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VIEWPOINTS

A Matter of Priorities: What the States Can Do in Response to Preemption

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At its core, the current debate over the impact of federal preemption on the dual-banking system is based upon fundamentally different views of the system.

For the Office of the Comptroller of the Currency, preemption is a way to maintain the integrity of the two independent regulatory systems and prevent the states from imposing inappropriate conditions or limitations on national banks.

For the states, preemption disrupts the balance of the dual-banking system. It allows national banks to avoid state laws and potentially gain a competitive advantage over state banks.

Can these divergent views be reconciled? Possibly.

The common ground may be that federal preemption does not bar states from addressing any competitive imbalance that may result from preemption. When state laws are preempted, the states retain the ability to achieve regulatory "equalization" simply by repealing the application of a preempted law on state banks. Georgia did just that after the OCC issued a preemption order related to a fair-lending statute.

Some states may decide not to exercise this right, especially if they conclude that the purpose of the preempted law is more important than the policy of competitive equality between state and national banks. Nonetheless, that decision rests with the states. If the states want to achieve regulatory equality, it is within their power to achieve it.

There is, however, more to this story. I suspect that the reason states emphasize a policy of equalization over a policy of distinction is because Congress has diminished their ability to distinguish state banks from national banks — not through the National Bank Act or any actions by the OCC, but through other federal laws, specifically the Federal Deposit Insurance Act and the Bank Holding Company Act.

Since the demise of state deposit insurance systems, all state banks have become subject to the Federal Deposit Insurance Act. It imposes a host of conditions on state banks, including a prohibition on their ability to engage in activities that are not permissible for national banks. The Bank Holding Company Act also places restrictions on state banks by limiting the scope of their affiliations.

If states were truly free to determine what activities and affiliations are appropriate for their banks, they might not be so focused on the policy of equalization or so upset with the doctrine of federal preemption. It appears, however, that the states have concluded that it is easier to pursue a policy of equal regulation rather than try to restore their independent control over state banks.

From the perspective of the states, that conclusion probably makes sense. It certainly would be difficult for the states to persuade Congress to reverse the decisions embodied in the Federal Deposit Insurance Act and the Bank Holding Company Act.

On the other hand, bankers should realize that equalization can be achieved either by excusing state banks from compliance with preempted laws or by curtailing the doctrine of preemption and subjecting national banks to state laws. Thus, the manner in which a policy of equalization is implemented will have a significant impact on the industry.

Bankers also may want to consider what type of system remains if the differences between the regulation of state and national banks disappear.

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