

COMMENTS OF THE
NATIONAL CONSUMER LAW CENTER
AND
CONSUMER FEDERATION OF AMERICA
NATIONAL ASSOCIATION OF CONSUMER ADVOCATES
U.S. PUBLIC INTEREST RESEARCH GROUP
TO
OFFICE OF COMPTROLLER OF THE CURRENCY
BANKING ACTIVITIES AND OPERATIONS;
REAL ESTATE LENDING AND APPRAISALS

Docket No. 03-16

October 6, 2003

The **National Consumer Law Center**¹ files these comments on behalf of its clients, with a special focus on low-income borrowers who have been affected by predatory mortgage lending and other abusive lending practices. These comments are also filed on behalf of **Consumer Federation of America**, the **National Association of Consumer Advocates** and the **U.S. Public Interest Research Group**.²

¹ The National Consumer Law Center, Inc. (NCLC) is a non-profit Massachusetts Corporation, founded in 1969, specializing in low-income consumer issues, with an emphasis on consumer credit. On a daily basis, NCLC provides legal and technical consulting and assistance on consumer law issues to legal services, government, and private attorneys representing low-income consumers across the country. NCLC publishes a series of sixteen practice treatises and annual supplements on consumer credit laws, including Truth In Lending, (4th ed. 1999) and Cost of Credit (2nd ed. 2000) and Repossessions and Foreclosures (4th ed. 1999) as well as bimonthly newsletters on a range of topics related to consumer credit issues and low-income consumers. NCLC became aware of predatory mortgage lending practices in the latter part of the 1980's, when the problem began to surface in earnest. Since that time, NCLC's staff has written and advocated extensively on the topic, conducted training for thousands of legal services and private attorneys on the law and litigation strategies to defend against such loans, and provided extensive oral and written testimony to numerous Congressional committees on the topic. NCLC's attorneys were closely involved with the enactment of the Home Ownership and Equity Protection Act in Congress, and the initial and subsequent rules pursuant to that Act. Representatives of NCLC have actively participated with industry, the Federal Reserve Board, Treasury, and HUD in extensive discussions about how to address predatory lending. *These comments are written by NCLC attorneys Elizabeth Renuart and Margot Saunders.*

²**Error! Main Document Only.**The **Consumer Federation of America** is a non-profit association of nearly 300 pro-consumer groups, with a combined membership of 50 million people. CFA was founded in 1968 to advance consumers' interests through advocacy and education.

The **National Association of Consumer Advocates** (NACA) is a non-profit corporation whose members are private and public sector attorneys, legal services attorneys, law professors, and law students, whose primary focus involves the protection and representation of consumers. NACA's mission is to promote justice for all consumers.

On August 5, 2003, the Office of the Comptroller of the Currency (OCC) published a notice of proposed rulemaking suggesting three new regulations that expand the authority of national banks and displace state law in an unprecedented fashion. These proposed regulations relate to real estate lending, lending not involving a security interest in real property, and deposit taking.³

Congress did not intend the OCC to preempt the field of lending generally or real estate lending in particular. To the extent that the format and language of this regulation suggest field preemption, the OCC does not have the authority to enact it. Congress did not divest the states of their inherent authority to regulate national banks conducting business within their borders. Instead, state laws apply to national banks unless they conflict with the National Bank Act or if they impair or impede the ability of national banks to conduct the business assigned to them by Congress.

These comments are provided in the following parts:

1. Overview – The OCC’s Mandate to Ensure the Safety and Soundness of National Banks Does *Not* Justify the Preemption of State Consumer Protection Laws.
2. National Banks, Their Operating Subsidiaries, Affiliates, and Holding Companies Participate in and Profit From Predatory Lending
3. Neither the OCC's Guidelines Nor the OCC’s Actions Provide Adequate Consumer Protection
4. The National Bank Act Does Not Explicitly or Implicitly Preempt All State Laws as They Relate to or Affect National Banks
5. The Scope of and Limitation to OCC’s Authority Regarding Real Estate Secured Lending: Section 371 Does Not Preempt the Field
6. Proposed 12 C.F.R. § 34.4 Improperly Overrides Traditional Areas of State Regulation
7. The OCC Lacks the Authority to Enact Proposed 12 C.F.R. § 7.4008 Regarding General Lending Practices
8. Operating Subsidiaries Are Not Entitled to the Preemption Privileges Afforded to Banks

The **U.S. Public Interest Research Group** is the national lobbying office for state PIRGs, which are non-profit, non-partisan consumer advocacy groups with half a million citizen members around the country.

³ 68 Fed. Reg. 46119 (Aug. 5, 2003).

1. Overview – The OCC’s Mandate to Ensure the Safety and Soundness of National Banks Does *Not* Justify the Preemption of State Consumer Protection Laws.

The basic rules of our republic have long placed the primary role of the protection of consumers on the states. While some federal agencies – the Federal Trade Commission and the Federal Reserve Board – are specifically charged with this task as well, nowhere in the National Banking Act is there any mention of the role of the OCC to protect consumers. The states have traditionally paved the way for the protection of their citizens, by creating state specific laws designed to balance the needs of the credit industry with the need to ensure that consumers are protected from overly aggressive lending tactics.

Congress delegated to the OCC the task of supervising national banks and protecting their viability by making sure that they do not engage in unsafe and unsound practices.⁴ The protection of consumers is not mentioned as part of a bank’s business or concern in the regulations issued by the OCC – except to the extent that the violation of consumer protection statutes might jeopardize the safety and soundness of the bank.⁵ As the OCC has pointed out, the violation of existing consumer protection laws poses risk to national banks either through actual threat of financial loss, risk of expensive or embarrassing litigation, or at the least risk to the reputation of the bank.⁶

However, the fact that enforcing safety and soundness principles may have the incidental benefit of providing protection to consumer, does not mean that the OCC, by itself, can both define the consumer protection rules applicable to national banks, *and* provide the only enforcement mechanism for those rules – as the OCC seeks to do in this regulation. Through this regulation the OCC seeks to place itself as the arbiter of the rules for national banks and operating subsidiaries – replacing its judgment for that of the legislatures of fifty states and the District of Columbia. The OCC also seeks to replace the consumer protection enforcement resources and judicial systems of these fifty one jurisdictions.

In fact, the OCC would be violating its statutory authority if it took actions simply for the protection of consumers, especially when the benefit of the protection might have a negative impact on the business of a national bank.⁷ While the OCC may vigorously enforce violations of federal consumer protection law, it does so to protect against

⁴ See 12 U.S.C. §§ 1813(q)(1) and 1818(b)(1).

⁵ Principles of “safety and soundness” generally apply to three goals– protecting the interests of bank as an institution, the depositor and of the deposit insurance funds. See, Financial Institutions Supervisory Act of 1966: Hearings on S. 3158 and S. 3695 Before the House Comm. On Banking and Currency 89th Cong., 2d Sess. 49-50 (citations omitted) (quoted in *In re Seidman*, 37 F.3d 911, 926 (3d Cir. 1994).

⁶ See, e.g. OCC Advisory Letter, AL 2003-2: Guidelines for National Banks to Guard Against Predatory and Abusive Lending Practices; and OCC Advisory Letter, AL 2003-3: Avoiding Predatory and Abusive Lending Practices in Brokered and Purchased Loans.

⁷ In *Gulf Federal Savings & Loan Ass’n v. FHLBB*, 651 F.2d 259 (5th Cir. 1981); *cert. denied* 458 U.S. 1121 (1982), the court specifically addressed issue of whether a supervisory agency could enforce consumer protections which did not pose a risk to the insurance funds, and the court specifically held that unsafe and unsound practices only encompass action that threaten the financial integrity of the institution or the insurance fund.

litigation, financial exposure, and ultimately risk of financial loss, or reputational risk to the banks.⁸ While, the OCC is charged with the mandate to enforce *existing* federal rules governing unfair or deceptive practices by national banks,⁹ it is not permitted to define what is unfair or deceptive, and it has done virtually nothing to use this authority for the protection of consumers.¹⁰ Requirements to ensure the safety and soundness of national banks may overlap with protecting consumers in some instances.¹¹ However, the general rule is that protecting consumers and protecting the value of the national bank charter are different goals with occasionally parallel, but often, conflicting paths. Examples of these conflicts include the myriad of consumer protection laws preempted by the OCC without any pretense that consumers would benefit from the preemption.¹²

The OCC spends so much effort in this proposal arguing that consumers will *benefit* from this preemption because if the OCC is permitted to preempt all state laws, there will be no effective consumer protections applicable throughout the United States. Federal consumer protection law relating to credit provides important, but minimal regulation regarding the terms and conditions of most credit. It is state law that regulates the rules of contract, the required terms of credit, the rules governing the ongoing relationship between the parties, the structure for repossession and foreclosure of secured property, and the definition of unfair practices, to name a few. Federal law does not begin to provide the detailed and explicit rules for the conduct of every day credit throughout the United States.

Relevancy of Fact Based Assertions. In support of its proposed actions, the OCC devotes a fair portion of its discussion on two fact-based issues which appear on first blush to be unrelated to the legal question of whether the OCC does have the legal authority to support this massive preemption of consumer protection laws. First, the OCC argues that national banks and their operating subsidiaries are *not* engaged in predatory lending. Second, in its Working Paper, the OCC claims that many of the laws passed by states to combat predatory lending actually hurt consumers by reducing credit availability.¹³

⁸ *In re Seidman*, 37 F.3d 911, 928 (1994) (“The “violation of law” provision . . . may be subject to the same limits as the “unsafe and unsound practice” provision If so, the cease and desist power would arise only when an association violates a law which protects the association’s financial integrity.”); *Kaplan v. OTS* 104 F.3d 417, 421 (D.C. Cir. 1997) (“the common element that (the agency) must show is behavior that creates an undue risk to the institution”); *Green County Bank v. FDIC*, 92 F.3d 633, 635 (8th Cir. 1996), *cert. denied*, 519 U.S. 1109 (1997); *Doolittle v. NCUA*, 992 F.2d 1531, 1538 (11th Cir. 1993), *cert. denied* 516 U.S. 987 (1995); *Jameson v. FDIC*, 931 F.2d 290, 291 (5th Cir. 1991) (*per curiam*) (falsifying bank records compromised the integrity of the records of the bank and thus was unsafe or unsound); *Van Dyke v. Board of Governors*, 876 F.2d 1377, 1380 (1989); *Gulf Fed. Sav. & Loan Ass’n v. FHLBB*, 651 F.2d 259, 264-65 (5th Cir. 1981), *cert. denied*, 458 U.S. 1121 (1982); *In re First Nat’l Bank of Eden v. Department of Treasury*, 568 F.2d 610, 611 n.2 (8th Cir. 1978);

⁹ 15 U.S.C. § 57a(f)(7).

¹⁰ See discussion below in section 4 of these comments on the OCC’s limited use of this authority to stop unfair or deceptive practices.

¹¹ *Id.*, see also, Patricia A. McCoy, *Banking Law Manual* § 13.03[3] (2d ed. 2002).

¹² Consider the extensive list of regulations and interpretative letters issued by the OCC preempting numerous state consumer protection laws between 1992 and 2003, without any pretense that consumers will benefit from this removal of consumer protections. <http://www.occ.treas.gov/advlst03.htm>.

¹³ OCC Working Paper, “Economic Issues in Predatory Lending,” July 30, 2003.

We vigorously dispute the factual basis for both of these assertions. First, national banks, their operating subsidiaries, their affiliates, and their stock holders *are* profiting extensively from loans which are defined as predatory in a broad variety of arenas.¹⁴ In the next section of these comments, we provide examples and explanations to refute the OCC's assertion on this point. The relevancy and reliability of the OCC's Working Paper are refuted in the attached letter to the OCC from Lauren Willis of Stanford Law School.¹⁵

The OCC's proposed preemption would have the effect of disenfranchising the considered approaches to protect consumers of the elected representatives to the legislatures of every state in the union. Yet, in its working paper, the OCC justifies the preemption of the particular laws passed by many states to combat predatory mortgage loans, by stating that consumers suffer from those state laws because the state laws result in a reduced availability of credit. While there is considerable dispute about that assertion – that the state laws have reduced the availability of credit – even assuming *arguendo* that were true, that does not justify the preemption of those laws.

Access to credit is valuable, but it is not always a good thing. Too much credit, especially when it is of the wrong kind –because it is unaffordable, strips equity or savings, results in the loss of other, more beneficial credit, or leads to the ultimate but avoidable loss of the home – is not good. State legislatures, in passing laws to combat predatory lending, have determined that some credit is not welcome in their state. So the OCC's assertion that because there is a reduced availability of credit in states where anti-predatory lending laws have been passed, thus justifies the preemption of those state laws, misses the point of those laws.¹⁶

The crux of the legal question at hand is the interpretation of the constitutional and federal statutory authority for the assertion of preemption. An essential facet of that interpretation is the issue of *who* or *which entities* will have the distinct charge of protecting consumers. Nothing in the National Banking Act supports a claim that the OCC is to look after the protection of consumers. Indeed, the OCC does *not* propose consumer protection as a justification for any of its regulations, advisory letters, or enforcement actions. Instead, the basis of the OCC's enforcement actions is always to ensure the safety and soundness of banks and the continued viability of the national bank charter. The task of protecting consumers is left to others – in this instance, primarily the states.

¹⁴See *e.g.* **Error! Main Document Only.**Opening Statement of Chairman Paul S. Sarbanes (D-MD) **Error! Main Document Only.**U.S.Senate, Committee on Banking, Housing and Urban Affairs, Hearing on "Predatory Mortgage Lending: The Problem, Impact and Responses." First Hearing in a Series, Thursday, July 26, 2001. http://banking.senate.gov/01_07hrg/072601/sarbanes.htm.; Testimony of Irv Acklesburg, **Error! Main Document Only.**Hearing on "Predatory Mortgage Lending: The Problem, Impact and Responses.." "Second Hearing in a Series, July 27, 2001. http://banking.senate.gov/01_07hrg/072701/aklsbrg.htm.

¹⁵ See, Exhibit A – Letter from Lauren Willis of Stanford Law School critiquing the OCC Working Paper.

¹⁶ *Id.*

The OCC offers these fact based assertions – that national banks are *not* engaged in predatory lending, and that state consumer protection laws hurt consumers anyway – in an attempt to show that the vacuum created by this preemption would not harm consumers. This factual issue – whether the proposed preemption of all state consumer protection laws would harm American consumers – is very much a relevant issue in this proceeding. **Our contention is that there is no question but that preemption of state consumer protection laws seriously jeopardizes consumers across the nation.**

2. National banks, Their Operating Subsidiaries, Affiliates, and Holding Companies Participate in and Profit From Predatory Lending

Predatory mortgage lending is an exploding problem in communities across America.¹⁷ Homeowners have not only lost their homes to foreclosure,¹⁸ they have lost their primary source of savings – their home equity – to overreaching and unethical business practices in the mortgage lending marketplace.

Three of the worst predatory practices involve the charging and financing of high amount of points and fees, heavy prepayment penalties accompanied by higher than par interest rates for those borrowers, and flipping. These practices typically provide the impetus for equity stripping (that reduces or eliminates the value of the consumer’s major asset) and most rewards the originator and subsequent holders of the loan (through an increase in the principal that is paid immediately to the originator upon sale to the secondary market or that is paid over time to the holder or recouped at foreclosure). The more the borrower is charged up-front, the more the financial gain achieved by the lender and holder. Prepayment penalties provide additional profit to the holder if the loan is paid off and provide an incentive to flip the customer to trigger this income stream. If the homeowner is unable to continue paying a loan, the lender or holder often refinances to make the loan “performing.” However, this just means more profit for the lender since a new round of points and fees are added to the principal and a prepayment may be collected as well.

Predatory lending is causing the massive loss of both equity and homes because the current legal and economic regime allows – indeed encourages – lending practices which reward lenders for making loans that are unnecessary, are unaffordable, bleed equity, and lead to foreclosure. Numerous state legislatures have recognized that the only way to halt these practices is to change the mortgage lending marketplace – so as to provide incentives to the lending industry to stop making predatory loans.

National banks, their subsidiaries and their affiliates are in business to make

¹⁷ **Error! Main Document Only.** U.S. Senate, Committee on Banking, Housing and Urban Affairs, Hearing on "Predatory Mortgage Lending: The Problem, Impact and Responses." First Hearing in a Series, Thursday, July 26, 2001. http://banking.senate.gov/01_07hrg/072601/index.htm.

¹⁸ While the rate of homeownership has increased only by 3.4% between 1980 and 2001, the rate of foreclosures has increased by over 252% during the same period. National Delinquency Survey, Mortgage Bankers Association of America and U.S. Census Bureau, Statistical Abstract of the U.S.; 2002, Tables 931 and 1160.

money. Banks and their affiliates profit from predatory lending in numerous way, including –

- making direct loans;
- buying predatory loans from brokers;
- investing in loan portfolios that contain predatory loans;
- providing securitization services for trusts which contain predatory loans.

The OCC's function as a regulator of national banks is to ensure that this activity does not jeopardize the deposits, or the ongoing functionality of the bank. Unless this activity affects the safety and soundness of a bank, the OCC has no other clear directive to intervene.

Unfortunately, many predatory practices are not illegal under federal law. This is why many states have stepped in and declared certain practices to be illegal. However, the OCC proposes to exempt national banks and their operating subsidiaries from the obligation to comply with state laws, thus leaving consumers who borrow money from non-exempt lenders potentially more protected than those who borrow money from banks. This makes no sense. In addition, affiliates of national banks would continue to be subject to the state laws. However, there is tremendous confusion around the country about which entities are operating subsidiaries and which are affiliates. To consumers these distinctions have no real meaning. Typically consumers go to their local bank, request a mortgage, and then are referred to either the bank's subsidiary or the bank's affiliate. The consumer has absolutely no way of knowing either that one entity is different from the next or that the legal structure governing their lending can be quite different.

Banks are more likely than finance companies to comply with applicable laws. This is because the banks are more closely supervised. Despite closer scrutiny, banks do engage in and profit from predatory lending, as described below.

A. Partial List of Pending and Closed Cases Involving National Banks or their Operating Subsidiaries or Affiliates Where Violations of Law and/or Predatory Practices Are Alleged

The following cases are examples of pending and closed cases against national banks or their operating subsidiaries involving violations of law and/or predatory loans. These are illustrative of the range of illegal or predatory lending activities currently engaged in by national banks, their affiliates and their subsidiaries throughout the nation.

Maudline Smith v. Ameriquest and NationsCredit, Case No. 32879-02 (N.Y. Sup. Ct., County of Queens). NationsCredit is an operating subsidiary of Bank of America. Case involved fraud and misrepresentation claims based upon a ten-year balloon loan with split loans made without knowledge of borrower.

Kelson v. Jones, Case No. #03cv1755 (D.D.C.). Case is against First Horizon Mortgage

Co., a subsidiary of First Tennessee Bank, N.A. Claims raised include violations of Truth in Lending Act, Real Estate Settlement Procedures Act, unconscionability, D.C. Consumer Protection Procedures Act violations, and D.C. Mortgage Lenders and Brokers Act violations.

Carroll v. Wells Fargo Home Mortgage, Case No. #03cv1837 (D.D.C.) Wells Fargo is an operating subsidiary of Wells Fargo Bank. Claims raised include TILA, D.C. Consumer Protections Procedures Act violations.

Jefferson v. Citibank as Trustee for Chase Manhattan Mortgage Corp, Case No. # 03-cv-4366 (D.C. Superior Court). Suit is against Citibank, N.A. Claims include D.C. Consumer Protections Procedures Act violations, unconscionability, D.C. Mortgage Lenders and Brokers Act violations.

Wells Fargo Home Mortgage v. Denise Brown et al. v. Peach & Pep Construction Co., Case No. 00-CH-481 (Cir. Ct. St. Clair County, Ill.). Case is against an operating subsidiary of Wells Fargo national bank. This is essentially a mortgage foreclosure action in which the homeowner counterclaimed against the lender for serious Truth in Lending disclosure violations; conspiracy to commit fraud with the seller (including misleading disclosures, not making a promised disbursement to a creditor); as well as claims against the seller.

Merriam v. Chase Manhattan Mortgage Corporation (In re Merriam), Case No. 02-10268-B.A.P. # 02-1111-B (Bankr. W.D.N.Y. Filed April 25, 2002). Case is against the purchaser of a loan originated by Advanta National Bank. The case is in the context of a Chapter 7 Bankruptcy Adversary proceeding involving allegations of 7 points and additional closing costs charged to elderly homeowners and of making two loans in order to charge another 5 points and to evade HOEPA; claims for other violations of HOEPA and TILA.

Hopkins v. Anderson, et al., Case No: C2 03 612 (Court of Common Pleas, Muskingum County, Ohio). This case is against ABN AMRO Mortgage Group, a subsidiary of Standard National Bank. This case is about the refinance of a mortgage loan through a broker whose licensed is not revoked, monthly payments which exceed 50% of Social Security income; loan with terms worse than promised. Causes of action include Ohio Consumer Sales Practices Act, fraud, aiding and abetting fraud, fruits of the fraud, unconscionability, and improvident lending, civil conspiracy, and negligent infliction of emotional distress.

Sandy and Michael Packer v. Bank One, Case No: ____ (Case Number to be assigned.) (Court of Common Pleas, Fairfield County, Ohio). This case, against a national bank, challenges the bank's repeated refinancing of its own mortgage loan, with origination points and lender fees exceeding \$12,000 on loans of \$140,000, with interest rates over 10% when conforming rates were close to 7%, unaffordable monthly payments that *increased* with refinancing. Legal claims include violations of the Truth in Lending Act, RESPA, Ohio Mortgage Brokers Act, breach of fiduciary duty, and civil conspiracy.

Bank One v. Kevin and Tamara Lethbridge v. Equitable Mortgage Group, et al., Case No: CV 2002-03-0723 (Court of Common Pleas, Butler County, Ohio). Claims are against Bank One and other players. As alleged, homeowners in this case, are defending against a foreclosure brought by a national bank, after being duped by a mortgage broker who tricked them into a much higher rate loan than the couple could afford. Claims include violations of the Ohio Mortgage Broker Act, breach of fiduciary duty, undue influence, breach of contract, violation of the Ohio Home Solicitation Sales Act, violation of the Consumer Sales Practices Act, fraud, intentional infliction of emotional distress, and violations of RESPA and TILA, as well as civil conspiracy.

Rossman v. Fleet Bank, 280 F.3d 384 (3d Cir. 2002). Case is against Fleet Bank. Court held that an alleged bait and switch scheme relating to a “no annual fee” credit card program could also violate the Truth in Lending Act.

Cooper v. First Gov’t Mortgage & Inv. Corp., 238 F. Supp. 2d 50 (D.D.C. 2002). One defendant was Altegra Credit Corp., an operating subsidiary of National City Bank of Indiana. Complaint alleged predatory and fraudulent tactics against lender, assignee, broker. Court denied summary judgment on issue of whether loan was a HOEPA loan and held that ordinary due diligence in the HOEPA context requires: 1) a review of the documentation required by TILA, the itemization of the amount financed, and other disclosure of disbursements regarding the loan at issue; 2) an analysis of these items; and 3) whatever further inquiry is objectively reasonable given the results of the analysis.

Williams v. Gelt Fin. Corp. (In re Williams), 232 B.R. 629 (Bankr. E.D. Pa. 1999), *aff’d*, 237 B.R. 590 (E.D. Pa. 1999). Case is against Gelt Fin. Corp. However, Altegra Credit Corp. bought a number of Gelt Fin. Corp. loans over the years. Altegra Credit Corp. is an operating subsidiary of National City Bank of Indiana. Case alleged violations of laws based on flipping of high cost loans (APRs were 20.243% and 15.123% balloon loans). Court found HOEPA TILA violations.

Bankers Trust Co. v. Payne, 730 N.Y.S.2d 200 (N.Y. Sup. Ct. 2001). Bankers Trust Co. of California, N.A., as trustee of loans originated by Delta Funding Corp. filed action to foreclose and homeowner defended. Homeowner defended on grounds of fraud and violations of HOEPA in a loan transaction to fund home improvements. Court denied summary judgment for the bank.

Crisomia v. Parkway Mortgage, Inc. (In re Crisomia), 2002 WL 31202722 (Bankr. E.D. Pa. Sept. 13, 2002). Case filed against Chase Manhattan Bank, among others. Homeowners alleged violations of the disclosure requirements of the Home Ownership and Equity Protection Act, violations of the Truth-in-Lending Act, violation of the Pennsylvania Home Improvement Finance Act, violation of the Pennsylvania Unfair Trade Practices and Consumer Protection Act. Court found the loan to be a high cost loan under HOEPA.

Lopez v. Delta Funding Corp., Case No. CV 98-7204 (CPS) (E.D.N.Y. Dec. 23, 1998). Case filed against the originator and trustees Bankers Trust Co. of California, N.A. and Norwest Bank Minnesota, N.A. Complaint alleged violations of state and federal law by the finance company and a group of mortgage brokers who allegedly systematically targeted low-income minority and/or elderly homeowners, inducing them to enter into fraudulent and exorbitantly priced mortgage loan transactions. Case settled.

People by Spitzer v. Delta Funding Corp., Case No. _____ (filed in E.D.N.Y.). The New York attorney general brought this lawsuit against a subprime mortgage lender for targeting African-American and Latino neighborhoods in Queens and Brooklyn for high-cost, high-interest mortgage loans. Also named as trustee on the pools of loans was Bankers Trust Co. of California, N.A. In 1999, the case settled. In 2000, the Attorney General's office enforced the injunctive relief obtained in the settlement through intensive monitoring, file review and other non-public actions. As a result, Delta has discontinued making loans that violate either the Home Ownership Equity Protection Act, or a new state regulation, Part 41. In addition, whereas broker fees had ranged as high as ten percent prior to the entry of the consent decree, brokerage fees effectively have been capped at five percent.¹⁹

Williams v. BankOne, N.A. (In re Williams), 291 B.R. 636, 664 (Bankr. E.D. Pa. 2003). Case is against BankOne, N.A. Allegations included a high cost loan made to an elderly couple with an APR of over 17% and violations of the Truth In Lending Act.

Jackson v. US Bank Nat'l Assoc. Trustee (In re Jackson), 245 B.R. 23 (Bankr. E.D. Pa. 2000). Adversary proceeding filed against U.S. Bank, N.A. as trustee of a pool of loans originated by Money-Line Mortgage. Complaint sought rescission under HOEPA and the TILA and claims for breach of contract, violation of the Pennsylvania Unfair Trade Practices and Consumer Protection Law, the Pennsylvania Home Improvement Finance Act, the Equal Credit Opportunity Act, and the Real Estate Settlement Procedure Act

Ray v. Citifinancial, Inc., 228 F. Supp. 2d 664 (D. Md. 2002). Case filed against Citifinancial, Inc., an affiliate or operating subsidiary of, or related to Citibank, N.A. or Citibank USA, N.A. Case involves a high cost loan with an APR of 18.99% plus five points with credit insurances allegedly packed into the loan.

Rodrigues v. U.S. Bank (In re Rodrigues), 278 B.R. 683, 688 (Bankr. D.R.I. 2002). Case filed against U.S. Bank, N.A. for a loan made by First Plus Financial, Inc. Court decision recites that the homeowners received a consolidation loan with an interest rate of 14.99% and had to pay ten points as well as other closing costs.

Matthews v. New Century Mortgage Corp., 185 F. Supp. 2d 874 (S.D. Ohio 2002). Case filed against original lender only. However, court opinion recites that U.S. Bank Trust, N.A., as the trustee, filed foreclosure against a named plaintiff to foreclose. Class action alleges that a broker referred a number of "stated income loans," high risk loans with high

¹⁹ For a press release about this case, see, www.oag.state.ny.us/2000AnnualReport.pdf.

interest rates, to New Century; that numerous such loan packages contained false and fraudulently obtained information; that all of the defendants engaged in a pattern or practice of targeting single, elderly females for unfair loan practices; that the defendants knew or should have known that the plaintiffs' monthly incomes were insufficient to take on the debt obligations that were effectively forced upon them by the defendants' fraudulent conduct. The lawsuit asserted claims the Federal Fair Housing Act; the Equal Credit Opportunity Act; the Truth-in-Lending Act; civil conspiracy; common law fraud; the Ohio RICO statute; and unconscionability.

Siradas v. Chase Lincoln First Bank, N.A., 1999 WL 787658 (S.D. N.Y. Sept. 30, 1999). Case filed against Chase Lincoln First Bank, N.A., succeeded by Chase Manhattan Bank, N.A. Class action alleges violation of state unfair and deceptive practices act due to the miscalculation of interest due to using the wrong index in variable rate loans).

Reynolds v. Beneficial Nat'l Bank, 260 F.Supp.2d 680 (N.D. Ill. 2003). Suit against Beneficial National Bank. Class action filed by recipients of high cost tax refund anticipation loans brought class action against bank and tax preparers, alleging violations of Truth in Lending Act, state consumer fraud statutes, breaches of contractual and fiduciary duties, and unjust enrichment. Court refused to accept proposed settlement after class members objected.

B. List of National Banks Acting as and Being Paid to be Trustees of Securitized Loans for Lenders of Notoriety

The following list of national banks received income from their roles as trustees of one or more pools of securitized loans for the listed lenders. A trustee, through written agreements, acts on behalf of the investors. It is essentially an administrative function which includes holding the pooled mortgages, hiring and monitoring servicers, managing and overseeing the payments to the bondholders, administering any reserve accounts, and foreclosing on the secured property if necessary. This list does not include the banks that bought shares of these securitized loan pools, another way that banks make a profit from predatory or problematic lending. In the aggregate, these pools represent billions of dollars of mortgage loans.

The listed lenders are those who have been the subject of federal and/or state enforcement actions, numerous individual lawsuits or class actions, and/or of newspaper articles or other press.

Trustee	Lender
Bank One, N.A.	Household Finance Co.
Bank One, N.A.	The Associates (bought by Citifinancial)
U.S. Bank, N.A.	Title 1 loans made to fund allegedly

	abusive home improvement loans in Philadelphia. ²⁰
U.S. Bank, N.A.	Equicredit Corp.
U.S. Bank, N.A.	Conseco Finance Corp.
Wells Fargo, N.A.	Delta Funding Corp.
Bankers Trust Co. of California, N.A.	Delta Funding Corp.
Deutsche Bank (formerly Bankers Trust)	United Companies Lending
Bankers Trust Co., N.A.	First Alliance Mortgage Co.
Chemical Bank	First Alliance Mortgage Co.
Norwest Bank, N.A.	First Alliance Mortgage Co.
Wells Fargo, N.A.	The Money Store
Bank One, N.A.	Southern Pacific Funding Corp.

3. Neither the OCC's Actions Nor its Guidelines Provide Adequate Protection Against Lending Activities of National Banks and Operating Subsidiaries

A. OCC's Actions Have Not Worked to Stop Predatory Lending Activities of National Banks

The preceding examples of lending activities of national banks and their operating subsidiaries should be viewed simply as *examples* of a huge problem existing in communities throughout this nation. Banks are very much involved in creating and profiting from the problems of predatory lending. Banks have consistently opposed efforts on both the state and federal levels to address these problems (with the one exception of their active support for the legislation designed to address predatory lending in North Carolina).

Despite the ongoing lawsuits and complaints about the sharp lending activities of some national banks and their operating subsidiaries, the OCC has done nothing meaningful to address the problem. In an effort to justify both the preemption determination of the Georgia Fair Lending Act (GFLA)²¹ and this proposal, the OCC issued two advisory letters purporting to provide comprehensive rules for banks to follow which would prevent predatory loans.²² And despite the lengthy verbiage included in both advisory letters, the bottom line is that neither Advisory Letter – nor any other guidelines issued by the OCC on predatory lending – actually provides clear rules to prohibit banks or their operating subsidiaries from engaging in or supporting predatory lending activities.

Notwithstanding some speeches by the Comptroller of Currency, and the Chief

²⁰ See “Deal is reached in loan fraud suit: A bank agreed to cover \$1 million for 164 homeowners victimized in the federal Title I program,” The Philadelphia Inquirer, Oct. 1, 2002.

²¹ 68 Fed. Reg. 46264 (Aug. 5, 2003).

²² OCC Advisory Letter, AL 2003-2: Guidelines for National Banks to Guard Against Predatory and Abusive Lending Practices; OCC Advisory Letter, AL 2003-3: Avoiding Predatory and Abusive Lending Practices in Brokered and Purchased Loans.

Counsel, there also appears to be little meaningful enforcement action taken over the past few years. The OCC is required to report to Congress every year regarding its required activities to address unfair or deceptive acts and practices.²³ This report is included in the report that the Federal Reserve Board makes to Congress every year. According to the most recent report, the OCC did not bring any actions against bank or operating subsidiaries for unfair or deceptive practices pursuant to its authority under Reg AA in 2002.²⁴

The OCC's website reveals its full list of actions taken to address unfair or deceptive practices in recent years. Only five actions are listed on the website, going back to year 2000.²⁵ While the OCC's actions in these cases are to be commended, there are only five actions in four years. Five enforcement actions should be juxtaposed with the multitude of private suits that have been brought during the same period (a few of which are listed in these comments above). This total of five is especially alarming when one realizes that if the OCC succeeds in its current plan to preempt consumer protection laws, many of the claims in these private enforcement actions will be thrown out of court.

Five enforcement actions in four years against over two thousand national banks, and thousands more operating subsidiaries, tells a story. It is an indication that the OCC has not, and cannot *by itself*, adequately protect consumers from the lending activities of the thousands of national banks and an unknown number operating subsidiaries²⁶ doing business in every community in this nation.²⁷

The OCC provides a link on its website to the OCC Customer Assistance Group.²⁸ This link supplies a method for bank customers who have problems with their banks to obtain the assistance from the OCC in resolving these problems. The assistance provided through this mechanism appears to be ephemeral, at best. While the website states that in the past year, over \$6 million in fees have been refunded to consumers, there is no detail provided regarding what kind of fees these were, or whether these are the same fees which are included in the self-laudatory explanation of the OCC's conclusion of its actions pursuant to its unfair and deceptive authority, referred to above. There is also a glaring lack of information regarding whether the consumers were satisfied with the resolution of the disputes, and whether the banks entered into binding stipulations designed to prevent a repeat of the illegal behavior.

Finally, common sense dictates that it is unlikely that the OCC could make a

²³ 15 U.S.C. § 57a(f)(7).

²⁴ Federal Reserve Board, 89th Annual Report to Congress – 2002, at 78.
<http://www.federalreserve.gov/boarddocs/rptcongress/annual02/ar02.pdf>.

²⁵ <http://www.occ.treas.gov/Unfair.htm>.

²⁶ When asked for a comprehensive list of the operating subsidiaries of national banks, the OCC has been unable to provide one. Julie Williams, Chief Counsel for the OCC, stated in a public meeting with consumer advocates on February 6, 2003, that the OCC was unable to provide a comprehensive list because the number and names of the operating subsidiaries were constantly changing.

²⁷ The OCC website states that there are two thousand, two hundred national banks that it supervises.
<http://www.occ.treas.gov/consumernews.htm>.

²⁸ <http://www.occ.treas.gov/customer1.htm>.

noticeable dent in the attack on predatory lending – especially when compared to the resources to protect consumers that this preemption regulation vaporizes. Currently, there is a nationwide network of state banking departments, offices of attorneys general, consumer protection divisions, and others to investigate and prosecute consumer complaints. Most of the state consumer protection laws the OCC would preempt have private rights of action that allow consumers to file cases in court. Indeed, many of the state anti-predatory lending laws specifically include provisions for attorneys’ fees for the purpose of enabling more private prosecutors to facilitate enforcement of these acts. Every one of these state enforcement mechanisms would be eliminated. To replace this panoply of state resources throughout the nation, with the power and authority of state government, the consistency of state judicial systems, and the transparency and openness provided by private and public enforcement of published rules, the OCC proposes its office of 40 individuals in Texas.

B. OCC’s Guidelines Will Not Stop Predatory Lending Activities by National Banks.

As partial justification for its preemption of state predatory lending laws, the OCC offers two advisory letters recently issued as a replacement for the full panoply of state anti-predatory lending laws which are being preempted. These letters are: OCC Advisory Letter, AL 2003-2: Guidelines for National Banks to Guard Against Predatory and Abusive Lending Practices; and OCC Advisory Letter, AL 2003-3: Avoiding Predatory and Abusive Lending Practices in Brokered and Purchased Loans. While these advisories identify several predatory practices, they do not prohibit or restrict these practices. Essentially, banks are cautioned to have procedures in place to guard against risk to the bank.

Both advisories concentrate their focus on the avoidance of risk for banks. The stated and only purpose of these letters is to direct banks to avoid threats to the safety and soundness and the reputation of the banks. There is nothing wrong with the OCC’s focus on directing national banks to protect themselves – that is the function of the OCC. *The problem is that very little in these advisory letters actually provides consumers with any valuable protection from predatory lending.* The only clear requirement imposed in these advisory letters is that banks –

have in place procedures and standards adequate to ensure that their broker arrangements and loan purchases do not present unwarranted risks.²⁹

While these advisory letters include discussion of predatory type behavior and caution about violating applicable federal law, they do not prohibit banks from engaging in these activities. The outlined standards are vague, require proof of the *intent* of the bank, or are permitted to be relaxed with justification.

The OCC’s Advisory Letter on Guidelines for National Banks to Guard Against

²⁹OCC AL 2003-3, at 1 (February 21, 2003).

Predatory and Abusive Lending Practices³⁰ was issued with great fanfare. This Advisory Letter is replete with truisms about the evils of predatory lending –

[T]he OCC believes it appropriate to set forth in this advisory letter supervisory guidance concerning lending practices that have been criticized as “predatory” or abusive.” Such practices are inconsistent with important national objectives, including the goals of fair access to credit, community development, and stable homeownership by the broadest spectrum of America. Any lending practices that take unfair advantage of borrowers, or that have a detrimental impact on communities, also conflict with the high standards of national banks.³¹

Everyone agrees that predatory lending should be stopped. However, rather than prohibiting predatory practices because they are or should be inherently unsafe and unsound, the OCC merely states that activities are proscribed if they are either –

- unlawful under existing federal laws and regulations, or
- involve unfair and deceptive conduct *and* present significant safety and soundness, reputation, and other risks to national banks.

If an activity is already illegal under federal law, the OCC’s letter provides no added value by directing banks to avoid it.

What exact predatory behaviors has the OCC actually provided direction about, under the second prong? None really, although there is a lot of discussion about the evils of certain specific behaviors – loan “flipping,” refinancing of special subsidized mortgages that result in the loss of beneficial loan terms, packing of hidden fees, using certain loan terms such as negative amortization or balloon payments, targeting inappropriate credit products to older borrowers, inadequate disclosure, offering single premium credit life insurance, and using mandatory arbitration clauses, no clear direction is provided. Banks are not prohibited from engaging in any behaviors.

There is no doubt that this Advisory Letter would be an extremely valuable tool in the overall battle against predatory lending *if these behaviors were specifically prohibited*. But they are not. There is no clear prohibition against selling single payment credit insurance. There is no clear direction to banks *not* to offer loans with negative amortization, balloon payment terms or mandatory arbitration clauses. *These loan terms are simply identified as possibly predatory – but banks are not prohibited from including them in mortgage loans.*

Banks are cautioned against violating the FTC Act’s prohibitions against unfair or deceptive acts or practices, and the FTC’s standard for evaluating these practices is outlined. Loan flipping and the refinancing of special subsidized mortgages are

³⁰ OCC AL 2003-2 (February 21, 2003).

³¹ *Id.* at 1.

specifically identified as potentially in violation of the FTC Act. The identification of the practice of refinancing special, subsidized mortgages as an unfair practice would seem to be valuable. However, the standard outlined for evaluating illegal loan flipping is so vague as to be fairly useless.

Similarly, in the balance of this Advisory Letter, there is little new direction that provides meaningful consumer protection against bad loans made by banks or the operating subsidiaries. For example, the banks are directed to avoid behaviors which might foreclose access to the secondary market, and the Fannie Mae and Freddie Mac guidelines against predatory lending are outlined. However, there is still no prohibition against making loans which violate these guidelines. As it is well known that there are many sources of funding for mortgage lending beyond Fannie Mae and Freddie Mac, repeating the predatory lending guidelines of the GSEs is fairly meaningless. The bottom line direction to banks is that they should ensure they have access to funds, not to avoid making loans which might hurt consumers.

A similar examination of the Advisory Letter on Avoiding Predatory and Abusive Lending in Brokered and Purchased Loans³² reveals little helpful to consumers. There is much discussion about the dangers of lending to borrowers who cannot afford the credit on the terms offered. However, there are no specific procedures that banks are required to engage in to ensure that consumers are not victimized by these practices. Even the identification of the clear abuse of charging an excessive amount of points and fees is undermined in two significant ways. First, the OCC seems to condone high points and fees so long as they are justified by the risk of the loan and second they are acceptable if the fees are adequately disclosed:

The potential for abuse is exacerbated when these fees and other charges far exceed those that would reflect the true costs and risks of the transaction, or are assessed and included in the loan principal without the borrower's informed consent.³³

Yet, the failure to adequately disclose the fees would result in violations of either the Truth in Lending Act or the Real Estate Settlement Procedures Act, or both, so the mandate on disclosures adds nothing. Further, the justification for high points based on the supposed costs and risks of the loan provides no helpful guidance. Why should a riskier loan merit more up-front fees to the originator? Risk of default has traditionally been recouped from higher interest rates, not fees. Finally, how does one evaluate and measure this?

The bottom line is summed up in the "Recommended Practices" section. Banks are required to have policies and procedures in place "to mitigate against the risks of acquiring predatory or abusive loans."³⁴ These procedures should ensure that the

³² OCC Advisory Letter, AL 2003-3 (February 21, 2003).

³³ *Id.* at 3.

³⁴ *Id.* at 6.

purchased loans “comport with the bank’s general lending . . . policies . . .”³⁵ Banks are required to have policies which must *address* certain activities, but banks are not required to *do or not do* any specific acts which would clearly prohibit loans and loan terms which are identified as predatory and damaging to consumers.

The vagueness of these Advisory Letters should be contrasted with the specific prohibitions and clear protections provided by the panoply of state laws which the OCC proposed to preempt in this regulation.³⁶

4. The National Bank Act Does Not Explicitly or Implicitly Preempt All State Laws as They Relate to or Affect National Banks

The OCC spends a large portion of the Supplementary Information accompanying the proposed rules discussing its view of the law regarding the relationship between national banks and state law. The agency argues that national banks are creatures of federal law and that federal banking jurisprudence places severe limits on the applicability of state law to these entities.³⁷ However, the OCC fails to mention the court decisions in which state laws were upheld in the face of challenges by national banks. Further, it does not discuss in any detail the numerous instances in federal law where Congress explicitly recognized the applicability of state law to national banks. To balance the record, we will comment on these issues.

Since the Civil War, the United States has maintained a dual banking system. “The dual American system of banking is premised on a federalist division of powers and divides the regulation of depository institutions between the federal government and the states.”³⁸ Further, Congress distributed federal regulatory authority over depository institutions to several federal agencies, including the Office of the Comptroller of the Currency, the Office of Thrift Supervision, the Federal Deposit Insurance Corporation, the Federal Reserve Board, the National Credit Union Administration, and the Federal Financial Institutions Examination Council.

Under the dual system, the states have authority to regulate the business of national banks unless such regulation conflicts with the NBA or if the state law impairs or impedes the ability of national banks to conduct the business assigned to them by Congress.³⁹ Indeed, the Supreme Court has stated:

In defining the pre-emptive scope of statutes and regulations granting a power to national banks, these cases take the view that normally Congress would not want States to forbid, or to impair significantly, the exercise of a

³⁵ *Id.*

³⁶ *See, e.g.* Georgia Fair Lending Act, GA Code. Ann § 7-6A-1 *et seq.*

³⁷ 68 Fed. Reg. at 46121-46123 (August 5, 2003).

³⁸ Patricia A. McCoy, *Banking Law Manual* § 2.01 (2d ed. 2002).

³⁹ *Waite v. Dowley*, 94 U.S. 527, 533 (1877). *See also Barnett Bank of Marion County v. Nelson*, 517 U.S. 25, 31 (1996).

power that Congress explicitly granted. To say this is not to deprive States of the power to regulate national banks, where (unlike here) doing so does not prevent or significantly interfere with the national bank's exercise of its powers.⁴⁰

The Court then cited to *Anderson Nat. Bank v. Lockett*, 321 U.S. 233, 247-252 (1944) (state statute administering abandoned deposit accounts did not "unlawful[ly] encroac[h] on the rights and privileges of national banks"); *McClellan v. Chipman*, 164 U.S. 347, 358 (1896) (application to national banks of state statute forbidding certain real estate transfers by insolvent transferees would not "destro[y] or hampe[r]" national banks' functions); *National Bank v. Commonwealth*, 76 U.S. (9 Wall.) 353, 362, 19 L.Ed. 701 (1869) (national banks subject to state law that does not "interfere with, or impair [national banks'] efficiency in performing the functions by which they are designed to serve [the Federal] Government").

Further, Congress has repeatedly expressed its intention that state laws apply to national banks on a host of issues. The Chart below lists these laws and describes how state law applies. However, it is illustrative only and does not purport to be exhaustive.

EXPRESS APPLICABILITY OF STATE LAW TO NATIONAL BANKS

Federal Law	Citation	Description of State Law Applicability
National Bank Act	12 U.S.C. § 92a(a)	Comptroller may grant fiduciary powers "by special permit to national banks applying therefor, when not in contravention of State or local law."
National Bank Act	12 U.S.C. § 29	National bank may hold certain real property for longer periods of time as would be permitted a state chartered bank by the law of the state in which the national bank is located.
National Bank Act	12 U.S.C. § 35	State bank can convert to a national bank as long as the conversion is not prohibited by state law.
National Bank Act	12 U.S.C. § 484	State auditors and examiners may review bank records to ensure compliance with applicable state unclaimed property or escheat laws.
National Bank Act	12 U.S.C. § 85	Banks permitted to charge a rate of

⁴⁰ *Barnett Bank of Marian County, N.A. v. Nelson*, 517 U.S. 25, 33-34 (1996).

		interest allowed by the laws of the state where the bank is located or an alternate federal rate.
National Bank Act	12 U.S.C. § 90	If any deposit is made by a state or political subdivision within the state, the national bank shall give security for the safekeeping of the funds and prompt payment to the same extent and of the same kind as authorized by the state law.
National Bank Act	12 U.S.C. § 75	National bank observes state legal holidays when setting the annual meeting of the shareholders.
Interstate Banking and Branching Efficiency Act of 1994	12 U.S.C. § 36(c)	Permitting national banks to operate branches, but only where state law authorizes state banks to do so.
Interstate Banking and Branching Efficiency Act of 1994	12 U.S.C. § 36(f)(2)	Laws of the state in which a branch is located apply to the branch to the same extent as if the parent national bank were located in that state.
Interstate Banking and Branching Efficiency Act of 1994	12 U.S.C. § 36(f)(1)	Laws of the host state regarding community reinvestment, consumer protection, fair lending, and the establishment of intrastate branches shall apply to any branch to the same extent that state law applies to a branch of a state chartered bank unless federal law preempts the application of such state law or the Comptroller determines there is a discriminatory effect on the branch.
Interstate Banking and Branching Efficiency Act of 1994	12 U.S.C. § 43	Comptroller must publish for comment and in final version any opinion letter or interpretative rule that concludes that federal law preempts the application of any state law regarding community reinvestment, consumer protection, fair lending, and the establishment of intrastate branches, except in limited circumstances.

Bank Holding Act	12 U.S.C. § 1846(a)	The act shall not be construed to prevent any state from exercising any powers which it had at the time the act was passed or may have in the future over banks, bank holding companies, and subsidiaries.
Bank Holding Act	12 U.S.C. § 1846(b)	The act shall not prevent the states from taxing any bank or holding company to the extent that the tax is otherwise permissible.
Gramm-Leach-Bliley Act	15 U.S.C. § 6701(d)(2)(B)(i)-(xiii), (e)	National banks may engage in insurance sales, solicitation, or cross-marketing subject to thirteen types of state regulation so long as the restrictions are no more burdensome than those in the act and do not discriminate against or impose a disparate burden on the bank.
Truth In Lending Act	15 U.S.C. § 1610(a)(2)	State disclosure laws not preempted except to the extent that those laws are inconsistent with TILA; no exclusion for banks.
Real Estate Settlement Procedures Act	12 U.S.C. § 2616	State laws regarding settlement practices not preempted except to the extent that those laws are inconsistent; no exception for banks.
Fair Debt Collections Practices Act	15 U.S.C. § 1692n	State laws regarding debt collection practices not preempted except to the extent that those laws are inconsistent; state law in not inconsistent if the protection such law affords is greater than the protection under the federal act; no exception for banks.
Equal Credit Opportunity Act	15 U.S.C. § 1691d(f)	State laws regarding credit discrimination not preempted except to the extent that those laws are inconsistent; state law in not inconsistent if the protection such law affords is greater than the protection under the federal act; no exception for banks.
Fair Credit	15 U.S.C. § 1681t	State laws regarding the collection,

Reporting Act		distribution, or use of any information on consumers not preempted except to the extent that those laws are inconsistent; however, states cannot legislate in six areas specifically mentioned; no exceptions for banks.
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Significantly, *silence* in the National Bank Act regarding the applicability of state law does not necessarily mean that state law cannot apply to a national bank even for activities that relate to express bank powers. For example, the Act expressly allows banks to loan money.⁴¹ By necessity, lending entails the collection of loans in default. However, the OCC itself recognized that states retain power to regulate in the area of debt collection.⁴² In 2002, the OCC clearly articulated that several types of state law apply to national banks, including contract, commercial, real estate, property, tort, criminal, debt collection, zoning, and unfair and deceptive acts.⁴³ National banks follow other state laws not specifically mentioned in the OCC’s list, including laws relating to foreclosure, redemption rights, homestead and property exemptions, statutes of frauds, and state procedural laws.

Given this history, states clearly play a role in regulating some of the activities of national banks. In the area of lending, that role, though limited, is important.

5. The Scope of and Limitation to OCC’s Authority Regarding Real Estate Secured Lending: Section 371 Does Not Preempt the Field

In its proposal, the OCC suggests that § 371 of the National Bank Act grants it authority to preempt *all* state laws related to real estate lending, *i.e.*, “field” preemption. This argument builds upon a suggestion by National City Bank in its request for a preemption opinion regarding Georgia’s Fair Lending Act.⁴⁴ However, until now, the OCC never interpreted §371 in this fashion in either its interpretative letters or the earlier and current regulations related to real estate lending.

Congress granted national banks the specific authority to conduct real estate lending activities in 1913.⁴⁵ The original provision and subsequent versions contained a limited grant of authority to national banks and imposed geographic, term, loan amount, and aggregate lending limits. In the Garn-St. Germain Depository Institutions Act of 1982, Congress considerably shortened what had been codified as 12 U.S.C. § 371 to the following:

⁴¹ 12 U.S.C. § 24 (Seventh).

⁴² See OCC Advisory Letter No. AL 2002-9 (Nov. 25, 2002) and OCC Advisory Letter No. AL 2002-3 (March 22, 2002). The OCC endorsed the court decision in *Bank of America v. City and County of San Francisco*, 309 F.3d 551, 559 (9th Cir. 2002).

⁴³ *Id.*

⁴⁴ 68 Fed. Reg. at 46124. (August 5, 2003).

⁴⁵ Federal Reserve Act, ch. 6, § 24, 38 Stat. 251,273 (1913).

Any national banking association may make, arrange, purchase or sell loans or extensions of credit secured by liens on interests in real estate, *subject to such terms, conditions, and limitations as may be prescribed by the Comptroller of the Currency by order, rule, or regulation.*⁴⁶

Significantly, the italicized portion of this language existed in the pre-1982 version as § 371(g). This provision stated: “Loans made pursuant to this section shall be subject to such conditions and limitations as the Comptroller of the Currency may prescribe by rule or regulation.” Thus, the 1982 changes to § 371 did not broaden the scope of the Comptroller’s authority to set terms and conditions. Rather, Congress eliminated restrictions to national bank powers.

A perusal of § 371 reveals that Congress did not state that only federal law applies to national banks when engaging in real estate lending. Nor did Congress exclude the possibility that state law would also apply to national banks when exercising this authority. Section 371 is *silent* on this issue. The statutory construction maxim of *expressio unius est exclusio alterius* (the mention of one thing implies exclusion of another) does not apply here because Congress mentioned neither federal nor state law in § 371. Therefore, there is no mention of one thing to the exclusion of another. What is clear is that the banks have more flexibility to engage in real estate lending than they did before 1982 and that the Comptroller may set terms, limitations, and conditions on this type of lending.

In the Supplementary Information accompanying the proposed rule changes at issue in this Comment, the OCC implies that it simply has not yet exercised its full authority.⁴⁷ This is a disingenuous version of history. In fact, the OCC’s prior interpretation of § 371 leads to quite a different conclusion. The history of the OCC’s view is important given the agency’s present attempt to preempt virtually all state law.

After the 1982 amendment to § 371, the OCC promulgated 12 C.F.R. § 34 that set forth standards for real-estate related lending and associated activities by national banks.⁴⁸ There, the OCC listed five categories of state law that expressly do not apply to national banks. The types of state laws affected were those that relate to the loan-to-value ratio, the schedule of repayment, the term, the maximum loan amount, and covenants and restrictions necessary to qualify a leasehold as acceptable security.⁴⁹ The regulation then

⁴⁶ Pub. L. No. 97-320, Title IV, § 403(a), 96 Stat. 1510 (1982)(emphasis added). The purpose of this change was to: “simplify the statutory framework by which national banks are authorized to engage in real estate activities. The revised provision deletes existing rigid statutory standards and authorizes the Comptroller to promulgate regulatory standards affecting such conduct including the terms and conditions of mortgage transactions.” Senate Report No. 97-536, 60 (Sept. 3, 1982), *reprinted in* 1982 U.S.C.C.A.N. 3054, 3114.

⁴⁷ 68 Fed. Reg. at 46125 (August 5, 2003).

⁴⁸ 48 Fed. Reg. 40698-01 (Sept. 9, 1983).

⁴⁹ 12 C.F.R. § 34.2. This regulation is reprinted below:

explicitly stated that state laws of the types listed in these categories are preempted. Since the agency identified only five categories of laws, state laws not described applied to national banks, absent preemption under another provision of the NBA.

At that time, the OCC had this to say about the new § 371 and § 34.2 and the preemption of state law:

The Congress, when it passed the Act, sought to provide flexibility in real estate lending for national banks. The Office is preempting, at this time, only those state laws that govern those areas in which federal limitations and restrictions are eliminated. This is to preclu[d]e any conflict of state law with Congressional intent and the intent of the Office in removing the regulatory restrictions. The final rule clarifies the *limited* scope of the preemption. Aside from the specific preemption of state law as to the restrictions discussed, the relationship between state and federal law in regard to real estate loans as it existed prior to the amendment of 12 U.S.C. § 371 is expected to remain unchanged. Other changes in the regulations are intended to assure that banks are aware that other federal laws and regulations remain applicable.⁵⁰

Thus, the extent of preemption in the area of real estate lending was limited to those five types of loan terms or loan conditions itemized in § 34.2(a) and *no others*. Otherwise, the relationship between federal and state law in existence before the 1982 revisions to § 371

(a) State Law. National banks may proceed under 12 U.S.C. 371 and § 34.1 without regard to state law limitations as to:

- (1) The amount of a loan in relation to the appraised value of the real estate;
- (2) The schedule for the repayment of principal and interest;
- (3) The term to maturity of the loan;
- (4) The aggregate amount of funds which may be loaned upon the security of real estate; and
- (5) The covenants and restrictions that must be contained in a lease to qualify the leasehold as acceptable security for a real estate loan.

Limitations imposed on paragraphs (a)(1) through (5) of this section directly or indirectly by law or judicial decisions of any state, the District of Columbia, Puerto Rico, the Virgin Islands, the Trust Territory of the Pacific Islands, and Guam are hereby expressed preempted.

(b) Federal Law. National banks, in making real estate loans pursuant to this part, must comply with all applicable federal laws and regulations, including those pertaining to disclosure.

⁵⁰ 48 Fed. Reg. at 40699(emphasis added).

remained unchanged. This meant that the agency believed that the scope of preemption was limited, rather than expansive. Now, however, the agency is attempting to re-write history.

It is interesting to note how the OCC has viewed its authority under § 34.2 since 1982. In a 1992 letter regarding Pennsylvania laws restricting residential mortgage loan amortization schedules, the OCC stated: “The states also concurrently regulate real estate lending. The OCC’s regulation provided for *limited* preemption of such state statutes in the case of national banks.”⁵¹

Since 1982, the OCC itself has applied conflict analysis in the area of real estate lending. For example, the OCC affirmed that conflict preemption principles must be used in deciding if another Georgia law, the Residential Mortgage Act, was preempted. There, the OCC opined: “There are *many* occasions when national banks are legitimately bound by state law. Nevertheless, national banks derive their powers and authority under federal law, and they are not subject to state law if it conflicts with some paramount federal law.”⁵²

As previously noted, the OCC has recognized that there are traditional areas of state law that generally apply to national banks. These types of laws include: contract, commercial (including each state’s version of the UCC), real estate, property, tort, criminal, debt collection, taxation, zoning, unfair and deceptive acts and practices, and foreclosure laws.⁵³ Consequently, the OCC’s public interpretation of § 371 is not and never has been that suggested by the OCC now, *i.e.*, a vehicle to preempt claim field preemption in the area of real estate lending.

If the OCC stakes out this position, the courts are not likely to uphold it. They have uniformly held that the standard to meet when reviewing a state law’s applicability to a national bank is whether the law in question impairs, impedes, or conflicts with the National Bank Act or the powers of national banks to operate. *See, e.g., Barnett Bank of Marion County v. Nelson*, 517 U.S. 25, 31 (1996); *Franklin Nat’l Bank of Franklin Square v. New York*, 347 U.S. 373, 378-379 (1954); *First Nat’l Bank v. Missouri*, 263 U.S. 640, 656 (1924), *First Nat’l Bank of San Jose v. California*, 262 U.S. 366, 368-369 (1923).

6. Proposed 12 C.F.R. § 34.4 Improperly Overrides Traditional Areas of State Regulation

Proposed § 34.4 dramatically expands the current § 34.4. As noted above, current § 34.4 identifies five types of state laws affecting real estate lending that do not apply to

⁵¹ Letter of September 30, 1992 from William B. Glidden, Assistant Director, Bank Operations and Asset Division. (emphasis added).

⁵² OCC Interpretative Letter No. 644 (May 1994)(emphasis added).

⁵³ *See* OCC Advisory Letter No. AL 2002-9 (Nov. 25, 2002) and OCC Advisory Letter No. AL 2002-3 (March 22, 2002). *See also Bank of America v. City and County of San Francisco*, 309 F.3d 551, 559 (9th Cir. 2002)(even though the court agreed that the NBA preempts local restrictions on fees charged at ATMs, the court recognized that certain types of state law traditionally have applied to national banks).

national banks. These are laws that govern the amount of a loan in relation to the appraised value of the real estate, the schedule for the repayment of principal and interest, the term to maturity of the loan, the aggregate amount of funds that may be loaned upon the security of real estate, and the covenants and restrictions that must be contained in a lease to qualify the leasehold as acceptable security for a real estate loan.

In contrast, proposed § 34.4 includes these five items as well as state law governing:

- licensing, registration, filings, or reports by creditors;
- the ability of a creditor to require or obtain private mortgage insurance, insurance for other collateral, or other credit enhancements or risk mitigants, in furtherance of safe and sound banking practices;
- amortization of loans, balance, payments due, minimum payments;
- the circumstances under which a loan may be called due and payable upon the passage of time or a specified event external to the loan;
- escrow accounts, impound accounts, and similar accounts;
- access to, and use of, credit reports;
- mandated statements, disclosure and advertising, including laws requiring specific statements, information, or other content to be included in credit application forms, credit solicitations, billing statements, credit contracts, or other credit-related documents;
- processing, origination, servicing, sale or purchase of, or investment or participation in, mortgages;
- disbursements and repayments;
- rates of interest on loans;
- due-on-sale clauses.

Given the host of activities related to lending described, the OCC clearly is setting the stage to claim field preemption in the final version or sometime in the future when it is convenient to do so. The fact that this regulation mirrors the OTS regulation which the OTS claims preempts the field, evidences this intent.

In addition to this general concern, the preemption of several items on this list is problematic. First, “reports by creditors” is a very broad category.⁵⁴ This could refer to credit reporting obligations imposed by the states under the authority granted by Congress in the federal Fair Credit Reporting Act. As noted in the chart above, that Act does not preempt state laws that are not inconsistent with certain provisions of the Act.⁵⁵ To the extent that the non-preempted state laws relate to credit reporting, they should not be included in OCC’s list. In addition, state escheat laws may require the reporting of dormant escrow accounts or other accounts containing funds owned by a borrower. State escheat laws apply to national banks. To the extent that this reporting provision trumps such laws, it should be limited or clarified.

⁵⁴ Proposed 12 C.F.R. § 34.4(a)(1).

⁵⁵ 15 U.S.C. § 1681t. There are six provisions of the Act that cannot be supplemented by state law.

Second, regarding credit insurance and private mortgage insurance,⁵⁶ the federal McCarran-Ferguson Act creates a clear-cut rule “that state laws enacted ‘for the purpose of regulating the business of insurance’ do not yield to conflicting federal statutes unless a federal statute specifically requires otherwise in certain circumstances.”⁵⁷ Only one federal law permits otherwise. The Gramm-Leach-Bliley Act (GLBA) permits national banks to engage in insurance sales, solicitations, and cross-marketing. However, the Act does not provide an exception from McCarran-Ferguson in thirteen areas.⁵⁸ These exceptions include: requiring private mortgage or other insurance to be purchased from the bank or an affiliate; the payment of commissions in certain circumstances; the release of information; and certain types of written disclosures. To the extent that proposed § 34.4 attempts to extend national bank preemption beyond that expressly permitted in GLBA, this action conflicts with the McCarran-Ferguson Act.⁵⁹

Third, state laws regarding escrow accounts, impound accounts, and similar accounts as well as disbursements from these accounts⁶⁰ are governed by the federal Real Estate Settlement Procedures Act.⁶¹ As noted in the chart above, state laws regarding escrow practices are not preempted by RESPA, except to the extent that those laws are inconsistent⁶² The laws of approximately seventeen states will be undermined by the OCC’s expansion into this area of consumer protection.⁶³

Fourth, as to access to and use of credit reports,⁶⁴ to the extent that states may legislate in this area under the Fair Credit Reporting Act, OCC cannot preempt those state laws.⁶⁵

Fifth, some state disclosure laws cover the same type of information as the Truth In Lending Act. Such laws are not preempted by TILA as long as they are not inconsistent with that Act.⁶⁶ Thus, such disclosure requirements should apply to national banks.⁶⁷ As Truth in Lending mandates neither similar or even related disclosures, it could not be the basis of the preempting these state disclosure requirements.

⁵⁶ Proposed 12 C.F.R. § 34.4(a)(2).

⁵⁷ *U.S. Dept. of Treasury v. Fabe*, 508 U.S. 491,507 (1993).

⁵⁸ 15 U.S.C. § 6701(d)(2)(B).

⁵⁹ The GLBA states that McCarran-Ferguson remains the law of the United States. 15 U.S.C. § 6701(a).

⁶⁰ Proposed 12 C.F.R. §§ 34.4(a)(6) and (11).

⁶¹ 12 C.F.R. § 2609.

⁶² 12 U.S.C. § 2616.

⁶³ Those states include: California, Colorado, Connecticut, Florida, Iowa, Kansas, Maryland, Minnesota, New Jersey, New Mexico, New York, North Dakota, Oregon, Rhode Island, Utah, Vermont, and Wisconsin

⁶⁴ Proposed 12 C.F.R. § 34.4(a)(8).

⁶⁵ 15 U.S.C. § 1681t.

⁶⁶ 15 U.S.C. § 1610(a)(2). *But see American Bankers Association v. Lockyer*, 239 F. Supp. 2d 1000 (E.D. Cal. 2002). There, the court held that TILA does not save the application of a state law requiring the disclosure of minimum payments on credit card accounts and related information against a national bank. However, this California law mandated the disclosure of information not covered by TILA. Consequently, the non-preemption provision in TILA arguably does not apply.

⁶⁷ 239 F. Supp. 2d 1000 (E.D. Cal. 2002). *See* Proposed 12 C.F.R. § 34.4(a)(9).

Sixth, the servicing of mortgage loans is often performed by third party agents of banks. In addition, national banks can perform the servicing for their own loans or the loans of others. The Real Estate Settlement Procedures Act governs the behavior of servicers, whether they are third parties or the lenders themselves.⁶⁸ As noted in the chart above, RESPA permits states to also regulate the behavior of such entities as long as those laws are not inconsistent or provide greater protections than RESPA.⁶⁹ The only relevant caveat to this general non-preemption provision exists in RESPA's servicing section. As to the timing, content, and procedures for notification of the borrower at the time of application or transfer of servicing, if a lender follows the federal rules, it is deemed to have followed any state laws on the governing the same issues.⁷⁰

By adding servicing into the list of preempted state laws,⁷¹ the OCC not only eviscerates the non-preemption provision of RESPA but also reverses its policy to recognize state laws related to servicing, as long as they are not preempted by RESPA. In the Comptroller's Handbook regarding consumer compliance examinations, *Real Estate Settlement Procedures* (August 1996), the Comptroller states: "In general, state laws shall not be affected by the act, except to the extent that they are inconsistent and then only to the extent of the inconsistency."⁷²

In addition, many servicers are third parties hired by national banks or their subsidiaries to collect monthly payments, manage the payment and escrow accounts, resolve delinquencies, and obtain an attorney in the event that foreclosure becomes necessary. These third parties are not governed by the National Bank Act. Consequently, state law fully applies to these entities. Indeed, regarding payday lenders operating as agents of national banks, the Comptroller stated:

The benefit that national banks enjoy by reason of this important constitutional doctrine [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*.⁷³

Thus, to the extent that the proposed regulation would deputize third parties to wear the national bank cloak when servicing loans for national banks, it is illegal as beyond the authority of the Comptroller to enact.

⁶⁸ 12 U.S.C. § 2605.

⁶⁹ 12 U.S.C. § 2616.

⁷⁰ 12 U.S.C. § 2605(h).

⁷¹ Proposed 12 C.F.R. § 34.4(a)(10).

⁷² Handbook at 14.

⁷³ Speech on Feb. 12, 2002, available at www.occ.treas.gov/ftp/release/2002-10a.doc.

The laws of approximately fourteen states are potentially undermined by the OCC's inclusion of servicing in its preemption regulation.⁷⁴ Given the OCC handbook, what other states have done, and the fact that many servicers are third parties, there should be no preemption for these activities.

Seventh, "rates of interest on loans" is listed in the expanded regulation.⁷⁵ The National Bank Act clearly states that national banks can charge the higher two alternative rates of interest: either the federal rate based on the federal discount rate or the rate allowed lenders under state law.⁷⁶ The Comptroller does not have the authority to say that all state laws related to rates of interest are preempted when the Act allows banks to charge the state rate if it is higher than the federal rate. In other words, the Comptroller does not have the authority to allow national banks to charge more than the state rate allowed in their home state. To the extent that the proposed regulation would permit this type of behavior, it is illegal.

Finally, the OCC sets forth eight examples of the types of state laws that are not preempted *if* they only incidentally affect the real estate lending powers of national banks. Noticeably absent from this list are state consumer protection laws which the OCC has agreed apply to national banks. In addition, state foreclosure, redemption statutes, and enforcement of judgment laws have traditionally applied to banks as well as state statute of frauds, limitations, and procedural rules. These are laws critical to consumers and must be listed. Further, the OCC makes itself the final arbiter of which other state laws may have only an incidental effect on banks. This type of decision is one historically left to the courts. By attempting to change this important system of checks and balances, the OCC, whose sole constituents are the banks, is making itself the servant of the banks and their judge and jury as well. Further, the standard is virtually impossible to meet because all laws will have something more than a mere incidental effect on the business of banking. Therefore, it is likely that the OCC will find that few, if any state laws apply to banks, a radical departure from the current regime.

7. The OCC Lacks the Authority to Enact Proposed 12 C.F.R. §§ 7.4008 and 7.4009 Regarding General Lending and Banking Practices

The OCC also proposes to preempt a wide range of state laws related to the business of lending not secured by real estate and to the remainder of the business of national banks. When viewed together, the suggested regulations purport to preempt the entire field of state law as to each and every aspect of a bank's business, unless the OCC says otherwise.⁷⁷ This can fairly be called "preempt the world" regulations.

⁷⁴ These states include: California, Colorado, Connecticut, Iowa, Kansas, Maryland, Minnesota, New Jersey, New York, North Dakota, Tennessee, Utah, Washington, and Wisconsin.

⁷⁵ Proposed 12 C.F.R. § 34.4(a)(12).

⁷⁶ 12 U.S.C. § 85.

⁷⁷ Compare proposed 12 C.F.R. § 34.4 (real estate lending) with §§ 7.4007(deposit-taking), 7.4008(general lending), 7.4009(all other bank activities).

These regulations fly in the face of the conflict analysis applied consistently by the courts to the business of national banks, as discussed above. Combined with the OCC's definition of the scope of its "visitorial" power discussed in an earlier proposed regulation,⁷⁸ the OCC is effectively saying: banks have complete preemption rights in relation to state law, unless we say otherwise and only we have the right to say otherwise and to inspect and enforce any state laws we say might apply. In combination, these regulations eliminate the dual banking system in place for over one hundred and forty years. The OCC is attempting to do through regulation what Congress has not condoned.

In addition to this general concern, the preemption of several items on this list is problematic. For this reason, we incorporate here our comments regarding proposed § 34.4 as they relate to the preemption of state laws dealing with "reports by creditors,"⁷⁹ insurance,⁸⁰ access to and use of credit reports,⁸¹ state disclosure laws,⁸² and rates of interest.⁸³

Once again, the OCC sets forth eight examples of the types of state laws that are not preempted *if* they only incidentally affect the real estate lending powers of national banks. Noticeably absent from this list are state consumer protection laws which the OCC has agreed apply to national banks. In addition, state repossession, protection from attachment, and enforcement of judgment laws have traditionally applied to banks as well as state statute of frauds, limitations, and procedural rules. These are laws critical to consumers and must be listed.

8. Operating Subsidiaries Are Not Entitled to the Preemption Rights Afforded National Banks

Until 2001, neither Congress nor the OCC had conferred national bank preemption rights upon national bank subsidiaries. However, in 2001, the OCC promulgated a very short and seemingly innocuous regulation: "Unless otherwise provided by Federal law or OCC regulation, State laws apply to national bank operating subsidiaries to the same extent that those laws apply to the parent national bank."⁸⁴ The OCC justified its action by arguing that the Gramm-Leach-Bliley Act (GBLA)⁸⁵ permits national banks to own subsidiaries that solely engage in activities that national banks are

⁷⁸ See 68 Fed. Reg. 6363 (Feb. 7, 2003).

⁷⁹ Proposed 12 C.F.R. § 7.4008(c)(i).

⁸⁰ Proposed 12 C.F.R. § 7.4008(c)(ii).

⁸¹ Proposed 12 C.F.R. § 7.4008(c)(vii).

⁸² Proposed 12 C.F.R. § 7.4008(c)(viii).

⁸³ Proposed 12 C.F.R. § 7.4008(c)(x).

⁸⁴ 12 C.F.R. § 7.4006; 66 Fed. Reg. 34784, 34788-89 (July 2, 2001).

⁸⁵ Pub. L. No. 106-102, § 121, codified at 12 U.S.C. § 24a(g)(3). For a discussion of this Act, see § 8.4.1.5.2, infra. The OCC, by regulation, permitted national banks to own operating subsidiaries prior to the enactment of Gramm-Leach-Bliley. See 12 C.F.R. § 5.34. There is no explicit authority in the National Bank Act. However, the OCC relied upon 12 U.S.C. § 24 (seventh), which grants to national banks "incidental" powers necessary to carry on the business of banking.

permitted to engage in directly and are conducted subject to the same terms and conditions that govern the conduct of such activities by national banks.⁸⁶

What is clear is that the authorization in GBLA to own subsidiaries was confined to "financial" subsidiaries. A financial subsidiary can engage only in activities that are financial in nature or incidental to a financial activity and activities that are permitted for national banks to engage in directly (subject to the same terms and conditions that govern the conduct of the activities by a national bank).⁸⁷ This provision prohibits financial subsidiaries from providing certain insurance and annuity products or engaging in real estate development, real estate investment or other activities, unless otherwise permitted by law.⁸⁸

However, the recognition of "financial subsidiaries" in the GLBA does not provide authority for the OCC to extend preemption of state law to operating subsidiaries. The GLBA was enacted to increase competition in the financial services industry by "providing a prudential framework for the affiliation of banks, securities firms, insurance companies, and other financial service providers. . . ."⁸⁹ National banks are provided the authority under the GLBA to engage in certain activities through "financial subsidiaries," subject to certain conditions.⁹⁰ However, the GLBA expressly prohibits preemption of state law for these subsidiaries in most circumstances.⁹¹

Furthermore, searching for express authority in the National Bank Act for the creation of operating subsidiaries is a fruitless exercise. The NBA does not mention, in any way, operating subsidiaries of national banks as state-chartered corporations affiliated with a national bank. Standard rules of statutory construction also dictate that the absence of this authority means something: "courts must presume that the legislature says in a statute what it means and means in a statute what it says there."⁹² The failure of the Congress to define the term "operating subsidiary" or include operating subsidiaries in the statutory scheme covering national banks must be presumed to be intentional in the absence of language to the contrary. Because there is nothing in the NBA regarding operating subsidiaries, there can be no express authority for the OCC to promulgate regulations allegedly governing them to the exclusion of the laws of the state in which they were chartered.

⁸⁶ 66 Fed. Reg. at 34788. The OCC has recently decided to rely upon the incidental powers provision in the NBA, 12 U.S.C. § 24(Seventh). See the discussion of the OCC position in *Wells Fargo Bank, N.A. v. Boutris*, 2003 WL 1220131 (E.D. Cal. March 10, 2003)(at the preliminary injunction stage, the court found that the operating subsidiary of Wells Fargo Bank will likely succeed on its argument that it is not subject to state enforcement actions).

⁸⁷ 12 U.S.C. § 24a(a)(2)(A).

⁸⁸ 12 U.S.C. § 24a(a)(2)(B).

⁸⁹ S. Rep. No. 44, 106th Cong., 1st Sess. (1999) at 2.

⁹⁰ 12 U.S.C. § 24a(a)(1) and (a)(2).

⁹¹ 15 U.S.C. § 6701(d)(4).

⁹² *Connecticut Nat'l Bank v. Germain*, 503 U.S. 249, 253-254 (1992).

It is clear that Congress has not extended national bank preemption to financial subsidiaries.⁹³ Logically, the OCC also does not have the authority to extend preemption privileges to operating subsidiaries. Even if operating subsidiaries – as distinguished from financial subsidiaries -- were separately authorized by statute, it does not necessarily follow that operating subsidiaries should enjoy preemption from state laws. Allowing banks to own operating subsidiaries and granting those non-bank entities the expansive rights of preemption and the related right of exportation are two completely different matters.

Finally, even – *arguendo* – if statutory authority for operating subsidiaries to enjoy preemption from state laws were to be found, as a policy matter the OCC should determine separately the extent to which preemption of state consumer protection laws is appropriate. While national banks are generally less likely to be directly engaged in predatory mortgage lending activities, the same can not be said for the subsidiaries of national banks. Consumer advocates believe that many of these non-bank entities are heavily involved in some of the most pernicious practices. Until the OCC can be completely assured that subsidiaries are not engaging directly or indirectly in predatory practices, the extension of preemption right is inappropriate.

VI. Conclusion

We believe that neither the National Bank Act nor other banking laws support the extreme position that the OCC is taking in its proposed regulations. The OCC's action will nullify virtually all of state law as it relates to the activities of national banks and their operating subsidiaries. States will be unable to protect their citizens from predatory loans. The OCC has not taken any meaningful action to clean up the national bank houses. We strongly urge the OCC to withdraw the proposed regulation preempting the application of state laws to the consumer loans made by national banks and the operating subsidiaries.

⁹³ Even if the Comptroller possessed the authority to enact 12 C.F.R. § 7.4006 regarding operating subsidiaries, that provision only applies to “operating subsidiaries.” 12 C.F.R. § 5.34 regarding “operating” subsidiaries by its terms does not apply to “financial” subsidiaries. Financial subsidiaries are governed separately by 12 C.F.R. § 5.39.

Exhibit A – Letter from Lauren Willis of Stanford Law School critiquing the OCC Working Paper

October 6, 2003

By Facsimile Transmission: (202) 874-4448
Comptroller of the Currency
250 E Street, S.W., Public Information Room, Mailstop 1-5
Attention: Docket No. 03-16
Washington, D.C. 20219

Re: OCC Working Paper: Economic Issues in Predatory Lending (July 30, 2003)

To whom it may concern:

Please accept this letter comprising my analysis of the Working Paper issued by the Office of the Comptroller of the Currency, Administrator of National Banks, dated July 30, 2003: “Economic Issues in Predatory Lending” (hereinafter, OCC Paper). That Paper purports to present “a summary and analysis of key statistics and studies on the issue of predatory lending” so as to answer a number of important questions about subprime and predatory home lending. OCC Paper at 1. However, the Paper then proceeds to base crucial parts of its analysis on a few unrepresentative data points and assumptions, rather than representative statistics. Further, the Paper’s analysis of loan price largely neglects what in the subprime and predatory market can be a very significant component of price – upfront charges, fees and “points.” The Paper also analyzes loan risk solely from the lenders’ perspective, asking whether risk is priced appropriately, without accounting for the negative externalities in the form of injuries to neighborhoods and communities caused by loans at high risk of default and foreclosure. By ignoring key elements of home loan price and risk, and by relying on unrepresentative data points and assumptions, the Paper fails to meet the Office of Management and Budget’s Guidelines for Ensuring and Maximizing the Quality, Objectivity, Utility, and Integrity of Information Disseminated by Federal Agencies, published at 67 Fed. Reg. 8,458 (Feb. 22, 2002) (hereinafter, OMB Regulations). The information disseminated in the Paper does not meet the requirement that information be presented in an “accurate, clear, complete, and unbiased manner,” nor the requirement for information presented in financial contexts that “the original and supporting data shall be generated, and the analytic results shall be developed, using sound statistical and research methods.” 67 Fed. Reg. at 8,459. My analysis of these problems with the Paper⁹⁴ is as follows:

Defining Predatory Lending:

⁹⁴ I do not analyze here the paper’s presentation of the various studies that have attempted to analyze the effect of North Carolina’s anti-predatory lending law, as it is my understanding that others more familiar with the North Carolina data will be doing so.

The OCC Paper starts with a concern that predatory lending lacks a precise enough definition for it to be analyzed at all, and intimates, without providing any evidence whatsoever for such a conclusion, that existing studies quantifying some of the costs to society of overpricing of predatory loans are not valid. OCC Paper at 6. I would offer the following definition: predatory home loans are home loans that are overpriced and/or overly risky. Overpriced loans take advantage of the fact that many borrowers do not price shop. They are loans priced significantly higher than others that were available on the market to the borrower, such that if the borrower had engaged in price shopping, the borrower would have saved more by finding the cheaper loan, than the borrower would have expended in tangible search costs. Overly risky loans take advantage of the fact that many borrowers do not understand the full risk of foreclosure posed by the loan, nor do some borrowers consider fully the alternatives that exist to taking the loan. They are loans taken when if the borrower had understood the risk of loss of home posed by the loan, and the existence of alternatives to taking the loan (such as foregoing the loan proceeds, declaring bankruptcy with a homestead exemption, selling the house on the open market instead of losing it at foreclosure, etc.) the borrower would not have taken the loan. Price and risk can be related from the borrower's perspective, in that an overpriced loan can endogenously create risk where the borrower would have been able to afford the payments on a competitively-priced loan, but can not afford the payments on an overpriced loan.

The OCC Paper without citation claims that “economists⁹⁵ typically suggest that judgments as to whether a loan's price is high or abusive in the absence of additional concrete economic analysis of underlying risks, costs and other fundamentals, such as the level of demand for credit, are not a valid basis for defining predatory lending.” *Id.* at 6. But an economist would find perfectly acceptable the above definition of an overpriced loan, one produced in a market where vulnerable borrowers do not price shop even where the benefits of doing so would outweigh tangible costs, and some lenders price discriminate based on borrower vulnerability. The Paper largely ignores the problem of risk of loss of the home from the borrower and neighborhood perspectives, and therefore fails to even address this aspect of the definition I have set forth above. Without an analysis of the social cost of foreclosure, any cost-benefit analysis of predatory lending and anti-predatory lending legislation is neither accurate nor complete, in violation of the OMB Regulations.

Overpricing of Predatory Loans:

The OCC Paper asserts that “the empirical data do not support the contention that subprime providers in the aggregate are earning excess profits.” OCC Paper at 4. Instead, the Paper claims “economists generally view the subprime lending area as highly competitive with a strong correlation between price and borrower risk.” *Id.* at 9. The Paper goes on to present data from which it draws the conclusion that subprime loan delinquencies and defaults increase steadily as paper grade declines, and that the pricing

⁹⁵ The paper continually claims that on one side of the predatory lending debate sit “proponents of anti-predatory lending legislation” and on the other side sit “economists.” OCC Paper at 5, 6 & 8. This is both inaccurate and offensive. Many of the analysts who have advocated anti-predatory lending legislation are economists, including economists at Freddie Mac and Fannie Mae, various universities, and policy groups.

structure of the loans is accordingly well-calibrated to account for the expected risk to the lender of loss of unpaid principal posed by each grade of loan. *Id.* at 8-10. The Paper uses the same data to make the extremely tenuous claim that because the price differentials between grades of subprime loans are roughly similar to the price differentials found between grades of corporate bonds, this data is evidence of a well-functioning competitive market for subprime loans. *Id.* at 11.

These assertions are all based on the pricing and loss rate data from a single subprime lender, Option One Mortgage Corporation. *Id.* at 8 (Table 1). The interest rates used in the analysis are for 30-year fixed rate loans from rate sheets in effect during a single week, the week of September 6, 2002, for two of Option One's loan programs in Colorado and Utah only, and the loss rates used in the analysis are Option One's reported loss rates for its existing portfolio of subprime loans in 2002. *Id.* There is no evidence that the practices of Option One as reflected in the rates for 30-year fixed rate loans on its rate sheets for one week in September, 2002 in two programs offered in Colorado and Utah, or the loss rates experienced by Option One on its portfolio in 2002, are particularly representative of the entire subprime industry, including predatory players in that industry. To the contrary, Option One has not been widely charged with predatory practices, and Colorado and Utah are not states where predatory lending has come to the fore as a particularly big problem. Moreover, predatory loans are frequently not 30-year fixed rate loans, but rather have short-term balloons, graduated increasing or variable interest rates, and other more complicated structures than 30-year fixed rate loans. There is simply no basis for making conclusions about the competitiveness of pricing in the entire subprime industry based on these totally unrepresentative data points, data points that were not generated using "sound statistical research methods" as required by the OMB Regulations.

Furthermore, the pricing analysis in the OCC Paper relies on unsupportable assumptions about the price of broker fees. In attempting to correlate borrower risk and loan price, the Paper assumes that the wholesale prices on Option One's September 6, 2002 rate sheets can be adjusted to retail prices by adding 50 basis points as average broker compensation. *Id.* No evidence supports an average broker fee of 50 basis points, and the Paper offers none. To the contrary, although no nation-wide randomly-sampled data are available, the only empirical studies of broker compensation show that brokers make between 186 and 230 basis points per loan.⁹⁶ This compensation is an amalgam of broker fees disclosed to borrowers as broker or origination fees, other fees paid to the broker such as processing or application fees, and fees extracted through yield spread premiums – upselling borrowers into higher interest rates than the borrower would qualify for from the lender, in exchange for which the lender gives the broker a kickback.

⁹⁶ See Jack Guttentag, *Another View of Predatory Lending*, Wharton Financial Institutions Center Working Paper #01-23-B at 10 & Table 2 (Aug. 2001) (based on study of 800 loans made between December 2000 and January 2001, reporting mortgage broker profit ranging from 1.86% to 2.30% of loan amount); Howell E. Jackson & Jeremy Berry, *Kickbacks or Compensation: The Case of Yield Spread Premiums* at 71 & 91 Fig. 13 (unpublished manuscript, 2002, reflecting data collected for expert report submitted July 9, 2001 in *Glover v. Standard Federal Bank*, Civ. Action No. 97-2068 (DWF/SRN) (D. Minn.)) (based on study of 2,947 loans sampled in litigation against a small number of lenders accused of predatory overpricing practices, finding average total broker compensation of about 2.25% of loan amount).

Moreover, even if the Paper had used a realistic average estimate of broker fees, the problem of predatory lending is not the average pricing of subprime loans, but rather the overpricing of predatory loans agreed to by vulnerable borrowers. The only empirical evidence available on this point indicates that broker compensation varies significantly, not according to how much work the broker puts into securing the loan for the borrower, but rather according to how vulnerable the broker thinks the borrower is,⁹⁷ and that African-Americans and Hispanics on average pay significantly more in broker compensation than do white borrowers.⁹⁸ The 50 basis point assumption again is data developed without the use of sound research methods.

Spurious Explanations of Loan Pricing Differentials:

A similar problem infects the Paper's later claim that the spread between interest rates "includ[ing] average points and fees" on prime 80% loan to value ratio (LTV) mortgages and subprime 80% LTVs where the borrower has a 680 FICO score can be explained entirely by differences in higher risk and cost of the subprime loan. OCC Paper at 13. Without citation to any source, the Paper asserts that the interest rate plus average points and fees on a prime mortgage of this type in September 2002 was 6.14%, and the interest rate plus average points and fees on a subprime loan of this type was 8.1%. *Id.* Without citation, there is no way to independently verify the accuracy of this data, in violation of the OMB Regulations. But more importantly, predatory loans do not come with "average" points and fees; they have higher points and fees not attributable to risk and cost. Therefore, whether the price differential between an average prime and average subprime loan can be explained by price and risk has little bearing on whether predatory lending is a problem.

Further, the reasoning of the Paper here is that because it is more costly to service loans to borrowers with blemished credit records than prime borrowers, *id.* at 12, 40 basis points of the price difference between the 680 FICO average subprime borrower and the comparable prime borrower is explained by servicing cost. But a 680 FICO score would indicate that this subprime borrower is not any more costly to service than the prime borrower, so the 40 basis points difference seems pulled from thin air, without any real underlying support.⁹⁹ Similarly, the Paper claims that because the different grades of subprime loans are priced at about 111 basis points between each grade, 111 basis points of the difference between the 680 FICO subprime borrower and the prime borrower is explained by risk. *Id.* Again, there is simply no sound statistical or research methodology being followed to come up with these non sequiturs.

Competition in the Secondary Market Does Not Ensure Competitive Pricing for Borrowers: Next, the OCC Paper sets forth the relationship between coupon rates and

⁹⁷ Guttentag at 8 ("According to the brokers, [a] major determinant of profit per loan is the sophistication of the borrower relative to the sales skills of the loan officer."); Jackson & Berry at 81-85.

⁹⁸ Jackson & Berry at 125-128.

⁹⁹ The only data cited by the Paper for this point is that servicers charge 25 more basis points to service subprime loans than prime loans, a number that the Paper inflates to 40 basis points based on a statement made by a failed auto lender that auto loans cost 75 more basis points to service if they are subprime than if they are prime. OCC Paper at 13. This is slim evidence, and certainly not data generated using "sound statistical methods."

serious delinquency rates, based on limited Mortgage Information Corporation (MIC) subprime data, and asserts that because delinquency rates generally rise as coupon rates rise, the price of subprime loans reflects their risk. OCC Paper at 10 (Chart 3). The first problem with this assertion is that the data upon which it is based is not representative of the entire subprime market – MIC data for subprime lenders includes only 27 lenders, and does not include any loans from ten states, several of which are particularly known for having difficulties with predatory lending.¹⁰⁰ The more fundamental problem with the assertion is that coupon rates do not reflect the price paid by the borrower for the loan. The coupon rate is the rate paid on the paper in the secondary mortgage backed securities (MBS) market, generally the note interest rate, not the price paid by the borrower. That the coupon rate in the MBS market would be appropriately priced for the risk of default, and that a very competitive subprime MBS market exists, is not surprising. But the competitive pricing structure of the MBS market need not be passed on to subprime borrowers, and abundant evidence exists that it is not passed on. Instead, borrowers pay a wide range of upfront broker fees, origination charges, and “points” that do not buy down the note interest rate¹⁰¹ – fees extracted at the retail level by the broker and originating lender. For predatory loans, these fees reflect not only origination costs, but also borrower vulnerability. A similar phenomenon exists in the stock market and brokerage commissions; although stocks are sold on the stock market at competitive prices, stock brokers can charge commissions to clients that are not competitively set, but instead are based on the broker’s sense as to how vulnerable the investor is to overpricing of brokerage services.¹⁰² The Paper’s reasoning here once again lacks a sound basis.

Prepayment Risk:

The OCC Paper briefly argues, without citation to evidence, that higher prepayment risk in the subprime market leads to higher prices to cover that risk. OCC Paper at 11. No explanation is given to explain why prepayment penalties alone would not be sufficient to cover prepayment risk. Further, the unstated assumption is that prepayments are always costly for the lender, when in fact, subprime loans prepay even when interest rates are rising, when lenders should be happy to have their funds freed to reinvest in a higher-rate environment, provided transaction costs are not too high. Further, when it is the same lender or related entity that is doing the refinancing, as is frequently the case for predatory loans that are repeatedly “flipped” by the same lender, that lender loses nothing from prepayment, and is able to charge a host of new origination fees at the refinancing, leaving no justification for the imposition of a prepayment penalty.

¹⁰⁰ Fred Phillips-Patrick, Eric Hirschhorn, Jonathan Jones & John LaRocca, *What About Subprime Mortgages?*, 4 Mortgage Market Trends 5-6 (OTS Research & Analysis, June 2002).

¹⁰¹ Up-front fees (“points”) that do buy down the note rate would have to be passed on to the secondary market to sell the loan in such a price competitive environment. But predatory loans often include up-front charges for “points” that do not buy down the interest rate. *See* Washington State Department of Financial Institutions, *Expanded Report of Examination for Household Finance Corporation III* 15 (April 30, 2002) (demonstrating that lender charged 7.25% in “points” without lowering, and in some cases even while increasing, the borrower’s note rate).

¹⁰² *See* Jackson & Berry at 64-65.

The Paper states that subprime loans prepay when borrower creditworthiness improves, *id.*, without noting that where the subprime loan was predatorily overpriced, the borrower's credit need not improve to be qualified for a lower interest rate loan – that is, where the borrower was qualified for a prime or lower rate subprime loan at the time she took the loan, her creditworthiness need not improve for her to chose to prepay and refinance at the lower rate for which she qualified all along.¹⁰³ Rather than charging a higher interest rate to cover for the risk that she might prepay, the lender should have charged a lower rate so the borrower would not be tempted to prepay in order to obtain that lower rate. A prepayment penalty in such a scenario could prevent a borrower from obtaining a competitively-priced loan, contrary to free market principles.

Further, the Paper attempts to explain prepayment penalties not as compensation for lost interest income stream, but rather as compensation for origination fees that subprime lenders “don’t collect ... upfront but build ... into the loan amount.” *Id.* at 15 n. §§. This cryptic and slightly misleading¹⁰⁴ reference is to yield spread premiums, brokers fees that lenders pay upfront and then collect from the borrower over time in the form of a higher interest rate. But lenders could refuse to pay yield spread premiums, or could only pay these premiums after confirmation that borrowers actually agreed to the full broker's fee and chose to have the fee paid through the premiums instead of financing them in the principal of the loan. Where the borrower chose to finance the fees rather than paying for them through a yield spread premium, this would obviate the necessity for prepayment penalties, because the lender would collect the financed origination fee as part of the principal balance paid off at refinancing. It would also result in brokers' fees that would in all likelihood become more competitively priced because borrowers would discover the price they are paying for broker services and could use this information to shop among brokers.

Even a Loan that Is “Correctly-Priced” for Risk Can Be Predatory:

The OCC Paper makes the assumption that so long as home loans are priced according to risk, cost, and supply and demand factors, the loans cannot be predatory or otherwise problematic. The Paper states: “there remains much debate about whether the higher rates and fees charged on many subprime loans are predatory or simply reflect higher borrower risk, servicing costs, or demand factors related to the macroeconomy.” OCC Paper at 26. But a loan can be priced strictly according to these factors, and yet still be overly-risky, when viewed in comparison to the alternatives the borrower would have chosen if she had understood the true risk presented by the loan. Where a borrower would have been better off by foregoing the loan proceeds, defaulting on unsecured debt

¹⁰³ It is estimated that between ten and fifty percent of borrowers with subprime loans were qualified for lower prime interest rate loans, based on their credit history and loan profile. *See* Business Wire, Fannie Mae Has Played Critical Role in Expansion of Homeownership (March 2, 2000) (50% estimate); Freddie Mac, *Automated Underwriting: Making Mortgage Lending Simpler and Fairer for America's Families*, 5-6 & Ch. 5 (Sep 1996) at www.freddiemac.com/corporate/reports/moseley/chap5.htm (10 to 35% estimate); *Half of Subprime Loans Categorized as “A” Quality*, INSIDE B & C LENDING (June 10, 1996) (50% estimate).

¹⁰⁴ The origination fees are not built into the loan amount, they are built into higher interest rates. If the fees were merely financed into the loan amount, the lender would not lose them at a refinancing, because they would be paid off as part of the principal balance by the new lender.

rather than paying it off from home loan proceeds, selling the house on the open market, or declaring bankruptcy with a homestead exemption, rather than taking a predatory loan, it is inefficient, in the sense of not putting resources to their highest and best use, for the borrower to take the predatory loan. But that borrowers would agree to loans that are overly-risky is not surprising, given that no lender tells the borrower the actual risk of foreclosure the borrower is going to face with this loan, according to the risk models the lender used, at least initially, prior to any excess price the broker or loan officer discovered he could extract, to price the loan. Further, the costs of very risky loans are borne, ultimately, not only by the borrower and the lender, but also by the borrower's family/household and by the neighborhoods and communities that are affected by the instability caused by foreclosure. The pricing of risky loans cannot internalize to either the lender or the borrower the negative externalities caused by high risk loans. Because predatory loans are concentrated in minority and low-to-moderate income communities, the impact of foreclosures and neighborhood instability are borne disproportionately by these communities. The failure of the OCC Paper to grapple with these costs of predatory lending renders its analysis neither accurate nor complete.

National Banks and Predatory Lending:

The OCC Paper claims that federally-regulated banks and their direct subsidiaries are not involved in predatory lending based on statistics as to what proportion of lenders classified as primarily subprime are national banks or their direct subsidiaries, and what proportion of national banks and their direct subsidiaries are classified as primarily subprime lenders. OCC Paper at 7. The relevant statistic here would be not the number of lenders, but the number of loans. That is, the relevant question is what proportion of subprime loans are made or held by national banks or their direct or indirect affiliates, either directly or through brokers or purchases of subprime mortgage-backed securities. Although the Paper characterizes bank purchases of securities backed by predatory loans or originations of predatory loans through brokers as “inadvertent[]” and “unintentional[]”, *id.*, these purchases are the result of a deliberate decision by the bank as to the degree of due diligence it exercises in purchasing and originating the loans. Moreover, bank practices of paying brokers yield spread premiums to sell borrowers higher-priced loans than the borrowers' risk and cost profile would garner, and service release premiums based on the size of the loan, encourage predatory practices of upselling borrowers to over-priced loans and loans that are larger, and thus more risky, than what the borrower needs. Further, the numerous lawsuits brought against national banks, their operating subsidiaries and their affiliates by the federal government for predatory practices, including the case brought by the Federal Trade Commission against The Associates and Citifinancial and the cases brought by the Department of Justice against Long Beach Mortgage Company, Huntington Mortgage Company, Fleet Mortgage Corporation, and First National Bank of Vicksburg, are striking evidence that banks, their operating subsidiaries and their affiliates have engaged in predatory lending.

Conclusion:

When one goes to the underlying sources cited by the OCC Paper, one sees a very different picture painted of the empirical information we have about subprime lending, including predatory lending, than the picture that emerges from the OCC Paper. The

Paper draws its empirical data¹⁰⁵ largely from two sources: a single Freddie Mac paper¹⁰⁶ and a single Office of Thrift Supervision (OTS) paper.¹⁰⁷ Those sources contain numerous caveats about the data not being representative; for example, the OTS paper relies on data from the Mortgage Information Corporation (MIC), but cautions that the MIC data for subprime lenders includes only 27 lenders, and does not include any loans from ten states, several of which are particularly known for having difficulties with predatory lending.¹⁰⁸ Further, those sources contain some discussion of parts of the data that indicate a potential problem with predatory overpricing of some loans. For example, the OTS paper notes that about 16 percent of the A-minus borrowers in the MIC data set had credit scores over 680, scores correlated with prime credit risk, raising the possibility that these were predatory loans, high cost subprime loans given to prime risk borrowers. But the caveats about the lack of representativeness of the data and the discussion of the predatory pricing implications of the data appear nowhere in the OCC Paper. One cannot help but be concerned about the bias being displayed here, a bias that consistently understates the problem of predatory lending.¹⁰⁹

Please contact me if I can be of any further assistance in this matter.

Very truly yours,

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¹⁰⁵ Apart from the data regarding the effect of anti-predatory lending laws in North Carolina, not addressed here.

¹⁰⁶ Amy Crews Cutts & Robert Van Order, *On the Economics of Subprime Lending* (Freddie Mac, March 2003).

¹⁰⁷ Fred Phillips-Patrick, Eric Hirschhorn, Jonathan Jones & John LaRocca, *What About Subprime Mortgages?*, 4 Mortgage Market Trends (OTS Research & Analysis, June 2002).

¹⁰⁸ *Id.* at 5-6.

¹⁰⁹ Similarly, the OCC Paper tries to refute Freddie Mac's analysis of inefficiency in pricing in the subprime market by arguing that the subprime loans Freddie examined are possibly riskier, and thus arguably should be higher priced, than the Freddie study allows. OCC Paper at 15 (citing Howard Lax, Michael Manti, Paul Raca & Peter Zorn, *Subprime Lending: An Investigation of Economic Efficiency* 17-18 (Freddie Mac, Dec. 2000)). Nowhere does the Paper note that the prices examined by Freddie are note interest rates, not including upfront brokers' fees, origination charges, and "points", all of which would most likely make the pricing differentials between prime and subprime loans substantially greater, and less explainable by differences in risk and cost, than the price differentials assumed by the study. That the OCC Paper would point out possible small understatements of the risk differential between the prime and subprime loans examined, without noting the likely large understatement of the price differential between the prime and subprime loans examined, displays a distinct bias.