O

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

Interpretive Letter #902
January 2001
12 USC 36J

November 16, 2000

Subject: **[ ]**-- Missouri Loan Production Offices

Dear **[ ]**:

This is in response to your inquiry concerning **[ ]** (" "), a division of **[** ***Bank name, City, State*** **]** ("the Bank"). Mr. Gregory Omer, Chief Counsel of the Missouri Department of Economic Development, Division of Finance, has informed you that it is his belief that **[ ]**'s offices in that state are in violation of Missouri regulation 4 C.S.R. § 140-6.075. This regulation contains activity restrictions and reporting requirements for loan production offices ("LPOs"), and purports to apply to both state and national banks. You believe that, as a division of a national bank, **[ ]** is not subject to this regulation, and requested a letter setting forth our views on this matter. Mr. Omer is aware that you have requested our views, and we understand that you will be providing a copy of this response to him.

The Bank has established no branches in Missouri but, through **[ ]**, operates LPOs in several locations in that state. These offices originate consumer-oriented loans such as home equity loans and other secured loans. They also purchase retail installment sales contracts from various dealers. **[ ]** does not offer unsecured loans in Missouri, although it does in other states. All loan applications are underwritten using the Bank's centrally-developed and applied consumer loan credit standards. The final decision to approve or deny a loan is made by a loan officer at the LPO based upon these standards, with certain authority to make exceptions based upon personal judgment.

No processing of loan payments is performed at these offices. Borrowers are directed to mail loan payments to a postal lockbox. However, loan payments are sometimes brought to a **[ ]** office in spite of these instructions, and in that event, **[ ]** personnel simply mail the payments to the lockbox address. You asked us to address the permissibility of loan approval and receipt of loan payments at an LPO.

It is well settled that national banks may conduct business without geographic restrictions unless Congress provides otherwise. *Clarke v. Securities Industry Association*, 479 U.S. 388 (1987); *NBD Bank, N.A. v. Bennett*, 67 F.3d 629 (7th Cir. 1995); *Independent Insurance Agents of America, Inc. v. Ludwig*, 997 F.2d 958 (D.C. Cir. 1993). The establishment of branches is one of the few areas where Congress has provided such an exception. Twelve U.S.C. § 36 incorporates state geographic restrictions on the establishment and location of national bank branches, and requires authorizing state legislation in the case of *de novo* interstate branches. Missouri has not authorized *de novo* interstate branching and considers the LPOs to be impermissible branches of the Bank. However, under federal law, nonbranch national bank facilities such as LPOs are not subject to state geographic restrictions. Hence, the disagreement in this case is about whether **[ ]**'s offices in Missouri are "branches" under federal law so as to be subject to state geographic requirements.

The Missouri regulation provides, in relevant part:

> Loans which are originated at a loan production office must be approved or denied at the main office or branch office of the lending bank and the proceeds of these loans must be disbursed from the main office or a branch office of the lending bank; disbursement may not be effected by or through the loan production office. No payments may be accepted at a loan production office.

Mo. Code Regs. Tit. 4, § 140-6.075(2) (1993). Missouri contends that if a loan production office does not observe these activity limitations, it is a branch.

However, while Missouri may define a "branch" for purposes of state law, the definition of a national bank "branch" is governed by federal law. *First National Bank in Plant City v. Dickinson*, 396 U.S. 122 (1969). Federal law defines a branch as any facility established by a national bank "at which deposits are received, or checks paid, or money lent." 12 U.S.C. § 36(j). (Automated teller machines and remote service units are specifically excluded, but they are not at issue here.) A national bank facility that does not fit this definition, such as a loan production office, is not a branch under federal law and therefore is not subject to state geographic restrictions. *First National Bank of McCook v. Fulkerson*, No. 98-D-1024 (D. Colo. filed Mar. 7, 2000); s*ee* Interpretive Letter No. 821, [1997-1998 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-271 (February 27, 1998) (ATMs); *Bank One Utah, N.A. v. Guttau*, 190 F.3d 844 (8th Cir. 1999), *cert. denied*, 146 L. Ed. 2d 641 (2000) (same). As the primary regulator of national banks, the OCC interprets the definition of "branch" under 12 U.S.C. § 36 (the McFadden Act).

The Missouri regulation treats loan approval as a branching activity, that is, a function that *must* be performed at a main office or branch and cannot be performed at an LPO. OCC regulations

provide that a national bank loan origination facility will not be considered a branch *if* the loans are approved at the bank's main office or a branch. 12 C.F.R. § 7.1004. However, this regulation is a safe harbor, not a legal requirement. Interpretive Letter No. 634, *reprinted in* [1993-1994 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,518 (July 23, 1993) (discussing the almost identically-worded predecessor of the current regulation). In other words, while that is one possible way for a bank to structure its lending operations, the OCC recognizes that loan approval may also take place at other locations without violating branching restrictions. This position is embodied in our regulation at 12 C.F.R. § 7.1005.

Credit underwriting is essentially a back office function, and has become even more so as modern technology has made it possible for loan "approval" functions to be performed virtually anywhere, based on pre-established criteria, with the results communicated instantly to anyplace else. Therefore, the physical location where loan "approval" takes place may have little significance in today's world. Moreover, the core branching function that is required under the McFadden Act is "making" loans. It is apparent that neither loan origination nor the technical act of loan approval, taken separately, constitutes the making of a loan. Interpretive Letter No. 634, *supra*. Performing two nonbranching functions at the same location does not change the nonbranching character of either. *First National Bank of McCook v. Fulkerson*, No. 98-D-1024 (D. Colo. filed Mar. 7, 2000); 12 C.F.R. § 7.4005; Interpretive Letter No. 691, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-006 (September 25, 1995). It follows that loan approval may take place at any location, including an LPO, without making that location a branch under federal law. Interpretive Letter No. 667, *reprinted in* [1994-1995 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,615 (October 12, 1994).[1] In the present situation, because loans in Missouri are underwritten using consumer loan credit standards centrally developed and applied by the Bank for its consumer lending business, we think it is particularly inappropriate to view the loan as "made" in Missouri.

You also asked us to address the issue of receipt of loan payments at LPOs. The Missouri regulation also treats this as a branching activity. But while Missouri is free to take this position as a matter of state law, in our view, the activities in question are not a branching function within the meaning of 12 U.S.C. § 36(j), and clearly would not be so based on the facts of the present situation, where loan payments at LPOs are proffered by customers even though the Bank has instructed the customer to pay in a different manner.

One court has characterized the repayment of loans as a "deposit," a core banking function under the McFadden Act. *Independent Bankers Association of America v. Smith*, 534 F.2d 921, 941 (D.C. Cir.), *cert. denied*, 429 U.S. 862 (1976). However, the Supreme Court has emphasized that statutes should be interpreted in accordance with their plain language. *See, e.g., Mansell v.*

[1] The OCC formerly took the position that the "aggregation" of loan origination and approval at one location was the functional equivalent of making a loan under the McFadden Act. *See, e.g.*, Interpretive Letter No. 343, *reprinted in* [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,513 (May 24, 1985). The Missouri regulation appears to reflect the same view. For the reasons discussed above, the OCC abandoned this position in Interpretive Letter No. 667, *supra*. It is possible that the Missouri regulation was originally based on OCC positions but has not been revised to reflect subsequent developments.

Mansell, 490 U.S. 581 (1989). Clearly, in adopting the definition of "branch" in 12 U.S.C. § 36, Congress distinguished between deposit-taking functions and loan functions and, in the context of lending, identified the *lending* of money -- not the repayment of money loaned -- as the branching function. Nevertheless, even assuming the continued viability of the *Smith* decision on this point, the present case is distinguishable.

As the Supreme Court has recognized, what is relevant in construing whether a facility is a branch is whether it might give the bank "an advantage in its competition for customers." *First National Bank in Plant City v. Dickinson*, 396 U.S. at 136-37. Potential borrowers do not select a lender based on where they can make loan payments; most borrowers make loan payments through the mail. **[ ]** borrowers are instructed to mail their loan payments to a designated lockbox address, and loan payments are only brought to a **[ ]** office if customers do not follow the established procedures. Thus, the number of such payments is limited, and is the result of actions by the customer, not by the Bank. Even then, the payments are not processed, but are simply mailed to the proper address. Such limited functions, performed solely to accommodate customers, should not be equated with receiving and processing loan payments as a normal business practice. We therefore conclude that under such circumstances, the receipt of loan payments at the Bank's LPO facility does not cause that facility to be a branch of the Bank under 12 U.S.C. § 36.

There is one other aspect of the Missouri regulation upon which we would like to comment. Paragraph (3) of the regulation requires that all banks, including national banks, must report annually to the state commissioner of finance the location of each loan production office; the volume of income generated by each office; the number of officers and other personnel employed at each location; and the address at which loans are approved or denied, and disbursement made. The right to operate an LPO is conditioned upon compliance with these requirements. Mo. Code Regs. Tit. 4, § 140-6.075(3) (1993).

State regulations are not preempted when Congress accompanies a grant of an explicit power with an explicit statement that the exercise of that power is subject to state law. *Bank One Utah, N.A. v. Guttau*, 190 F.3d at 848. However, where Congress has not expressly conditioned a national bank power upon a grant of state permission, ordinarily, no such condition applies. *Barnett Bank of Marion County v. Nelson*, 517 U.S. 25, 34 (1996). As explained earlier, Congress has not made state law applicable to the establishment of national bank facilities except in the case of branches. Moreover, these regulatory conditions appear to give Missouri visitorial[2] powers over national banks, at least with respect to LPOs. The OCC is the primary regulator of national banks and, unless otherwise expressly provided by federal law, has the sole visitorial and enforcement authority over them. 12 U.S.C. § 484; 12 C.F.R. § 7.4000; *Guthrie v. Harkness*, 199 U.S. 148 (1905).

[2] "Visitation" is not limited to inspection of books and records, but includes any act of a superintending official to "inspect, regulate, or control the operations of a bank to enforce the bank's observance of the law." *First Nat'l Bank of Youngstown v. Hughes*, 6 F. 737, 740-41 (6th Cir. 1881), *appeal dismissed*, 106 U.S. 523 (1883). *See* 12 C.F.R. § 7.4000(a)(2).

To summarize, we conclude that loans may be approved, and loan payments may be forwarded to the proper address under the circumstances described above, at the Bank's loan production office, and these activities will not cause the LPO to be a branch of the Bank within the meaning of 12 U.S.C. § 36. We further conclude that the Missouri regulation is not applicable to **[ ]** or the Bank, insofar as it attempts to authorize visitorial powers over national banks, contrary to federal law.

The scope of this letter is confined to the issues of loan approval, receipt of payments, and the necessity of state approval, as discussed herein, and we take no position on any other branching issues that may exist. I hope that you have found this discussion to be helpful. Please let me know if we can be of further assistance.

Sincerely,

-signed-

Eric Thompson
Director
Bank Activities and Structure Division