



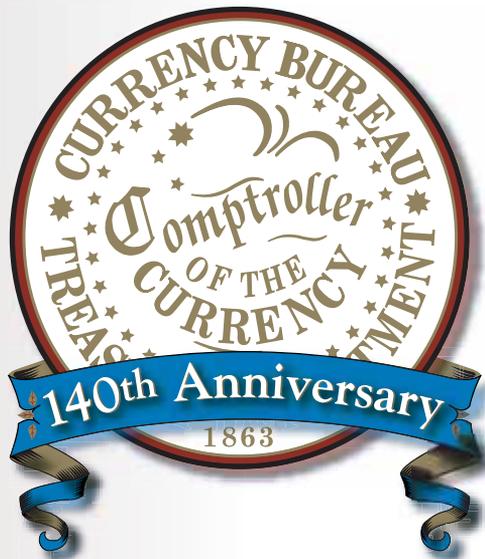
---

Comptroller of the Currency  
Administrator of National Banks

---

2003

# SIGNIFICANT LEGAL, LICENSING AND COMMUNITY DEVELOPMENT PRECEDENTS



**2003**

**Significant Legal, Licensing and  
Community Development Precedents  
for National Banks**

**Office of the Comptroller of the Currency**

**March 2004**

## Contents

<b>Activities</b>	<b>3 – 8</b>
<b><i>General Banking Activities</i></b>	<b>3 – 6</b>
<i>Branching</i>	3
<i>Capital</i>	3 – 4
<i>Consulting and Financial Advice</i>	4
<i>Corporate Governance</i>	5
<i>Finder Activities</i>	5
<i>Lending</i>	5 – 6
<i>Other Activities</i>	6
<b><i>Fiduciary Activities</i></b>	<b>7</b>
<b><i>Insurance and Annuities Activities</i></b>	<b>7</b>
<b><i>Securities Activities</i></b>	<b>7 – 8</b>
<i>Derivatives</i>	7
<i>Tying</i>	7 – 8
<b><i>Technology and Electronic Activities</i></b>	<b>8</b>
<i>Electronic Commerce</i>	8
<i>Software Development, Production, Licensing</i>	8
<b>Compliance</b>	<b>8</b>
<b>Enforcement Actions</b>	<b>9 – 14</b>
<i>General</i>	9
<i>Anti-Money Laundering</i>	9 – 10
<i>Consumer Protection</i>	10 – 12
<i>Early Intervention for Problem Banks</i>	12 – 13
<i>Identity Theft, Computer Intrusion, Privacy</i>	14
<b>International</b>	<b>14</b>
<b>Investments</b>	<b>15 – 17</b>
<b>Preemption</b>	<b>17 – 19</b>
<b>Regulations</b>	<b>19 – 21</b>

## **Significant Legal, Licensing and Community Development Precedents for National Banks**

### *Activities*

#### *General Banking Activities*

##### *Branching*

- *Drop Boxes.* Placement of United Parcel Service drop boxes at nonbranch offices of a bank does not make those offices branches within the meaning of 12 U.S.C. § 36 because the boxes are owned by an independent third party, have no bank identification, and may be used by the general public for nonbanking transactions. Interpretive Letter No. 980 (December 24, 2003).
- *Historic Preservation.* The OCC conditioned the approval of the establishment of a branch of a national bank on the bank's execution of a Memorandum of Agreement with the State, the State Historic Preservation Officer, and the OCC. The Agreement is to facilitate the bank's efforts in preserving the historic significance of the proposed branch building. Conditional Approval No. 601 (July 23, 2003).
- *Underserved Communities.* A national bank may establish branches for the sole purpose of serving an underserved community, and may acquire a non-controlling investment a company that specializes in providing these services. Conditional Approval No. 612 (November 21, 2003).
- *Use of Trade Names.* Based on representations as to steps that would be taken to avoid customer confusion, bank's operation of branches at Wal-Mart stores under a trade name was found to be consistent with Interagency Statement on Branch Names. Interpretive Letter No. 977 (October 24, 2003).

##### *Capital*

- *Government Sponsored Entities (GSE) Preferred Stock.* Pursuant to the OCC's risk-based capital guidelines preferred stock issued by a GSE fall within the meaning of the term "security" and qualify for a 20 percent risk weight as a security issued by a GSE. Interpretive Letter, publication pending (March 17, 2003).

- *Merchant Processing Intangibles (MPIs)*. OCC determines that MPIs generally fail to satisfy the separability, valuation, and marketability criteria, and therefore, the list of qualifying intangible assets should not be expanded to include MPIs. Consequently, MPIs must be deducted from Tier 1 capital and assets in calculating the bank's risk-based capital ratio. Interpretive Letter pending publication (October 17, 2003).
- *Multifamily Residential Mortgage Property Annual Net Operating Income Requirements*. The actual operating income of a multifamily residential property must be used by the bank in order to determine whether the a loan secured by a first mortgage on a multifamily residential property would satisfy the annual net operating income requirements, and therefore, qualify for the 50 percent risk weight under the risk-based capital guidelines. An operating statement prepared by a qualified asset manager (not based on the actual operating income of the property) would not satisfy the annual net operating income requirements. Interpretive Letter publication pending (August 18, 2003).
- *Second Liens in Structured Mortgage Transactions*. Clarifies the joint final rule on the "Capital Treatment of Recourse, Direct Credit Substitutes, and Residual Interests in Asset Securitizations," 66 Fed. Reg. 59621 (November 29, 2001), and concludes that second mortgages liens will not, in most instances, constitute recourse because they generally do not function as credit enhancements. Interpretive Letter pending publication (March 17, 2003).
- *Synthetic Securitizations of Residential Mortgage Loans*. Determination by the OCC and the Federal Reserve Board staff that the principles established in Joint Agency Guidance on Synthetic Collateralized Loan Obligations (November 15, 1999) and a final rule, "Capital Treatment of Recourse, Direct Credit Substitutes, and Residual Interests in Asset Securitizations," 66 Fed. Reg. 59621 (November 29, 2001) may be applied to a synthetic securitization. The Agencies modified some of the risk management, measurement, and disclosure requirements established in their 1999 Guidance. Interpretive Letter; publication pending (July 28, 2003).
- *Tax Refund Anticipation Loans*. Tax refund anticipation loans should be risk-weighted at 100%, as they are not directly or indirectly guaranteed by the U.S. Government or its agencies and are, therefore, ineligible to receive a lower risk-weight. Interpretive Letter No. 959 (February 2, 2003).

#### *Consulting and Financial Advice*

- *Investment Advisor May Hold Special Equity Interests*. A national bank operating subsidiary may receive compensation for management and performance fees in the form of a special limited interest profit allocation in the private investment funds for which it serves as investment manager and advisor. Conditional Approval No. 578 (February 27, 2003).

### *Corporate Governance*

- *Reduction of Par Value.* A national bank may reduce the par value of its shares to \$0.01 per share with an offsetting increase to the bank's capital surplus. The reduction in par value may reduce the bank's state franchise taxes. Interpretive Letter No. 963 (April 14, 2003).
- *Reverse Stock Split.* Consistent with 12 CFR 7.2000(b) and 7.2023, a national bank in Mississippi may elect the corporate governance provisions of Mississippi law and complete a reverse stock split with those provisions. Conditional Approval No. 562 (December 9, 2002).
- *Termination of National Bank Activities.* A national bank may terminate its activities, and cease operations through a series of transactions including those granted under the authority provided under 12 U.S.C. § 215a-3. The bank ceased its deposit-taking activities, caused FDIC to cancel its status as an insured depository institution, and an affiliated bank acquired its remaining assets through a § 215a-3 merger. Corporate Decision No. 2003-12 (November 26, 2003).

### *Finder Activities*

- *Sale and Support of Credit Card Incentive Plans.* A national bank operating subsidiary may sell access to its existing credit card promotional reward points program to unaffiliated third party merchants. The merchants will purchase an inventory of the program's reward points and award them to their own customers, employees or other parties. The points will be redeemed from a merchandise/services catalog administered by the national bank operating subsidiary. Corporate Decision No. 2003-10 (June 27, 2003).

### *Lending*

- *Exportation of Interest Rates.* Twelve U.S.C. § 85, including "most favored lender" provision, applies to operating subsidiaries in the same manner and to the same extent that it applies to the parent national bank. Interpretive Letters No. 968 (February 12, 2003) and 974 (July 21, 2003).
- *Lending Limit for Loans to Leasing Companies.* Letter concludes that the leasing exception at 12 CFR 32.3(c)(10) can apply when the proceeds of the loan to the leasing company are not used directly to purchase the assets to be leased but rather are used to reimburse the leasing company for the past purchase of such assets. Interpretive Letter No. 955 (1/31/2003).
- *Lending Limit for Loans to Related Entities.* Letter addresses the application of the various loan combination/attribution rules at 12 CFR 32.5 to loans to several related entities. The letter also addresses the issue of how to treat the gross income from a subchapter S

corporation that is reported as part of the shareholder's adjusted gross income on his or her federal tax return in determining substantial financial interdependence for the purpose of 12 CFR 32.5(c)(2). Interpretive Letter No.951 (1/17/2002).

- *Same Source of Repayment.* On the specific facts presented, the same source of repayment test in 12 CFR § 32.5(c)(1) does not result in the combination of loans to members of The Lower Sioux Indian Community with loans to other members or with a loan to the Community, itself. Interpretive Letter No. 979 (December 18, 2003).
- *Share of Profits as Part of Interest.* National bank may: (1) take a share of borrower's profits as part of interest on loans, 12 CFR § 7.1006; (2) negotiate percentage of profits bank will take; and (3) compensate borrower for originating loans by providing borrower with office space and paying borrower's expenses, 12 CFR § 7.1004(a). Interpretive Letter No. 956 (January 31, 2003).

#### *Other Activities*

- *Coin and Bullion.* A national bank may dispose of coins discovered in its vaults at fair market value, pursuant to 12 U.S.C. § 24(Seventh) and OCC Banking Circular 58 (Rev)., even though that may exceed the value of the metallic content or the face value. Since coins were acquired in the course of normal banking operations, disposal at fair market value does not constitute impermissible speculation. Interpretive Letter No. 975 (October 14, 2003).
- *Employee Relocation Services.* Letter provides that an operating subsidiary of a national bank may acquire, for a short period of time and subject to conditions requiring retransfer, title to the relocating employees' residential real estate as incidental to the package of relocation services offered by the subsidiary. Interpretive Letter 966 (May 12, 2003).
- *Indicia of Ownership of Real Property.* National bank operating subsidiary may acquire and hold certain indicia of ownership of real estate when incidental to the package of relocation services offered by that subsidiary. There are several restrictions and conditions: the subsidiary must use a nominee to hold legal title; the subsidiary may not use or enjoy the benefit of the property; the subsidiary may not manage the property; and the subsidiary must dispose of the indicia within 90 days. Interpretive Letter No. 966 (May 12, 2003).
- *Messenger Service.* A national bank may operate a messenger service that will provide pick up and delivery of cash, checks, and other financial items for non-financial institution businesses having no deposit relationship with the bank. Items will be transported between facilities of such businesses, and between such businesses and their financial institutions. Corporate Decision No. 2003-9 (June 25, 2003).

### ***Fiduciary Activities***

- *Self-deposit in Short-term Investment Fund.* A national bank may pool individual fiduciary accounts awaiting investment or distribution and self-deposit them in a short-term investment fund. Assuming applicable law in states in which the bank does business and plans to self-deposit does not prohibit such deposits, 12 CFR § 9.10(b) provides the applicable authority required by 12 CFR § 9.12 for the bank to self-deposit such funds or to deposit them with affiliates. Interpretive Letter No. 969 (April 28, 2003).

### ***Insurance and Annuities Activities***

- *Disclosure for Renewals of Insurance Policies.* Section 305 of the Gramm-Leach-Bliley Act and implementing regulations do not mandate that banks provide disclosures for renewals of insurance policies sold prior to October 1, 2001. Interpretive Letter No. 960 (February 28, 2003).
- *Insurance Information Sharing Agreements.* The OCC entered into insurance information sharing agreements with insurance regulators of nine additional states in 2003. As of the end of 2003, only two states (Massachusetts and Rhode Island) and Puerto Rico do not have such agreements with the OCC.
- *Risk Management Activities.* Risk management activities are part of an insurance agency's activities. A national bank is not required to file a new financial subsidiary notice with the OCC if the bank's existing insurance agency financial subsidiaries provide risk management services as part of their insurance agency activities. Interpretive Letter No. 967 (June 6, 2003).

### ***Securities Activities***

#### *Derivatives*

- *Electricity Derivatives.* A national bank may expand its financial intermediation business to include customer-driven, electricity derivative transactions that involve transitory title transfers as an activity incidental to banking, provided the bank has established, to the satisfaction of the OCC, an appropriate risk measurement and management process. Interpretive Letter No. 962 (April 21, 2003).

#### *Tying*

- *Underwriting Services Conditioned on Bank's Letter of Credit.* A national bank may condition the offering of its securities underwriting services on the use of the bank's letter of credit to secure the bond issue. The traditional bank product exception of 12 U.S.C. §

1972(1) permits a bank to tie any product or service to a loan, discount, deposit or trust service offered by that bank. The direct advance of funds to a borrower through a letter of credit is well recognized in the industry as a traditional bank product. Interpretive Letter No. 982 (September 29, 2003).

### ***Technology and Electronic Activities***

#### *Electronic Commerce*

- *Collection of Corporate Card Use Data.* A national bank may establish an operating subsidiary that will purchase and then sell or license data processing software that automatically collects information on corporate card use and then merge the data, generate invoices, and approve and make payments. The software also can be licensed to large corporate credit card users. Corporate Decision No. 2003-6 (March 17, 2003).
- *Sponsoring of a Stored Value System.* National bank financial subsidiaries may engage in a Stored Value Payment System. The national bank may sponsor the stored value systems and associated PIN Cards with certain ATM/POS financial networks. The transactions allow for cross border ATM transactions and purchases through deposits in an aggregate account to the benefit of the unbanked public. Conditional Approval No. 568. (December 31, 2002).

#### *Software Development, Production, Licensing*

- *Sale or License of Corporate Credit Card Data Processing Software.* A national bank operating subsidiary may purchase for subsequent sale or license to unaffiliated companies that operate large corporate credit card programs, data processing software designed to monitor corporate credit card usage, merge usage data, generate invoices, and approve/make payments. Corporate Decision No. 2003-6 (March 17, 2003).

### ***Compliance***

- *Abusive Lending Practices.* Two advisory letters address the avoidance of abusive lending both in a bank's loan originations and in loans acquired through loan brokers or in loan purchase transactions. Guidance outlines the credit, legal, and other risks inherent in predatory lending, and provides detailed recommendations for banks to incorporate in their policies, procedures, and practices in order to minimize those risks. AL 2003-02, "Guidelines for National Banks to Guard Against Predatory and Abusive Lending Practices"; AL 2003-3, "Avoiding Predatory and Abusive Lending Practices in Brokered and Purchased Loans."

## ***Enforcement Actions***

### ***General***

- *Use of Formal Agreements.* The OCC is required to find that change in bank control notices are technically complete before taking action to decide the notice. In connection with such, the OCC found a notice technically complete following submission of commitments by a national bank including a commitment to enter into a Formal Agreement with the OCC. The Agreement was meant to ensure various supervisory and safety and soundness measures. Conditional Approval No. 576 (January 31, 2003).

### ***Anti-Money Laundering***

- *Anti-Money Laundering Provisions; Credit Card Bank and Corporate Parent Ordered to Comply.* In connection with accepting cash payments on private-label credit card accounts at a number of retail chain stores, the OCC issued a consent cease and desist order against the corporate parent of the stores and the credit card issuing bank, immediately restricting the ability of any stores owned by the corporation to accept cash payments on the private-label credit card accounts until certain requirements were met. The order additionally required the corporation to implement and ensure the business' adherence to a program of policies and procedures mandating compliance with the Bank Secrecy Act, as amended, and the regulations promulgated hereunder, including provisions pertaining to Currency Transaction Reports, and Suspicious Activity Reports. The OCC issued a similar order to the bank that issued the private-label credit cards. *In the Matter of Saks Incorporated, a Tennessee Corporation*, Enforcement Action No. 2003-40 (April 11, 2003); *In the Matter of National Bank of the Great Lakes, Elmhurst, Illinois*, Enforcement Action No. 2003-38 (April 11, 2003).
- *Federal Branch Official Ordered to Comply with Anti-Money Laundering and OFAC Requirements.* In October 2003, the OCC issued a consent cease and desist order requiring an official of a federal branch of a Shanghai, China bank to take precautions when dealing with multiple bills of lading, and prohibiting him from engaging in any trade settlement transactions involving false documentation or a violation of Office of Foreign Asset Control provisions. *In the Matter of Stephen Lee*, Enforcement Action No. 2003-145 (October 29, 2003).
- *Federal Branch Ordered to Address Compliance with Anti-Money Laundering and OFAC Provisions Ordered.* The OCC entered into a formal agreement with the New York-based federal branch of a Shanghai, China bank. The agreement required the federal branch to address the branch's strategic plan, management, management information systems and credit risk controls. The agreement also required the branch to address compliance with the Bank

Secrecy Act, anti-money laundering and Office of Foreign Asset Control provisions. *In the Matter of Bank of Communications Federal Branch, New York, New York*, Enforcement Action No. 2003-11 (February 4, 2003).

### ***Consumer Protection***

- *Consumer Protection Action; Cooperation by OCC and State Authorities.* In a case referred by state officials, the OCC entered into a formal agreement with a bank to provide significant restitution to aggrieved consumers in three states. The OCC found that the bank issued private label cards that were used to finance purchases of heating and air conditioning units sold door-to-door by a third-party air conditioning firm to Spanish-speaking residents of Arizona, Texas and California. Installation and operation of the units were problematic. The bank, through its third-party vendor provided faulty credit disclosures, and its remediation program was further flawed. *In the Matter of Household Bank (SB), NA, Las Vegas, Nevada*, Enforcement Action No. 2003-17 (March 25, 2003).
- *Consumer Protection Statutes; Troubled Bank Fined and Ordered to Take Corrective Action.* In May and July 2003, the OCC issued consent cease and desist and civil money penalty orders against a Florida-based bank. The consent order terminated a litigated enforcement proceeding that had been initiated by the OCC in 2002. The OCC's 2003 cease and desist order was intended to remedy a number of serious safety and soundness concerns, including violations of the Real Estate Settlement Procedures Act, Federal Trade Commission Act, Fair Credit Reporting Act, Equal Credit Opportunity Act, and Truth in Lending Act. *In the Matter of Guaranty National Bank of Tallahassee, Tallahassee, Florida*, Enforcement Action Nos. 2003-37 (May 2, 2003) and 2003-81 (July 10, 2003).
- *Credit Card Customers; Restitution of Annual and Over the Limit Fees Ordered.* The OCC required a credit card bank to sell, merge or liquidate, pursuant to a consent cease and desist order issued in 2002. Pursuant to this consent order, on December 28, 2002, the bank entered into a contractual agreement whereby the bank knew or should have known that its credit card customers likely would not have use of their cards for an entire year from the date of this December 28 agreement. Yet, the bank continued to charge annual fees on account holders' monthly credit card statements in January and February 2003. These fees caused several bank customers' accounts to exceed their credit limit, thereby generating additional "overlimit fees." The bank then terminated its credit card program on March 7, 2003, making the credit cards useless to consumers. The OCC found these practices in violation of section 5 the Federal Trade Commission Act, and required the bank to refund the pro rata share of the annual fees it charged customers on or after December 28, 2002. Any "overlimit fees" generated by these annual fees were also subject to a full refund. *In the Matter of First Consumers National Bank, Beaverton, Oregon*, Enforcement Action No. 2003-100 (July 31, 2003).

- *FTC Act Section 5 Violation; Consumer Restitution Required.* The OCC determined that a bank's credit card programs violated section 5 of the Federal Trade Commission Act. For example, the bank sent messages that a card carried "no annual fee," but a monthly fee was charged. The OCC ordered the bank to establish a \$6 million reserve to fund restitution payments to consumers. *In the Matter of First National Bank in Brookings, South Dakota*, Enforcement Action No. 2003-1 (January 17, 2003).
- *FTC Act Unfair Practices Case; Restitution Ordered.* In November 2003, the OCC issued a consent cease and desist order in connection with a Texas bank predecessor's predatory tax lien loans to sub-prime borrowers. The loans involved violations of the Truth in Lending Act, Home Ownership Equity Protection Act and Real Estate Settlement and Procedures Act, and unfair and deceptive practices under section 5 of the Federal Trade Commission Act. The unfair and deceptive practices included fees that were charged for services that were never performed, duplicative fees, and in some cases, fees far above the customary fees for the services provided. The OCC ordered the bank to make full restitution to tax lien customers for all fees and interest charged on the loans, and to review a mortgage loan portfolio considered at-risk for similar violations. The OCC ordered the bank to pay additional restitution to any mortgage loan customers who were victims of violations of law or unfair and deceptive practices. The OCC also issued a consent cease and desist order to the partnership that solicited and processed the bank's tax lien loans, requiring the partnership to seek the OCC's non-objection prior to entering into agreements with other national banks. Finally, in connection with the tax lien loans, the OCC issued a consent personal cease and desist order against a former officer of the predecessor bank restricting her future lending activity and assessing a \$10,000 civil money penalty. *In the Matter of Clear Lake National Bank, San Antonio, Texas*, Enforcement Action No. 2003-25 (November 7, 2003); *In the Matter of Sedona Pacific Housing Partnership, DBA Sedona Pacific Properties*, Enforcement Action No. 2003-26 (November 7, 2003); *In the Matter of Nancy Kinder*, Enforcement Action No. 2003-27 (October 20, 2003).
- *Payday Lending Cessation.* In January 2003, the OCC issued two consent orders to national banks in Texas and South Dakota, bringing the banks' respective payday loan programs to an end. By issuing these orders, the OCC terminated the involvement of all national banks making payday loans through third-party vendors. The first order was based on examination findings that the South Dakota bank's oversight of its payday lending operation was weak, ignored deficiencies identified by its auditors, and resulted in significant data integrity issues. The second order was based on the OCC's findings that the Texas bank and its vendor routinely violated federal consumer protection laws and regulations in making payday loans. This order also required the payment of a \$175,000 civil money penalty. The OCC issued another consent cease and desist order against the Texas bank's third-party vendor for violating federal consumer protection laws and regulations when acting as the bank's agent. This order required the vendor to terminate its arrangement with the bank, and to seek the OCC's non-objection prior to entering into agreements with other national banks. *In the*

*Matter of First National Bank in Brookings, South Dakota*, Enforcement Action No. 2003-1 (January 17, 2003); *In the Matter of Peoples National Bank, Paris, Texas*, Enforcement Action No. 2003-2 (January 30, 2003); *In the Matter of Advance America, Cash Advance Centers, Inc., Spartanburg, South Carolina*, Enforcement Action No. 2003-3 (January 29, 2003).

### ***Early Intervention for Problem Banks***

- ***CEBA Credit Card Bank Early Intervention.*** In March 2003, the OCC initiated a cease and desist proceeding against a CEBA credit card bank, and the OCC issued a temporary cease and desist order, which was immediately effective. In this temporary order, the bank was directed (a) to cease performing its duties as servicer under the relevant securitization agreements as soon as practicable; (b) formally resign as servicer within one day of the effective date of the temporary order, in conformance with the requirements of the relevant securitization agreements; (c) immediately, and on a daily basis thereafter, withhold funds the bank collects as servicer to fully compensate it for servicing costs and expenses, but in no event withhold less than 3.5% per annum; (d) immediately make written demand on all necessary parties to amend the securitization agreements to ensure that the priority of the bank's servicing fee in the waterfall is consistent with the payment priority accorded to a third party, non-affiliated servicer and fully compensates the bank for its servicing costs; and (e) if bank has not executed written amendments to the securitization agreements within 30 days, to rescind the agreements and cease servicing. Finally, in April 2003, the OCC issued a second<sup>1</sup> consent cease and desist order against the bank, which resolved the OCC's ongoing cease and desist litigation, and terminated the temporary order. This consent order required that the bank withhold, as the cost of servicing, a stated percentage of the funds from the cash flow waterfall for three months, and to cease performing servicing by June 30, 2003. *In the Matter of First Consumers National Bank, Beaverton, Oregon*, Enforcement Action No. 2003-39 (April 15, 2003).
- ***Credit Card Accounts Purchase Facilitating Resolution of Problem Bank.*** A national bank facilitated the resolution of a problem credit card bank by purchasing the credit card accounts of the problem national bank. In connection with the purchase, the problem bank committed to enter into voluntary liquidation upon consummation of the purchase. Conditional Approval No. 602 (August 8, 2003).
- ***Lack of Viable Capital and Strategic Plans.*** A national bank consented to the issuance of a cease and desist order requiring that it formulate acceptable capital and strategic plans within a certain timeframe, or submit a plan to sell or merge the bank, or to liquidate the bank in

---

<sup>1</sup> The bank had entered into a first consent cease and desist order in FY 2002, calling, among other things, for a plan of disposition to sell, merge or liquidate the bank at no loss or cost to the federal deposit insurance fund.

accordance with 12 U.S.C. § 181. The bank, which had been subject to a number of enforcement actions over the past several years, had been unable to achieve consistent, stable earnings to support capital needs and strategic risks. The bank had suffered a number of losses in recent years and exhibited a repeated inability to formulate a reliable strategy to maintain continued profitability. In the Matter of The Park Avenue Bank, N.A., Enforcement Action 2003-28 (January 31, 2003).

- *Sale, Merger or Liquidation at No Loss to the Federal Deposit Insurance Fund Ordered.* Two banks were ordered to sell, merge or liquidate within specified time frames. The first bank suffered from weaknesses in capital levels, credit underwriting, loan administration, and problem loan identification, and failed to comply with an outstanding formal agreement it entered into with the OCC. The second bank's overall financial condition was declining and its credit risk increasing. These issues related to poor corporate governance and bank management's inability to effectively address credit risk and maintain internal controls and audit processes to ensure accurate bank records. Therefore, the OCC issued consent cease and desist orders in January and June 2003, requiring the banks to, among other things, outline the plans to sell, merge or liquidate within 60 days of the respective banks' receipt of no supervisory objection from the OCC as to the plan. Both banks were subsequently sold. *In the Matter of First National Bank of Littlefield, Littlefield, Texas, Enforcement Action No. 2003-15 (January 29, 2003); In the Matter of First National Bank of O'Donnell, O'Donnell, Texas, Enforcement Action No. 2003-70 (June 17, 2003).*
- *Unique Capital Requirement.* The bank had accumulated a large concentration of loans to finance the purchase, construction, and operation of hotels and motels. The practice of concentrating so much of the bank's assets in one industry was considered contrary to the generally accepted standard of diversification of risk. Further, by failing to prudently diversify its assets, the bank placed itself at an abnormal risk of loss. Because the concentration was so large in relation to capital, a small percentage decline in the carrying value of the hotel/motel loan portfolio would likely have a significant adverse impact on bank capital. The OCC entered into a Consent Order with the bank to address, among other things, the risk associated with the concentration of credit. Rather than requiring the bank to reduce the concentration of credit in relation to assets or capital, the Order required the bank to hold a capital "surcharge" for the hotel/motel loan portfolio. More specifically, the Order required the bank to hold tier one capital equal to 5% of its total assets, plus an additional amount of capital equal to 11% of the dollar amount of hotel/motel loans to protect against the risk of a downturn in that sector. This allowed the bank to maintain its market niche in hotel/motel lending, provided it maintained sufficient additional capital to support the concentration. Enforcement Action 2003-69 (July 2, 2003).

### ***Identity Theft, Computer Intrusion, and Privacy Violations***

- *Illegal Sale of ATM Cards and Pin Numbers.* In March 2003, the OCC issued a consent prohibition order against a former bank employee. The employee confessed to secretly taking over customer accounts by issuing at least five ATM cards. She then sold the ATM cards and PINs on the street for \$500 each. The ATM cards were used to withdraw money or purchase items totaling over \$33,000. *In the Matter of Wendy Webb*, Enforcement Action No. 2003-34 (March 19, 2003).
- *Privacy Regulations and Computer Intrusion Violations.* In April 2003, the OCC issued consent prohibitions, personal cease and desist and civil money penalty orders against a bank's former vice president and loan officer and his assistant for stealing approximately 2200 electronic loan files from the bank, and e-mailing them to a third party. By doing so, the former officer and employee each violated 12 CFR Part 40, titled "Privacy of Consumer Financial Information," engaged in unsafe or unsound practices, and in the case of the officer, breached his duty to the bank. The two were fined \$20,000 and \$10,000, respectively. These were the first enforcement actions alleging violation of the OCC's privacy regulations by bank insiders. *In the Matter of James Earl Smith*, Enforcement Action No. 2003-20 (April 4, 2003); *In the Matter of Vicki Boutilier*, Enforcement Action No. 2003-19 (April 4, 2003).
- *Theft and Sale of Customer Information to Third Parties.* In July 2003, the OCC issued a consent prohibition order against a former bank employee, who stole and sold customer identification documents and information to third parties. *In the Matter of Arthur D. Castillo*, Enforcement Action No. 2003-92 (July 8, 2003).

### ***International***

- *International Activities.* The OCC issued a final rule that makes regulatory requirements for foreign operations of national banks and federal branches and agencies of foreign banks operating in the U.S. more streamlined and risk-focused. The rule clarifies certain regulatory definitions and simplifies approval procedures for foreign banks seeking to establish federal branches and agencies in the U.S. The changes further conform the treatment of federal branches and agencies to their domestic national bank counterparts consistent with the national treatment principles of the International Banking Act of 1978. *68 Fed. Reg.* 70691 (December 19, 2003).
- *International Information Sharing Agreements.* The OCC entered into information sharing memoranda of understanding with The Netherlands and Brazil and exchanged information sharing letters with Slovakia, Latvia, and Jersey.

## *Investments*<sup>2</sup>

- *Community Reinvestment Act; Employment Fund.* National bank's proposed investment in a fund with the purpose of providing employment for low- and moderate-income individuals would be a qualified investment under the Community Reinvestment Act regulations. The fund's sole purpose is to invest in a limited liability company that will employ individuals the majority of whom will be low- and moderate-income, and who will be expected to qualify for various federal employment tax credits. The bank's investment will finance the hiring of employees who will perform various types of work, including clerical, retail, security, and building maintenance. The bank's investment will also help to finance the provision of ancillary services to facilitate employees' continued employment, such as job training, medical insurance, and employee assistance programs. Interpretive Letter No. 983 (October 24, 2003).
- *Community Reinvestment Act; New Market Tax Credits.* National bank's investment in connection with the New Markets Tax Credit program in a "Community Development Entity" (CDE), or a loan by a bank's CDE to a "Qualified Active Low-Income Community Business" or to another CDE, would receive consideration as a qualified investment or a community development loan, respectively, under the Community Reinvestment Act regulations. Interpretive Letter No. 984 (December 17, 2003).
- *Crime Prevention Programs in Nursing Homes.* A national bank may purchase preferred stock in a foundation that operates crime prevention programs in nursing homes. The foundation uses the bank's funds to purchase government and agency securities. Interest earned on these securities is used to fund crime prevention activities in nursing homes located in low- and moderate-income areas or occupied by low- and moderate-income residents. Notices dated November 17, 2003 and December 10, 2003; publication pending.
- *Debt Rating Requirement for Establishing Financial Subsidiaries.* A national bank may rely on the rating assigned to the uninsured portion of the bank's certificates of deposit to satisfy the debt rating requirement necessary to establish a financial subsidiary under Section 121 of the Gramm-Leach-Bliley Act. The certificates of deposit qualify as "eligible debt" for purposes of the requirement under Section 121 that any of the 50 largest insured banks must have at least one investment grade rated issue of debt outstanding in order for the bank to establish a financial subsidiary. Interpretive Letter No. 981 (August 14, 2003).
- *Federal Employment Tax Credits.* A national bank may purchase an equity interest in a limited liability company (LLC) whose primary purpose is to invest in an operating company

---

<sup>2</sup> For investments in partnerships, note that subsidiaries of national banks may become general partners, but national banks may not.

that employs individuals, which employment is expected to qualify the operating for federal employment tax credits, including the Work Opportunity Credit, the Welfare to Work Credit, and the Renewal Community Employment Credit. The bank represented that most of the individuals will be low- and moderate-income individuals, and some may reside in low- and moderate-income areas and/or in areas that have been targeted for redevelopment by the federal government as Renewal Communities. The LLC will assign the individuals to provide labor hours with companies, many of which operate in low- and moderate-income areas or in areas that have been targeted for redevelopment by a government agency. In addition, the LLC will provide job training, medical insurance, and employee assistance programs for its employees. Letter dated September 26, 2003; publication pending.

- *Financial Services Company Generating an Enhanced Yield Based on Foreign Tax Benefits.* A national bank operating subsidiary may invest in the preferred shares of a foreign domiciled company. A foreign domiciled bank will be the only other co-investor in the company. The foreign company will invest in long-term assets of the national bank and extend long term credit to the foreign bank co-investor. The structure of the transactions achieves certain foreign tax benefits for the company, which ultimately accrue to its investors. Conditional Approval No. 595 (June 5, 2003).
- *Foundation.* A national bank may make an investment in a foundation that will use the funds to help capitalize a loan pool that makes loans that support affordable housing, community services, or permanent jobs for low- and moderate-income individuals, financing for small businesses; area revitalization or stabilization; or other activities, services or facilities that primarily promote the public welfare. The foundation is a community development financial institution certified by the U.S. Department of Treasury. Notice dated April 6, 2003; publication pending.
- *Hedging DPC Stock.* A national bank may purchase and hold options on the shares of stock of a company when the bank has acquired shares of that company in satisfaction of debts previously contracted. The bank would hold the options to hedge the market risk associated with changes in the value of the DPC shares. Interpretive Letter No. 961 (March 17, 2003).
- *Limited Purpose Bank.* A national bank may, pursuant to 12 U.S.C. § 24(7) and the four-part test for non-controlling equity investments by national banks, acquire and hold a non-controlling equity interest in a limited purpose, state-chartered bank that will limit its activities to those permissible for a bankers' bank, *i.e.*, the proposed bank will (1) take deposits from depository institutions; (2) buy and sell loan participations; (3) engage in lending transactions permissible for a banker's bank; and (4) provide correspondent services to depository institutions. Interpretive Letter No. 970 (June 25, 2003).
- *Merchant Processing.* Application by a national bank to establish an operating subsidiary to engage in merchant processing activities through a limited partnership. The subsidiary will

serve as the General Partner and hold a 1% ownership interest in the limited partnership. A second affiliated national bank will be a limited partner and hold a 99% non-controlling ownership interest in the limited partnership. The limited partnership will engage in proprietary merchant services in which applications are handled on-line through a software application that enables the sales force to review the application in real time. Corporate Decisions Nos. 582 and 583 (March 12, 2003).

- *Purchase of Bonds and Other Tax Exempt Instruments Issued by Government Agencies.* A national bank may purchase preferred shares in a trust that acquires and owns tax-exempt participating and nonparticipating first mortgage bonds and other tax-exempt instruments that are issued by various state or local government, agencies or authorities. The proceeds from the bonds are used for financing affordable housing development and rehabilitation, and most of those properties also benefit from the use of federal low-income housing tax credits. Notices dated March 24, 2003 and September 30, 2003; publication pending.
- *Reinsurance Company.* Insurance agency operating subsidiary of a national bank may make a minority equity investment in a Bermuda reinsurance company that is necessary for the subsidiary to obtain liability insurance for itself. Interpretive Letter No. 965 (February 24, 2003).

### ***Preemption***

- *Applicability of Doctrine of Complete Preemption to Usury Suits Brought in State Court.* Reversing the 11<sup>th</sup> Circuit, the Supreme Court, in a 7-2 decision, held that a usury case brought against a national bank in state court could be removed to federal court under the doctrine of complete preemption. Complete preemption is a corollary to the well-pleaded complaint rule that a claim that falls within an exclusively federal cause of action necessarily presents a federal question warranting removal. *Beneficial National Bank v. Anderson*, 537 U.S. 1169 (2003).
- *Applicability of State Laws That Restrict Information Sharing with Affiliates.* A U.S. District Court held that provisions of the Fair Credit Reporting Act preempt local ordinances that impose restrictions on the sharing of confidential consumer information between financial institutions and their affiliates. As to the sharing of information with affiliates, the court decided that it need not address whether an express provision of the Gramm- Leach- Bliley Act also preempted the ordinances. However, as for the sharing of confidential consumer information with third parties, the court found that neither GLBA nor the National Bank Act preempts the ordinances. The OCC filed an amicus brief jointly with groups of bank amici and insurer amici. Upon appeal before the U.S. Court of Appeals for the Ninth Circuit, the defendant municipalities notified the Ninth Circuit that they had repealed the ordinances in dispute in the litigation and asked the court to dismiss the banks' appeal as moot and vacate the district court's decision in its entirety. The banks responded, agreeing

that the appeal was moot, but that only that portion of the district court decision on appeal, the decision that section 104 of the GLBA did not preempt the municipal ordinances, should be vacated. *Bank of America v. Daly City*, 279 F.Supp. 2d 1118 (N.D. Cal. 2003).

- *Debt Cancellation Contracts and Debt Suspension Agreements (12 CFR Part 37)*. The OCC published a final rule that addresses debt cancellation contracts and debt suspension agreements. The purposes of the customer protections are to facilitate customers' informed choice about whether to purchase debt cancellation contracts and debt suspension agreements, based on an understanding of the costs, benefits, and limitations of the products and to discourage inappropriate or abusive sales practices. The final rule also promotes safety and soundness by requiring national banks that provide these products to maintain adequate loss reserves. The final rule was published at 67 Fed. Reg. 58962 (Sept. 19, 2002). The OCC subsequently delayed, pending further action, the date for mandatory compliance with certain provisions of the rule for national banks offering debt cancellation or debt suspension products through a non-exclusive agent in connection with closed-end consumer credit. See 68 Fed. Reg. 35283 (June 13, 2003).
- *Determination and Order Preempting the Georgia Fair Lending Act (GFLA)*. The OCC issued a Determination and Order in response to a request from National City Bank, National City Bank of Indiana, and their operating subsidiaries, National City Mortgage Company and First Franklin Financial Company. The request asked the OCC to determine whether the GFLA applied to the banks and their operating subsidiaries, and to issue an appropriate order. The OCC concluded that the provisions of the GFLA affecting national banks' real estate lending are preempted by Federal law and, accordingly, that the GFLA does not apply to National City or to any other national bank or national bank operating subsidiary that engages in real estate lending activities in Georgia. The Determination and Order was published in the Federal Register at 68 Fed. Reg. 46264 (Aug. 5, 2003).
- *Multistate Fiduciary Operations*. The OCC issued a letter to a national bank that concluded that (i) a national bank's trust powers are governed by federal law and derive from 12 U.S.C. § 92a and Part 9 of the OCC's regulations; (ii) a national bank looks to the law of the state in which it acts in a fiduciary capacity in order to determine which capacities are permissible for the bank to act in for customers in that state as well as other states; and (iii) a state's authority to regulate instrumentalities of its own government (for example, by enacting state laws restricting the types of trustees, or other fiduciaries, those state government instrumentalities may appoint) does not affect the fiduciary authorities granted to national banks as a matter of federal law. Interpretive Letter No. 973 (August 12, 2003).
- *"On us" Check Cashing Fees*. National banks may charge a non-accountholder a convenience fee for using a bank teller to cash an "on us" check. An "on us" check is a check drawn on the bank by one of the bank's customers. The fee is essentially compensating the bank for making cash immediately available to the payee; otherwise the

payee would have to wait for the check to clear through the payment system. The U.S. Court of Appeals for the Fifth Circuit, affirming a decision below, held that the National Bank Act, specifically, 12 U.S.C. § 24 (Seventh), preempts state law prohibiting the charging of fees for cashing on-us checks. *Wells Fargo v. James*, 321 F.3d 488 (5<sup>th</sup> Cir. 2003). The OCC participated as amicus in the litigation.

- *State Insurance Sales Law Under the Gramm-Leach-Bliley Act.* The Commonwealth of Massachusetts and its Commissioners of Insurance and Banks filed a petition with the U.S. Court of Appeals for the First Circuit seeking review of an OCC Preemption Determination opining that provisions of a state consumer protection statute regulating insurance sales, solicitations, and cross-marketing activities of banks in Massachusetts were preempted by the Gramm-Leach-Bliley Act. The panel held that the OCC's opinion letter did not give rise to a regulatory conflict between state and federal regulators meeting the "case and controversy" requirement for judicial review. *Bowler v. Hawke*, 320 F. 3d 59 (1<sup>st</sup> Cir. 2003). In an earlier opinion, the majority of a Fourth Circuit panel, facing essentially the same scenario, held that the State of West Virginia and the State Insurance Commissioner had standing to bring the suit, that the OCC had implicit authority under the GLBA to preempt state statutes, and that the statutes were preempted. One of the judges dissented and found lack of standing. *Cline v. Hawke*, 51 Fed. Appx. 392 (4<sup>th</sup> Cir. 2002), *cert. denied*, *Independent Ins. Agents and Brokers of America v. Hawke*, 124 S.Ct. 63 (2003).
- *Visitorial Powers Over National Bank Operating Subsidiaries.* An interpretive letter explains OCC supervision of operating subsidiaries of national bank and the applicability of state law to operating subsidiaries. Interpretive Letter No. 971 (January 16, 2003). In two separate decisions, a U.S. District Court held that only the OCC may exercise visitorial authority over the operating subsidiary of a national bank, and that the Depository Institutions Deregulatory and Monetary Control Act (DIDMCA) preempts state law that prohibits a home mortgage lender from receiving interest for more than one day prior to the date that the mortgage is recorded. *Wells Fargo, N.A. v. Boutris*, 252 F.Supp.2d 1065 (E.D. Cal. 2003); *National City Bank of Indiana v. Boutris*, 2003 WL 21536818 (E.D. Cal. July 2, 2003).
- *Visitorial Powers; State Licensing.* An operating subsidiary of a national bank is not required to be licensed under California law in order to engage in mortgage lending in the state. Interpretive Letter No. 957 (January 27, 2003).

## **Regulations**

- *Community and Economic Development Entities, Community Development Projects and Other Public Welfare Investments (12 CFR Part 24).* The OCC published a final rule amending part 24, the regulation governing national bank investments that are designed primarily to promote the public welfare. The final rule updates the regulation to reflect the

additional types of public welfare investment structures that have become more common in recent years and that are permissible under the governing statute. It also clarifies the statutory standard that applies to the activities of those entities; simplifies the standards for making public welfare investments; clarifies how a national bank calculates the value of its public welfare investments for purposes of complying with the rule's investment limits; simplifies the regulation's investment self-certification and prior approval processes; and expands the list of examples of qualifying public welfare investments that satisfy the rule's requirements. The final rule was published at 68 Fed. Reg. 48771 (Aug. 15, 2003).

- *Corporate Activities; Bank Activities and Operations.* The OCC issued a final rule to implement sections 1204, 1205, and 1206 of the American Homeownership and Economic Opportunity Act of 2000, which enables national banks to undertake certain corporate organizational changes more efficiently than under previous law and provides for more modern corporate governance mechanisms for national banks. 68 Fed. Reg. 70122 (December 17, 2003).
- *Customer Identification Programs for Banks, Savings Associations, and Credit Unions (31 CFR 103 and 12 CFR 21).* The Department of the Treasury, together with the Financial Crimes Enforcement Network, the OCC, Board of Governors of the Federal Reserve System, FDIC, Office of Thrift Supervision, and National Credit Union Administration published a final rule implementing section 326 of the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001. Section 326 requires a regulation that contains minimum standards that financial institutions must implement: 1) to verify the identity of any person seeking to open an account; 2) to maintain records of the information used to verify the person's identity; and 3) to determine whether the person appears on any lists of known or suspected terrorists or terrorist organizations provided to the financial institution by any government agency. The final rule was published at 68 Fed. Reg. 25090 (May 9, 2003).
- *Debt Cancellation Contracts and Debt Suspension Agreements.* On September 19, 2002, the OCC issued a final rule establishing consumer protection and safety and soundness requirements for debt cancellation contracts and debt suspension agreements. The regulation clarified that its provisions, and not the federal insurance regulations or state law, governs national banks that provide these products. See 67 Fed. Reg. 58962. The OCC delayed, pending further action, the date for mandatory compliance with certain provisions of the rule for national banks offering debt cancellation or debt suspension products through a non-exclusive agent in connection with closed-end consumer credit. 68 Fed. Reg. 35283 (June 13, 2003).
- *Electronic Filings.* The OCC issued an interim rule to permit national banks to make any class of licensing filings electronically. The purpose of the rule is to facilitate the OCC's e-Corp program, which enables national banks to make certain types of licensing filings

electronically through the OCC's National BankNet Web site. National banks may consult the *Comptroller's Licensing Manual* to determine which types of filings may be made electronically. 68 *Fed. Reg.* 17890 (April 14, 2003).

- *Regulatory Capital; Asset-backed Commercial Paper.* The OCC, the Federal Reserve Board, the FDIC, and the OTS issued an interim final rule to amend the risk-based capital standards for the treatment of assets in asset-backed commercial paper programs consolidated under the recently issued Financial Accounting Standards Board Interpretation No. 46, Consolidation of Variable Interest Entities. The interim rule applies only for the regulatory reporting periods ending September 30 and December 31, 2003, and March 31, 2004. 68 *Fed. Reg.* 56530 (October 1, 2003).
- *Removal, Suspension, and Debarment of Accountants from Performing Audit Services (12 CFR Part 19).* The OCC, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, and Office of Thrift Supervision, published a final rule implementing the agencies' authority to suspend or debar accountants and accounting firms from performing the annual independent audits that are required by section 36 of the Federal Deposit Insurance Act (12 U.S.C. 1831m). The final rule establishes rules of practice and procedure to implement this authority and reflect the agencies' increasing concern with the quality of audits and internal controls for financial reporting at insured depository institutions. The final rule enhances the agencies' ability to address misconduct by accountants who perform annual audit and attestation services. The final rule was published at 68 *Fed. Reg.* 48256 (Aug. 13, 2003).
- *Sarbanes-Oxley Act Implementation.*
  - *National banks with securities registered under the Securities Exchange Act of 1934.* The OCC issued a final rule revising regulations to reflect changes in the Securities Exchange Act of 1934 (Exchange Act) made by the Sarbanes-Oxley Act of 2002. The changes to the Exchange Act give the OCC authority to administer and enforce new reporting, disclosure, and corporate governance requirements with respect to national banks that have a class of securities registered under the Exchange Act. The rule also revises the OCC's securities offering disclosure rules for national banks that issue securities that are not subject to the registration requirements of the Securities Act of 1933. 68 *Fed. Reg.* 68489 (December 9, 2003).
  - *Electronic filing and disclosure of beneficial ownership reports.* The OCC issued an interim rule to amend the agency's regulations, policies, and procedures to require the electronic filing of beneficial ownership reports by officers, directors, and major shareholders of national banks that have equity securities registered under the Exchange Act. The rule also requires that all reports filed under section 16(a) of the Exchange Act must be filed electronically and posted on a registered national bank's Web site. 68 *Fed. Reg.* 54981 (September 22, 2003).

*For More Information Please Contact*

**Office of the Comptroller of the Currency**

250 E Street S.W. • Washington, DC 20219

Phone (202) 874-5000 • FAX (202) 874-5263