 653 F.3d 912, 917 (9th Cir. 2011) (quoting *General Motors Corp. v. Abrams*, 897 F.2d 34, 41-42 (2d Cir. 1990)).
[110] FDIC, Notice of proposed rulemaking, "Federal Interest Rate Authority," 84 Fed. Reg. 66845, 66849 (Dec. 6, 2019).
[111] *See* Wilmarth Usury Preemption Transfer Comment Letter, *supra* note 4, at 7-13.

in the loan agreement" or "[f]unds the loan."[112] The proposed rule is designed to "operate together" with the OCC's usury preemption transfer rule.[113] Working in tandem, the rules would permit national banks or federal thrifts to form "partnerships" with nonbank lenders. A nonbank lender that generates loans through such a "partnership" could claim preemptive immunity from state usury laws under 12 U.S.C. 85 or 1463(g), even if its bank "partner" does not retain any meaningful credit risk or other economic risk related to those loans. The bank "partner" could act as a mere conduit by quickly transferring loans to the nonbank lender, and the nonbank lender could assume all of the economic risks, dictate the terms, and control the enforcement of those loans. Such "partnerships" would represent "rent-a-charter" schemes, which the OCC barred national banks from establishing during the early 2000s.[114]

The OCC's proposed "true lender" rule evidently seeks to preempt not only state usury laws but also a wide range of other state laws – including state licensing, examination, and consumer protection laws – that would otherwise apply to nonbank lenders that establish "partnerships" with national banks. For example, a loan that is deemed to be "made" by a national bank under either of the proposed rule's two tests would apparently be covered by the OCC's sweeping claims of preemption of state law under 12 C.F.R. § 7.4008 (for loans "made" by national banks that are not secured by real estate) or 12 C.F.R. § 34.4 (for real estate loans "made" by national banks) – even if the bank subsequently transfers the loan to a nonbank "partner." The proposed rule's potential scope of preemption therefore embraces a very broad array of state laws.[115]

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[112] OCC Proposed "True Lender" Rule, *supra* note 5, at 44228.
[113] *Id.* at 44227.
[114] *See* Wilmarth "True Lender" Comment Letter, *supra* note 5, at 1-2.
[115] *See id.* at 2 (citing 85 Fed. Reg. at 44225).

In its notice of proposed rulemaking, the OCC acknowledged that federal statutes – including 12 U.S.C. §§ 85 and 1463(g) – "do not specifically address which entity makes a loan (or, in the vernacular commonly used in case law, which entity is the 'true lender')" and therefore do not identify "what legal framework applies, when the loan is originated as part of a lending relationship between a bank and a third party." In addition, the OCC admitted that *none* of the federal statutes authorizing national banks and federal savings associations to make contracts and loans "describes how to determine when a bank has, in fact, exercised this authority, and when, by contrast, the bank's relationship partner has made the loan."[116] Thus, the OCC conceded that its proposed "true lender" tests are *not* supported by any explicit statutory authority.

The proposed rule also ignores the fact that contracts made by national banks are governed by applicable state laws *unless* a particular state law creates an irreconcilable conflict with a federal statute. The Supreme Court has repeatedly held that national 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. *All their contracts are governed and construed by State laws.* Their acquisition and transfer of property, their right to collect their debts, and their liability to be sued for debts, are all based on State law."[117]

Similarly, the Supreme Court affirmed in 2009 that "States . . . have always enforced their general laws against national banks – and have enforced their banking-related laws against national banks for at least 85 years."[118]

[116] OCC Proposed "True Lender" Rule, *supra* note 5, at 44224, 44225.
[117] *Atherton v. FDIC*, 519 U.S. 213, 222-23 (1997) (emphasis added) (quoting *National Bank v. Commonwealth*, 76 U.S. (9 Wall.) 353, 362 (1870)).
[118] *Cuomo v. Clearing House Ass'n*, 557 U.S. 519, 534 (2009); *see also* Wilmarth, "Dodd-Frank," *supra* note 29, at 944-48 (discussing additional Supreme Court decisions upholding the application of state laws to contracts and other transactions made by national banks).

Contracts for loans are subject to state usury laws as well as general state contract laws. State usury laws are valid exercises of the states' historic police power to protect their residents from abusive and exploitative lending practices.[119] Because usury is a traditional field of state regulation, federal courts have declined to infer from statutory silence that Congress intended to preempt state usury laws.[120] As indicated above, Congress has *not* expressed any intention to preempt "true lender" doctrines that are a key element of many state usury laws.[121]

Federal courts have repeatedly held that Section 85 incorporates the entire usury jurisprudence of the relevant state, including that state's usury statutes and interpretations of those statutes by the state's courts.[122] Federal and state courts have also held that usury claims should be determined based on the "substance" of the relevant transactions and not their legal

[119] *See Griffith v. Connecticut*, 218 U.S. 563, 569 (1910) (It is "elementary" that usury laws fall "within the police power" of the states.); *Goleta National Bank v. Lingerfelt*, 211 F.Supp.2d 711, 716 (E.D.N.C. 2002) ("[T]he State does have a vital interest in protecting its citizens from predatory lending, usury, and other forms of deceptive trade practices."); *Pa. Dept. of Banking v. NCAS of Delaware, LLC*, 948 A.2d 752, 759 (Pa. 2008) ("[R]egulation of the rate of interest is a subject within the police power of the State, and this is especially true in the case of loans of comparatively small amounts, since the business of making such loans profoundly affects the social life of the community.") (quoting *Equitable Credit & Discount Co. v. Geier*, 21 A.2d 53, 58 (Pa. 1941)); James M. Ackerman, "Interest Rates and the Law: A History of Usury," 1981 *Arizona State Law Journal* 61, 85-110 (explaining that state usury laws "are viewed as a protective measure imposed to safeguard consumers from abuse and exploitation by sellers of credit," *id.* at 110).

[120] *See Doyle v. Southern Guaranty Corp.*, 795 F.2d 907, 914 (11th Cir. 1986) (noting Congress's "traditional deference to the state's right to determine its usury statute"); *Goleta National Bank v. Lingerfelt*, 211 F. Supp. 2d at 716-18 (rejecting the assertion that the NBA completely preempted the application of state usury laws to a nonbank lender that made loans as an alleged partner of a national bank, because that preemption claim was "far from being facially conclusive or readily apparent"); *see also In re Seolas*, 140 B.R. 266, 272 (E.D. Cal. 1992) ("ERISA does not preempt generally applicable usury laws [in the] absence of any evidence that Congress intended preemption," because "usury laws are a traditional subject of state regulation.").

[121] *See* the third paragraph of this Part 2(b).

[122] *Union National Bank v. Louisville, N., A. & C. Ry. Co.*, 163 U.S. 325, 330-31 (1896) (holding that 12 U.S.C. § 85 incorporated the usury statutes of Illinois as interpreted by Illinois state courts); *accord, Citizens National Bank v. Donnell*, 195 U.S. 369, 374 (1904) ("[W]e follow the state court" in determining whether a national bank violated Missouri's usury laws); *Daggs v. Phoenix National Bank*, 177 U.S. 549, 555 (1900) ("The intention of the [NBA] is to adopt the state law, and permit to national banks what the state law allows to its citizens and to the banks organized by it."). *See also Bartholomew v. Northampton National Bank*, 584 F.2d 1288, 1295 (3d Cir. 1978) (The NBA "incorporates by reference the usury law of the state where the national bank is located."); *First National Bank of Mena v. Nowlin*, 509 F.2d 872, 876 (8th Cir. 1975) (Section 85 "adopts the entire case law of the state interpreting the state's limitations on usury; it does not merely incorporate the numerical rate adopted by the state."); *Roper v. Consurve, Inc.*, 777 F. Supp. 508, 513 (S.D. Miss. 1990) (Section 85 "adopts not only the numerical interest rates set by state statute, but also the entire case law of the state interpreting the state's limitations on usury."), *aff'd*, 932 F.2d 965 (5th Cir.) (table), *cert. denied*, 502 U.S. 861 (1991).

"form." In an 1835 decision, the Supreme Court declared (in an opinion by Chief Justice John Marshall) that an alleged violation of usury laws should be evaluated based on "*the substance of the transaction* and the true intent and meaning of the parties, for they alone are to govern, *and not the words used*."[123] Other courts have similarly evaluated usury claims against national banks by "look[ing] behind the form of a transaction to its substance" in accordance with state usury laws.[124]

Several courts have applied a substance-over-form analysis in determining whether nonbank lenders were actually the "true lenders" even though they claimed to be "partners" of banks." Those courts rejected claims by nonbank lenders for preemptive immunity under 12 U.S.C. § 85 or 12 U.S.C. § 1831d, based on their status as "partners" or "agents" of national banks or FDIC-insured state banks. The courts held that nonbank lenders should be treated as the "true lenders" if they held the "predominant economic interest" in the loans. In determining which party possessed the "predominant economic interest," the courts considered several factors, including which party bore the greatest amount of credit risk under the loans, which party dictated the terms and controlled the enforcement of the loans, and whether the nonbank lender agreed to indemnify its "partner" bank.[125]

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[123] *Scott v. Lloyd*, 34 U.S. 418, 453 (1835) (quoting Lord Mansfield; emphasis added); *see also id.* at 456 ("[T]he only question in all cases like the present, is, *what is the real substance of the transaction*, not what is the colour and form" (quoting Lord Mansfield; emphasis added).

[124] *Anderson v. Hershey*, 127 F.2d 884, 886 (6th Cir. 1942) (applying Kentucky law); *accord, First National Bank in Mena v. Nowlin,* 509 F.2d at 877 (applying Arkansas law); *Ubaldi v. SLM Corp.*, 852 F. Supp. 2d 1190, 1194-98 (N.D. Cal. 2012) (applying California law); *First National Bank v. Phares*, 174 P. 519, 521 (Okla. 1918) (applying Oklahoma law).

[125] *In re Community Bank of N. Va.*, 418 F.3d at 283-85, 294-97 (applying Pennsylvania law); *Ubaldi*, 852 F. Supp. 2d at 1194-1200 (applying California law); *Eul v. Transworld Systems*, 2017 WL 1178537 at *5 –*10 (N.D. Ill. Mar. 30, 2017) (applying Illinois law); *Goleta National Bank v. O'Donnell*, 239 F. Supp. 2d 745, 753-58 (S.D. Ohio 2002) (applying Ohio law); *Goleta National Bank v. Lingerfelt*, 211 F. Supp. 2d at 717-19 (applying North Carolina law); *CashCall, Inc. v. Morrissey*, 2014 WL 2404300, at *14 –*15 & n.19, *18 (W.Va. May 30, 2014) (applying West Virginia law); *see also CFPB v. CashCall, Inc.*, 2016 WL 4820635 at *5 (C.D. Cal. Aug. 31, 2016) (applying the laws of 16 states, and concluding that the court "should look to the substance, not the form, of the transaction to identify the true lender" in a joint venture between a nonbank lender and a "tribal lending entity," and determining that the nonbank lender was the "true lender").

The OCC's proposed rule disregards the foregoing court decisions and seeks to preempt state "true lender" laws. The proposed rule attempts to create a conclusive, inflexible, and formalistic standard for determining the "true lender" for loans produced by "partnerships" between national banks and nonbank lenders. The proposed rule would consider only two narrow factors – whether the national bank was named as the lender in the loan agreements or funded the loans *for at least one day*. The proposed rule would grant preemptive immunity to nonbank lenders from a wide range of state laws even if those lenders held the "predominant economic interest" in loans generated by "partnerships" with national banks.

The OCC's proposed rule would enable national banks and federal thrifts to form "rent-a-charter" schemes with nonbank lenders. "Rent-a-charter" schemes are designed to prevent states from enforcing their usury laws and other consumer protection laws against high-cost nonbank lenders, including payday lenders and auto title lenders. Those lenders impose very high interest charges on consumers and small businesses with annual percentage rates ("APRs") that often exceed 100%. Loans made by high-cost nonbank lenders produce staggering rates of delinquency and default among borrowers. For example, Elevate, a high-cost lender that is a "partner" of several banks, reported charge-off rates on its loans that exceeded 52% of its revenues in 2016 and 2017. Similarly, more than one-fifth of borrowers who enter into auto title loans eventually lose their cars through repossession. High-cost nonbank lenders usually focus their marketing efforts on vulnerable minority and lower-income households.[126]

[126] Testimony of Graciela Aponte-Diaz, Center for Responsible Lending, before the House Financial Services Committee (Feb. 5, 2020), at 3-8, available at https://financialservices.house.gov/uploadedfiles/graciela_testimony_crl_rent_a_bank_final_rev.pdf; Testimony of Lauren Saunders, National Consumer Law Center, before the House Financial Services Committee (Feb. 5, 2020), at 7-13, available at https://financialservices.house.gov/uploadedfiles/lauren_saunders_testimony_on_rent_a_bank_hearing_revised_2-5-20.pdf; *see also CashCall, Inc. v. Morrissey*, 2014 WL 2404300, at *1 –*8 (stating that more than two-thirds of West Virginia borrowers who received high-cost loans from CashCall defaulted on those loans, and describing the

In the early 2000s, the OCC recognized the dangers to consumers from payday loans that were marketed by "rent-a-charter" schemes between national banks and nonbank lenders.[127] The OCC took decisive action to shut down those schemes. The OCC issued enforcement orders that required four national banks (Eagle National Bank, First National Bank of Brookings, Goleta National Bank, and Peoples National Bank of Paris, Texas) to stop making payday loans and to terminate their "rent-a-charter" arrangements with nonbank lenders.

In January 2002, the OCC issued an enforcement order against Eagle National Bank after determining that Eagle's payday lending partnership with Dollar Financial Group "risked its financial viability" and violated "a multitude of standards of safe and sound banking, compliance requirements, and OCC guidance." The OCC stated that the Eagle's partnership with Dollar "demonstrates the dangers inherent in arrangements under which national banks rent out their charters to nonbank providers of financial services . . . . [Eagle] effectively collaborated in Dollar's scheme to evade state law requirements that would otherwise be applicable to it."[128]

In announcing a similar enforcement order against Peoples National Bank in January 2003, Comptroller of the Currency John D. Hawke, Jr. stated:

> We have been greatly concerned with arrangements in which national banks essentially rent out their charters to third parties who want to evade state and local consumer protection laws . . . . The preemption privileges of national banks derive from the Constitution and are not a commodity that can be transferred for a fee to nonbank lenders.[129]

predatory lending and abusive debt collection practices that CashCall perpetrated against those borrowers in violation of West Virginia laws).

[127] OCC Consent Order 2003-2, at 1-2 (Jan. 30, 2003) (Peoples National Bank), available at https://www.occ.gov/static/enforcement-actions/ea2003-2.pdf.

[128] OCC News Release 2002-1 (Jan. 3, 2002) (Eagle National Bank), available at https://www.occ.gov/news-issuances/news-releases/2002/nr-occ-2002-1.html.

[129] OCC News Release 2003-6 (Jan. 31, 2003) (Peoples National Bank), available at https://www.occ.gov/news-issuances/news-releases/2003/nr-occ-2003-6.html. *See also* OCC News Release 2003-3 (Jan. 31, 2003) (First National Bank of Brookings), available at https://www.occ.gov/news-issuances/news-releases/2003/nr-occ-2003-3.html; OCC Consent Order 2002-93 (Oct. 28, 2002) (Goleta National Bank), available at https://www.occ.gov/static/enforcement-actions/ea2002-93.pdf.

In a speech delivered in February 2002, Comptroller Hawke declared that "rent-a-charter" schemes posed serious threats to the "safety and soundness" of national banks and represented "an abuse of the national charter." He condemned such schemes as illegitimate because

> [t]he benefit that national banks enjoy by reason of this important constitutional doctrine [of preemption] cannot be treated as a piece of disposable property that a bank may rent out to a third party that is not a national bank. Preemption is not like excess space in a bank-owned office building. *It is an inalienable right of the bank itself.*[130]

Thus, the OCC established a strong policy in the early 2000s against allowing national banks to organize "rent-a-charter" schemes with nonbank payday lenders. As shown by the OCC's current website, that policy has remained in effect – at least formally – *until now*.[131] The OCC's enforcement orders from the early 2000s provide compelling evidence of the significant harms that the OCC would inflict on states, consumers, and small businesses if it adopts its proposed "true lender" rule and implements its usury preemption transfer rule. Those harms would include: undermining the states' longstanding authority to protect their residents from predatory nonbank lenders, threatening the financial and reputational soundness of national banks, encouraging reckless lending practices, and facilitating efforts by predatory nonbank lenders to exploit consumers and small businesses with exorbitant interest charges and fees, deceptive marketing practices, privacy violations, abusive debt collection practices, and other unconscionable conduct.[132]

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[130] Remarks by Comptroller of the Currency John D. Hawke, Jr. before the Women in Housing and Finance (Feb. 12, 2002), at 10 (emphasis added), available at https://www.occ.gov/news-issuances/speeches/2002/pub-speech-2002-10.pdf.

[131] OCC webpage, "Consumers and Communities: Consumer Protection – Payday Lending," available at https://www.occ.gov/topics/consumers-and-communities/consumer-protection/payday-lending/index-payday-lending.html (visited on Sept. 27, 2020). .

[132] *See* Comments filed by the Center for Responsible Lending et al. opposing the OCC's proposed "true lender" rule (Sept. 3, 2020), available at https://www.nclc.org/images/pdf/high_cost_small_loans/payday_loans/OCC-True-

By enabling predatory lending and impairing the states' authority to protect their residents, the OCC's proposed "true lender" rule and its usury preemption transfer rule undermine fundamental purposes of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank).[133] When Congress passed the Dodd-Frank Act in 2010, it strongly criticized federal financial regulators for failing to take effective measures to stop predatory nonprime mortgage lending during the 1990s and 2000s. Congress also condemned the OCC and the Office of Thrift Supervision ("OTS") for aggressively preempting efforts by many states to stop predatory lending during the 1990s and 2000s.[134]

The OTS's and OCC's regulatory failures and their unjustified preemption of state laws were major factors behind Congress's decisions to abolish the OTS and to adopt 12 U.S.C. § 25b, which imposes significant constraints on the OCC's authority to preempt state consumer financial laws.[135] As shown in the next section, the OCC has not complied with Section 25b and therefore has no legal authority for its new preemption efforts, which would severely undermine the states' ability to protect their residents from predatory nonbank lenders.

B. The OCC's Fintech Charter Initiative and Preemption Rules Do Not Comply with Section 25b

Section 25b of the NBA, enacted as part of the Dodd-Frank Act, establishes a new framework for determining whether state consumer financial laws apply to national banks and federal savings associations. Under Section 25b(b)(1) , a state consumer financial law is preempted "only if" (A) the state law has "a discriminatory effect on national banks," or (B) the

Lender-Comments.pdf; Christopher K. Odinet, "Predatory Fintech and the Politics of Banking," *Iowa Law Review* (forthcoming) (Aug. 26, 2020 draft available at http://ssrn.com/abstract=3677283).

[133] Pub. L. No. 111-203, 124 Stat. 1376 (2010).

[134] S. Rep. No. 111-176, at 15-18 (2010). For analysis of the pervasive failures by federal financial regulators to stop predatory nonprime lending and the devastating injuries caused to states, consumers, and the U.S. economy by the OCC's and OTS's preemption of state consumer protection laws and state enforcement efforts, see Kathleen Engel & Patricia A. McCoy, *supra* note 29, at 157-226; Wilmarth, "Dodd-Frank," *supra* note 29, at 897-919.

[135] S. Rep. No. 111-176, at 16-17, 25-26, 175-77 (2010).

state law "prevents or significantly interferes with the exercise by the national bank of its powers," or (C) the state law is preempted by a federal statute other than the NBA. Section 25b(b)(1)(B) expressly incorporates the "prevent or significantly interfere" standard for preemption established by the Supreme Court's 1996 decision in *Barnett Bank of Marion County, N.A. v. Nelson*.[136] The preemption framework for national banks under Section 25b also governs federal thrifts.[137]

When the OCC issues a preemptive ruling, Section 25b(c) requires the OCC to demonstrate that "substantial evidence, made on the record of the proceeding," supports the OCC's "specific finding" of preemption in accordance with *Barnett Bank*. The OCC must also act on a "case-by-case basis" when it issues a preemptive ruling. To satisfy the "case-by-case" requirement, the OCC must consider "the impact of a particular State consumer financial law on any national bank that is subject to that law, or the law of any other State with substantially equivalent terms." In addition, the OCC must "first consult with the Bureau of Consumer Financial Protection and take the views of the Bureau into account" when the OCC makes its "case-by-case" determination.[138]

The OCC fintech charter initiative, usury preemption transfer rule, and proposed "true lender" rule did not comply with Section 25b. The OCC did not apply the "prevents or significantly interferes" preemption standard, or satisfy the "substantial evidence" requirement,

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[136] 517 U.S. 25, 33 (1996); *see* 12 U.S.C. § 25b(b)(1)(B); *Lusnak*, 883 F.3d at 1188, 1191-94; *Hymes v. Bank of America, N.A.*, 408 F. Supp. 3d 171, 184 (E.D.N.Y. 2019); S. Rep. No. 111-176, at 175-76 (2010).

[137] 12 U.S.C. § 1465. Sections 25b(b)(4) and Section 1465(b) declare that the statutes governing national banks and federal thrifts do *not* create a regime of field preemption. Accordingly, state laws apply to national banks and federal thrifts *unless* they create an irreconcilable conflict with federal law, based on the "prevent or significantly interfere" preemption standard set forth in *Barnett Bank*, 517 U.S. at 31, 33. *See* Jared Elosta, "Dynamic Federalism and Consumer Financial Protection: How the Dodd-Frank Act Changes the Preemption Debate," 89 *North Carolina Law Review* 1273, 1276-77, 1298 (2011); Wilmarth, "Dodd-Frank," *supra* note 29, at 925-30 (2011).

[138] 12 U.S.C. § 25b(b)(3)(A), (B); *see Lusnak*, 883 F3d at 1192, 1194; Elosta, *supra* note 137, at 1300-01; Wilmarth, "Dodd-Frank," *supra* note 29, at 931-32.

or follow the "case-by-case" procedure when it issued those measures. Indeed, the OCC did not even attempt to fulfill Section 25b's requirements when it adopted those measures.[139]

The OCC claimed that its usury preemption transfer rule fell "outside of the scope of section 25b because of section 25b(f)."[140] However, that assertion is clearly erroneous. As shown above, Section 25b(f) provides that Section 25b does not affect "the authority conferred by [Section 85] for the charging of interest *by a national bank*" (emphasis added). Section 25b(f) did *not* exempt the OCC from complying with Section 25b when it sought to extend the preemptive scope of Section 85 to reach purchasers, assignees, and transferees of bank loans. The OCC's rule went far beyond the subject of the "charging of interest *by a national bank*."

The OCC's recent actions are the latest examples of its repeated failures to comply with Section 25b. When Congress passed the Dodd-Frank Act in 2010, it rejected the sweeping preemption rules issued by the OCC in 2004. The Senate committee report stated that, under Section 25b, "[t]he standard for preempting State consumer financial law would return to what it had been for decades, those recognized by the Supreme Court in *Barnett Bank v. Nelson*, 517 U.S. 25 (1996) (*Barnett*), undoing broader standards adopted by rules, orders, and interpretations issued by the OCC in 2004."[141]

In 2011, the OCC revised its preemption rules, purportedly to bring them into conformity with Section 25b.[142] However, the OCC's revised rules do not include the "prevent or significantly interfere" preemption standard established by *Barnett Bank*, despite Congress's express incorporation of that standard in 12 U.S.C. 25b(b)(1)(B). Notwithstanding that explicit

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[139] *See* Wilmarth Usury Preemption Transfer Comment Letter, *supra* note 4, at 2-4; Wilmarth "True Lender" Comment Letter, *supra* note 5, at 3-5.
[140] *See* OCC Usury Preemption Transfer Rule, *supra* note 4, at 33533.
[141] S. Rep. No. 111-176, at 175-76 (2010); *see also* Elosta, *supra* note 138, at 1298-1300; Wilmarth, "Dodd-Frank," *supra* note 29, at 936-37.
[142] OCC, "Office of Thrift Supervision Integration; Dodd-Frank Act Implementation," 76 Fed. Reg. 43549 (July 21, 2011).

mandate, the OCC asserted that "the Dodd-Frank Act does not create a new stand-alone 'prevents or significantly interferes' preemption standard."[143]

Three of the preemption rules that the OCC reissued in 2011 – 12 C.F.R. §§ 7.4007, 7.4008, and 34.4 – continue to assert that broad categories of state laws are preempted across the nation. When the OCC issued those sweeping and categorical preemption rules in 2011, the OCC did not comply with Section 25b's "substantial evidence" and "case-by-case" requirements. The OCC claimed that it did not need to comply with those requirements because its blanket preemption rules were based on the rules it adopted in 2004. The OCC claimed that its "regulations in effect prior to the effective date [of Dodd-Frank] are not subject to the case-by-case requirement."[144]

The OCC's contention that its 2004 rules remained valid – even though they did *not* comply with Section 25b's requirements – was plainly wrong. Under Section 25b(b)(1), state consumer financial laws are preempted "only if" a federal agency or court makes a preemption determination in full compliance with *all* of the requirements of Section 25b. Section 1043 of the Dodd-Frank Act (codified at 12 U.S.C. §5553) provides a very limited exception to that mandate. Section 1043 preserves the applicability of previous OCC regulations and orders to "any contract entered into [by a national bank or its subsidiary] before July 21, 2010" (the date of Dodd-Frank's enactment).[145] Congress intended that Section 1043 would "provide stability to existing contracts" – those entered into *before* Dodd-Frank's enactment – by allowing those contracts to be governed by the OCC's pre-Dodd-Frank rules and orders.[146]

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[143] *Id.* at 43555; *see Lusnak*, 883 F.3d at 1193-94 ("[T]he OCC has largely reaffirmed its previous preemption conclusions without further analysis under the *Barnett Bank* standard," and therefore the OCC's 2011 preemption rules "are entitled to little, if any, deference.").
[144] 76 Fed. Reg. at 43553, 43556-57, 43558.
[145] 12 U.S.C. § 5553.
[146] S. Rep. No. 111-176, at 175 (2010).

Section 1043's carefully limited exception demonstrates Congress's intent that the OCC's previous preemptive rules and orders would *not* apply to national bank transactions occurring *after* July 21, 2010 *unless* they were brought into full compliance with the new preemption framework established by Section 25b. The OCC's argument that its 2004 preemption rules – as reissued in 2011 – remain valid for *new* transactions *after* 2010 would render Section 1043 "meaningless, in violation of the 'endlessly repeated principle of statutory construction . . . that all words in a statute are to be assigned meaning, and that nothing therein is to be construed as surplusage.'"[147] Accordingly, the OCC violated Section 25b by issuing three blanket preemption rules in 2011 that did not comply with Section 25b's "prevents or significantly interferes" preemption standard or with Section 25b's "case-by-case" and "substantial evidence" requirements.[148]

The OCC has also failed to comply with Section 25b(d), which requires the OCC to "periodically conduct a review, though notice and public comment, of each determination that a provision of Federal law preempts a State consumer financial law," within five years after issuing that determination. The OCC must issue a public notice for each preemption review, including an invitation for public comments. After completing each preemption review, the OCC must issue a public notice describing the results of its review and submit a report to the House Financial Services Committee and the Senate Committee on Banking, Housing, and Urban Affairs. The OCC's public notice and report to those Committees must state whether the OCC intends to continue, rescind, or amend the preemption determination it reviewed. The OCC

[147] *Independent Ins. Agents of America, Inc. v. Hawke*, 211 F.3d 638, 643-44 (2000) (quoting *Qi-Zhou v. Meissner*, 70 F.3d 136, 139 (D.C. Cir. 1995)); *see also* Wilmarth, "Dodd-Frank," *supra* note 29, at 939-40.

[148] 12 C.F.R. §§ 7.4007, 7.4008 & 34.4. *See* Arthur E. Wilmarth, Jr., "OCC Gets It Wrong on Preemption, Again," *American Banker* (July 29, 2011), at 8, available on Westlaw at 2011 WLNR 14961080; *see also* Arthur E. Wilmarth, Jr., "The Financial Industry's Misguided Quest to Undermine the Consumer Financial Protection Bureau," 31 *Review of Banking & Financial Law* 881, 914-16 (2012), available at http://ssrn.com/abstract=1982149.

has not conducted any public reviews pursuant to Section 25b(d), even though the OCC issued its most important preemption rules nine years ago, in July 2011. The OCC has issued several other preemption rules that are at least 15-20 years old, and it has not conducted any public reviews of those rules under Section 25b(d).[149]

The Supreme Court has admonished the OCC that it cannot "pick and choose what portion of the law binds [it]."[150] The OCC should abandon its nondepository fintech charter initiative, rescind its usury preemption transfer rule, and withdraw its proposed "true lender" rule due to their lack of compliance with 12 U.S.C. § 25b. The OCC should also conduct public reviews of all of its existing preemption rules and orders that are more than five years old, as required by Section 25b(d). I urge Congress to exercise its oversight powers to compel the OCC to bring all of its preemptive regulations, orders, and policies into full compliance with Section 25b.

A.E.W., Jr. (9/29/20)

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[149] 12 U.S.C. § 25(d); *see, e.g.*, 12 C.F.R. §§ 7.4002, 7.4003, 7.4004, 7.4005, 34.5, and 37.1.
[150] *First National Bank of Logan v. Walker Bank & Trust Co.*, 385 U.S. 252, 261 (1966).