



# State of North Carolina

OFFICE OF THE COMMISSIONER OF BANKS

MICHAEL F. EASLEY  
GOVERNOR

October 2, 2003

JOSEPH A. SMITH, JR.  
COMMISSIONER OF BANKS

The Honorable John D. Hawke, Jr.  
Office of the Comptroller of the Currency  
250 E Street, SW  
Public Information Room, Mail stop 1-5  
Washington, DC 20219

Attention: Docket No. 03-16; Notice of Proposed Rulemaking, 68 Fed. Reg. 46119 (2003) (the "Proposed Rulemaking")

Dear Mr. Hawke:

I am Commissioner of Banks of the State of North Carolina, in which capacity I am submitting this letter of comment with regard to the above-referenced Proposed Rulemaking. I have reviewed and endorse the analysis and conclusions of policy and law submitted to you by the Conference of State Bank Supervisors ("CSBS") in its comment letter to you, dated September 26, 2003. I will not replicate the CSBS comment letter; however, I will augment it with an analysis of the foreseeable and detrimental impact of the Proposed Rulemaking on North Carolina statutes that address abuses in the residential mortgage lending market. On the basis of the arguments set forth in the CSBS letter and this letter, I request that you withdraw the Proposed Rulemaking.

## **North Carolina Legislation Regarding Home Mortgage Lending**

Adoption of the Proposed Rulemaking would, among other things, undermine the regulatory and enforcement structure established by the General Assembly of North Carolina with regard to home mortgage lending. The foundation of this regime is the North Carolina predatory lending law,<sup>1</sup> which places limitations on the making of high-cost home loans and forbids specified lender actions such as "flipping." The North Carolina predatory lending law was enacted in response to the conduct of a variety of firms (including a finance company that is now part of a banking organization that includes a national bank) that was unconscionable but was not prohibited by then-applicable federal law.<sup>2</sup> The statute was drafted with the

<sup>1</sup> N.C. Session Law 1999-332, codified as N.C. Gen. Stat. § 25-1.1E.

<sup>2</sup> E.g., Testimony of Martin Eakcs, Self-Help CEO and Spokesperson for the Coalition for Responsible Lending before the Senate Committee on Banking Housing and Urban Affairs, July 26, 2001. Available at <http://predatorylending.org/pdfs/testimony072601.pdf>.



participation of representatives of the State government, the non-profit sector, and the financial services industry, including national banks. It was endorsed by all of those stakeholders and was enacted by large majorities of both houses of the General Assembly, including substantial majorities of both political parties. With the exception of a few technical amendments in later legislative sessions, I am not aware of any proposal by any person or entity to materially amend or repeal the predatory lending law.

In 2001, the General Assembly supplemented the predatory lending law by adoption of the Mortgage Lending Act ("MLA"). The MLA provides for licensure by the North Carolina Office of Commissioner of Banks ("OCOB") of mortgage lenders, brokers and loan officers, defines with specificity a number of prohibited activities in connection with the making of residential mortgage loans, and gives OCOB enhanced enforcement powers to address violations of the MLA and the predatory lending law.<sup>3</sup> National banks, subsidiaries of national banks and their employees are expressly excluded from the licensing requirements of the MLA; however, they are subject to a provision of that law requiring them to inform OCOB of their exempt status under the law and identify their supervisor or regulator.<sup>4</sup> National banks, their subsidiaries and the employees of each are, in the view of OCOB, subject to the provisions of the MLA regarding prohibited activities.<sup>5</sup> Like the predatory lending law, the MLA was drafted with the participation of all material stakeholders, including representatives of national banks, and was adopted by overwhelming and bipartisan majorities in both houses of the General Assembly. With the exception of amendments in 2002 to provide for limited licensure under MLA for the employees of consumer finance and insurance companies, there has been no attempt to materially amend or repeal the MLA.

The North Carolina predatory lending law has worked. It has been estimated by the Center Responsible Lending ("CRL") that the enactment of the predatory lending law has saved North Carolina consumers \$100 million during its first year in effect.<sup>6</sup> That amount has been disputed, but if the public benefit of the statute is only a fraction of the amount claimed by CRL it is still a substantial one and one that has been achieved with no material adverse effect on the market for credit overall, and subprime credit in particular.

It has been alleged that North Carolina's predatory lending law has reduced the availability of credit to subprime borrowers in this state.<sup>7</sup> I do not believe that this allegation is correct. A recent study by Dr. Michael Stegman and his colleagues at the University of North

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<sup>3</sup> N.C. Session Laws 2001-393 and 2001-399, amended by N.C. Session Law 2002-169 (codified as N.C. Gen. Stat. Chapter 53, Article 19A); N.C. Gen. Stat. 53-243.02, 53-243.11, 53-243.12, 53-243.14.

<sup>4</sup> N.C. Gen. Stat. 53-243.15.

<sup>5</sup> N.C. Gen. Stat. 53-243-11. "Prohibited activities" under this section of the statute comprise eleven specified violations, including false or misleading representations or advertising in connection with a mortgage loan; misapplication of funds; failure to pay for ordered appraisals; and violation of the predatory lending law.

<sup>6</sup> Ernst, Faris and Stein, "North Carolina's Subprime Home Loan Market After Predatory Lending Reform" (August 12, 2002). Available at [http://www.predatorylending.org/pdfs/HMDA\\_Study\\_On\\_NC\\_Market.pdf](http://www.predatorylending.org/pdfs/HMDA_Study_On_NC_Market.pdf)

<sup>7</sup> E.g., Remarks by John D. Hawke, Comptroller of the Currency Before The Federalist Society, Washington, DC, July 24, 2003, at p.6. Available at <http://www.occ.treas.gov/ftp/release/2003-57a.pdf>. The assessment of North Carolina's predatory lending law contained in these remarks was later revised by means of a "Clarification" published on July 30, 2003, which admitted that "our initial conclusion regarding a specific percentage decline in originations [based on the UNC study cited *infra* at note 8] could not properly be derived from the study's tables and therefore was mistaken." Available at <http://www.occ.treas.gov/ftp/release/2003-57b.pdf>.

Carolina has concluded, among other things, that the predatory lending law sharply reduced the number of subprime loans involving the predatory terms and conduct, with no negative impact on credit availability.<sup>8</sup>

These conclusions are supported by my experience in office. As Commissioner of Banks, I hear a variety of consumer complaints virtually every day: from consumers themselves, from the Governor's Office, and from the constituent service offices of Members of Congress and State Legislators. During the last twelve months, over seventy-five percent of formal complaints to the Office of Commissioner of Banks have involved mortgage lending activities. Not one of these complaints has involved the inability of a North Carolina citizen to obtain residential mortgage credit. All of them have involved alleged violations of law or good practice in connection with the origination of such loans.

### **Impact of the Proposed Rulemaking on North Carolina Law**

Adoption of the Proposed Rulemaking would apparently preempt, directly or by implication, all provisions of the North Carolina predatory lending law and MLA. As a result, such statutes would no longer apply to national banks and their subsidiaries. These statutes would continue to apply to state-chartered financial institutions and their subsidiaries (except with regard to licensure) and to non-bank mortgage lenders, brokers and loan officers otherwise subject to such statutes. I submit to you that preemption of these statutes would be bad public policy because:

1. It would create distinctions between banks on the basis of jurisdiction of organization without any showing that the pre-empted statutes conflict in any material way with the National Bank Act. It is ironic that national banks that supported the North Carolina legislation would be included in such pre-emption without, to my knowledge, having asked for it or made a showing of conflict and harm.
2. It would create distinctions between non-bank mortgage companies included in banking organizations based on where they are located in the organization. Holding company subsidiaries would be subject to the North Carolina laws; bank subsidiaries would not.
3. Given the distinctions referred to above, preemption would create opportunities for regulatory arbitrage – choices between organizational structures – that would reduce consumer protections rather than increase them. This arbitrage would substantially reduce the benefits to consumers of state enforcement of consumer protection laws.
4. It would reduce the tools available to financial services regulators, state and federal, to protect consumers from misconduct in the marketplace. The prohibited acts and enforcement provisions of the MLA are much more focused and effective than the provisions of the Federal Trade Commission Act, which do not expressly apply to mortgage lending. Further, use of bank examinations as an enforcement tool with regard

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<sup>8</sup> Quercia, Stegman and Davis, "The Impact of North Carolina's Anti-Predatory Lending Law: A Descriptive Assessment" (2003). Available at [http://www.kenan-flagler.unc.edu/assets/documents/CC\\_NC\\_Anti\\_Predatory\\_Law\\_Impact.pdf](http://www.kenan-flagler.unc.edu/assets/documents/CC_NC_Anti_Predatory_Law_Impact.pdf).

to mortgage lending would be limited in effect. A matter that is significant at the state or local level may – and probably will – be considered immaterial when viewed in the context of the total business of a large national bank or its subsidiary. North Carolina's laws allow for tailored and specific enforcement actions with regard to consumer protection that can and should supplement OCC's supervisory powers.

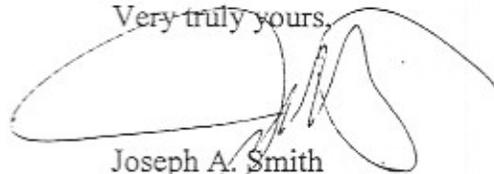
In sum, any gains the Proposed Rulemaking could or would confer on the financial system in terms of efficiency would, in my opinion, be more than outweighed by losses to consumers of legal protection in North Carolina and other comparable jurisdictions.

Whatever the outcome of the Proposed Rulemaking, one aspect of my office's consumer protection activities will remain constant: cooperation with federal authorities, including OCC, in the handling of consumer complaints and the enforcement of consumer protection laws. The policy of the North Carolina Office of Commissioner of Banks has been for a number of years, and will continue to be, to promptly forward consumer complaints involving national banks to OCC for handling and resolution.<sup>9</sup> Adoption of the Proposed Rulemaking will not affect our policies and practices; it will reduce the tools available to OCC and OCOB to address abuses in the mortgage market that involve national banks or their subsidiaries.

### Conclusion

My service as North Carolina Commissioner of Banks has involved a substantial amount of activity in the residential mortgage market, including interaction with the various industries that make mortgage loans and first-hand enforcement activity. On the basis of this experience, it is clear to me that the resources of both state and federal regulatory and law enforcement agencies are necessary to set standards of conduct for all market participants and to police the marketplace. Effective regulation and enforcement can best be achieved by cooperation between state and federal authorities. Such cooperation is not facilitated by the Proposed Rulemaking's assertion of exclusive jurisdiction, particularly as it relates to mortgage lending. As your colleague in government, I urge you to withdraw it and to work with state supervisors and Congress to address the very important issue of consumer protection in the residential mortgage market.

Very truly yours,



Joseph A. Smith  
Commissioner of Banks

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<sup>9</sup> Such referrals have been made during the last twelve months with regard to 84 formal banking complaints against national banks, comprising 22% of the 366 banking complaints received during that period.