

## Viewpoint: Supreme Court Unwisely Backed OCC in Watters

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It is often said that ours is a dual banking system; charters are available at both the state and federal level featuring different but sometimes overlapping regulatory oversight.

For decades the courts and Congress have fostered a policy of “competitive equality” between the players in this system. Though the economic assumptions underlying this structure have their critics, the concept of competitive equality has long cultivated the appearance (if not the fact) of a vibrant, free-market atmosphere in which state and federal institutions and their regulators compete to provide or permit innovative products and services to attract consumers and converts from one charter to the other.

In its April 17 decision in *Watters v. Wachovia*, the Supreme Court took a subtle step away from a concept that may have been only an illusion after all.

The majority held that a national bank’s operating subsidiary—in this case, a mortgage lender—is subject only to the “OCC’s superintendence, and not to the licensing, reporting, and visitorial regimes of the several states in which the subsidiary operates.” The decision validates the Office of the Comptroller of the Currency’s efforts to preempt state laws affecting operating subsidiaries of national banks and could encourage the OCC and other federal regulators to further flex their muscles.

In his *Watters* dissent, Justice John Paul Stevens decried this result, invoking court precedent for the proposition that “the policy of competitive equality is ... firmly embedded in the statutes governing the national banking system” and is not “open to modification by the comptroller of the currency.”

The majority opinion attempted to rebut the dissent’s focus on “competitive equality” by arguing that the words “should not be ripped from their context.” The ruling pointed out that the principal case Justice Stevens cited for the proposition involved a statute (the McFadden Act) that conditioned national bank branching on state branching laws. Because there is no such “condition” in the provisions of the National Bank Act relevant to the *Watters* case, the majority suggested, the principle of competitive equality does not apply.

But this reasoning ignores the “two-way street” aspect of a principle aimed at protecting both prongs of the dual banking system (state and federal).

The Watters decision serves to enhance the national charter's appeal.

It could increase the rate of conversion from state to federal charters and therefore can be seen as striking a body blow to the dual banking system. Consumers could end up the losers in this episode unless Congress or the OCC addresses perceived weaknesses in the ability of the OCC—usually seen as principally a safety-and-soundness regulator—to plug emerging holes in consumer protection, where states traditionally have played the leading role.

This is true even though state statutes of “general application,” such as (presumably) state codifications of the Uniform Deceptive Trade Practices Act, still will apply to national banks and their operating subsidiaries.

Congress and the OCC should act to prevent the Supreme Court's step away from the doctrine of competitive equality from becoming a permanent detour off the dual banking highway.

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