Fordham Urban Law Journal

Volume 31 | Number 6 Article 7

2004

In Pursuit of Safety and Soundness: An Analysis of the OCC's Anti-Predatory Lending Standard

Diana McMonagle

In Pursuit of Safety and Soundness: An Analysis of the OCC's Anti-Predatory Lending Standard

Cover Page Footnote
J.D. candidate, Fordham University School of Law, 2005; B.A., Political Science, Fordham University, 2001. I wish to thank Professor Susan Block-Lieb for introducing me to the topic of predatory lending and for her invaluable guidance in developing my ideas. Special thanks to Christiana Brennan for her constructive advice and ceaseless encouragement. This Comment is dedicated to my family, Karen, Jack, and Kristen McMonagle, whom I credit for all my accomplishments.

IN PURSUIT OF SAFETY AND SOUNDNESS: AN ANALYSIS OF THE OCC'S ANTI-PREDATORY LENDING STANDARD

*Diana McMonagle**

> To borrow a concept from the animal kingdom . . . a classic predator traps the unwary and preys on the weak. Put in the lending context, a predatory lender ensnares . . . vulnerable customers, offering loan products designed to prey on their weakness, bleed them financially and . . . strip them of their most precious possessions.[1]

PROLOGUE

George Campbell lived his entire life in the same home in Queens, New York.[2] Disabled, living solely on monthly Supplemental Security Income checks, Mr. Campbell had one significant financial asset: the value of his home appreciated substantially over the years and he amassed considerable equity in the property.[3] A few years ago, an aggressive mortgage broker persuaded Mr. Campbell to take out a second mortgage to finance much-needed repairs.[4] The broker claimed Mr. Campbell, with neither a checking account nor an established credit history, was ineligible for a bank loan.[5] Unable to read well, Mr. Campbell did not understand his obligations under the agreement; like countless other unsuspecting borrowers in the United States, Mr. Campbell became the victim of a predatory lender.[6] The terms of the mortgage required

* J.D. candidate, Fordham University School of Law, 2005; B.A., Political Science, Fordham University, 2001. I wish to thank Professor Susan Block-Lieb for introducing me to the topic of predatory lending and for her invaluable guidance in developing my ideas. Special thanks to Christiana Brennan for her constructive advice and ceaseless encouragement. This Comment is dedicated to my family, Karen, Jack, and Kristen McMonagle, whom I credit for all my accomplishments.

1. Julie L. Williams & Michael S. Bylsma, *The Predatory Lending Challenge*, 61 MORTGAGE BANKING 117, 118 (2000).

2. *See*, Dennis Hevesi, *New Curbs on Predatory Loans*, N.Y. TIMES, Nov. 10, 2002, at 1.

3. *Id.*

4. *Id.*

5. *Id.*

6. *Id.*

monthly payments almost equal to Mr. Campbell's social security income.[7] Predictably, he defaulted.[8]

INTRODUCTION

Predatory lenders are unscrupulous, aggressively marketing their loans to borrowers who cannot afford their credit on the onerous terms offered. Their prey are some of the most vulnerable members of society: the elderly, persons living in low-income areas, the socially and economically disadvantaged, the financially unsophisticated. The consequences are devastating, and include enormous personal losses, foreclosures on homes, and the devastation that foreclosure brings to entire neighborhoods. Many common abusive lending practices are already illegal under federal law,[9] yet predatory lending continues to destroy communities.[10]

In response to this escalating problem, the Office of the Comptroller of the Currency ("OCC"), a federal regulator of the national banking industry, issued a Final Rule on January 7, 2004 ("Final Rule").[11] The OCC has always prohibited banks from engaging in predatory lending, but difficulties defining "predatory" and the problematic application of conflicting state-lending laws has caused significant supervisory and enforcement problems.[12] The Final Rule addresses these problems and sets forth a uniform federal standard to guide banking policies on predatory practices and to aid regulators' identification of predatory loans.[13] The Final Rule forbids national banks from making consumer loans, includ-

7. *Id.*

8. *Id.*

9. *See, e.g.*, Federal Trade Commission Act § 5, 15 U.S.C. § 45(a)(1) (1914) (prohibiting deceptive and unfair trade practices); Truth in Lending Act, 15 U.S.C. §§ 1601-1666 (1968) (imposing disclosure requirements in lending); Home Ownership and Equity Protection Act, 15 U.S.C. § 1639 (1994) (protecting against certain high-rate and high-fee loans); Regulation Z, 12 C.F.R. § 226.34(a)(3) (2002) (prohibiting loan flipping under certain circumstances).

10. *See* Hevesi, *supra* note 2.

11. Bank Activities and Operations, 12 C.F.R. § 7.4008 (2004); Real Estate Lending and Appraisals, 12 C.F.R. § 34.3 (2004).

12. *See* Press Release, Office of the Comptroller of the Currency, *OCC Issues Final Rules on National Bank Preemption and Visitorial Powers; Includes Strong Standard to Keep Predatory Lending Out of National Banks* (Jan. 7, 2004) [hereinafter OCC Final Rule Press Release], *available at* http://www.occ.treas.gov/scripts/NewsRelease.aspx?Doc=ZN9I8H7T.xml. Before promulgation of the Final Rule, national banks were subject to state as well as federal anti-predatory lending laws. *Id.* This caused regulatory problems for banks with branches in states with inconsistent laws. *Id.*

13. *See* 12 C.F.R. §§ 7.4008, 34.3.

ing mortgage loans, car loans, and student loans,[14] based predominantly on the foreclosure value of the borrower's collateral.[15] The rationale lies in the OCC's belief that the value of a borrower's collateral does not indicate their ability to repay the loan. As a result, such loans are now per se predatory, and for that reason, prohibited.[16]

The Final Rule also preempts several categories of state banking laws[17] that are no longer enforceable against national banks.[18] States now have little authority to regulate the lending practices of those national banks situated within their jurisdictions.[19] Specifically, the Final Rule preempts state regulation of lending licenses, loan terms, interest rates, terms of credit, disclosure requirements, and other conditions of lending.[20] The Final Rule also codifies the judge-made determination that the OCC has authority to enforce Section 5 of the Federal Trade Commission Act ("FTC Act")[21] and regulations thereunder against unfair and deceptive trade practices in banking.[22]

Effectively, as a result of the Final Rule national banks are no longer subject to state anti-predatory lending laws.[23] The OCC

14. *See* Memorandum from the Office of the Comptroller of the Currency, Preemption Final Rule Questions and Answers 7 (Jan. 7, 2004), *available at* http://www.occ.treas.gov/2004-3dPreemptionQNAs.pdf.

15. 12 C.F.R. §§ 7.4008, 34.3.

16. *See* 12 C.F.R. §§ 7.4008, 34.3.

17. *See* 12 C.F.R. §§ 7.4008(d), 34.4(a). Pursuant to the National Bank Act, the OCC has authority to issue preemption regulation. 12 U.S.C. § 93(a); *see also* CSBS v. Conover, 710 F.2d 878 (D.C. Cir. 1983) (holding that the Comptroller of the Currency has authority under the National Bank Act to issue regulations preempting state laws that are inconsistent with national banking activities).

18. *See* 12 C.F.R. §§ 7.4007-7.4009. The OCC's authority to preempt state laws that place limitations and restrictions on national banks is based on constitutional principles under the Supremacy Clause. *See* McCullough v. Maryland, 17 U.S. 316 (1819) (applying the doctrine of preemption to banking regulation).

19. *See* 12 C.F.R. § 7.4008. The Final Rule also identifies those state laws that are not preempted. State laws that only incidentally affect lending are not preempted, including state regulation over matters pertaining to contract law, debt collection remedies, zoning restrictions, tort law, rules for the transfer of property, tax law, criminal law, and homestead rights. *Id.*; 12 C.F.R. §34.4(b).

20. *See* 12 C.F.R. § 34.4.

21. Federal Trade Commission Act § 5, 15 U.S.C. § 45(a)(1) (1914). The Final Rule gives the OCC authority to enforce the FTC Act. 12 C.F.R. §§ 7.4008(c), 34.3(c). Yet, the OCC's authority is limited to enforcement alone and the Federal Reserve maintains exclusive authority to promulgate rules and regulations under the FTC Act. § 15 U.S.C. 45(a).

22. 12 C.F.R. §§ 7.4008(c), 34.3(c).

23. *See* 12 C.F.R. §§ 7.4008, 34.4.

standard has replaced a multitude of state laws, and national banks are now only accountable to the OCC and its single standard.[24]

This Comment will analyze the potential ineffectiveness and possible consequences of the OCC's anti-predatory lending standard and argue that, despite the perceived comfort in having a single federal standard for evaluating predatory lending, the standard set forth in the Final Rule is inadequate, and inherently flawed.

Part I of this Comment attempts to define predatory lending and distinguishes predatory lending from non-predatory subprime lending.[25] Part I also explains the OCC's role in regulating predatory lending.[26] Part II examines the standard set forth in the Final Rule and analyzes it in light of the agency's justifications for adopting the rule,[27] which include agency concerns for the maintenance of the safety and soundness of the national banking system and the goal of ensuring fair and equal access to financial services for all Americans.[28] Part II concludes that the OCC's preemption of state anti-predatory lending laws and substitution of a single anti-predatory lending standard cannot reasonably be justified on these grounds.[29] Part II also explores the potential negative social and economic consequences that this regulation may have for low-income borrowers.[30] Part II suggests that this effect may increase the predatory lending problem by forcing these individuals to seek subprime loans from the largely unregulated non-bank sector, the segment of the financial industry notorious for committing predatory lending.[31] Part III proposes a solution to ameliorate the potential social and economic costs of the regulation.[32] It suggests that the OCC should interpret and enforce the regulation so that it only prohibits loans extended with a calculated intent to foreclose, and provides guidelines for determining a bank's intent.[33]

---

24. *See* 12 C.F.R. §§ 7.4008(e), 34.4(b).
25. *See infra* notes 34-65 and accompanying text.
26. *See infra* notes 66-88 and accompanying text.
27. *See infra* notes 89-165 and accompanying text.
28. *See infra* notes 99-165 and accompanying text.
29. *See infra* notes 109-33, 139-65 and accompanying text.
30. *See infra* notes 151-65 and accompanying text.
31. *See infra* notes 162-65 and accompanying text.
32. *See infra* notes 166-68 and accompanying text.
33. *See infra* notes 166-68 and accompanying text.

I. PREDATORY LENDING IN THE SUBPRIME MARKET AND THE ROLE OF THE OCC

A. Defining the Problem

John D. Hawke, Comptroller of the Currency, defines predatory lending as "the aggressive marketing of credit to people who simply cannot afford it."[34] This may be an oversimplification. Other commentators argue that the term in fact applies to a catalogue of exploitative lending practices that generally fall into one of two categories.[35] The first consists of illegal and unconscionable lending tactics, such as forging signatures on loan documents, fraudulently misrepresenting the terms of a loan, double billing, hidden fees, and charging for services that were never rendered.[36] The second category addresses activities which are not as obviously abusive—legal lending practices which are misused by unprincipled lenders. This includes loan flipping,[37] equity stripping,[38] high interest rates and hidden fees,[39] among other abusive lending practices.[40] Still others believe that the term defies traditional defini-

34. John D. Hawke, Jr., Remarks Before The Federalist Society (July 24, 2003), *available at* http://www.occ.treas.gov/ftp/release/2003-57a.pdf.

35. *See* Kurt Eggert, *Held Up in Due Course: Predatory Lending, Securitization, and the Holder in Due Course Doctrine*, 35 CREIGHTON L. REV. 503, 513 (2002).

36. *Id.*

37. Loan flipping is the frequent refinancing of a loan, where the service fees and credit insurance costs are financed by the loan so that the principal continually rises, even as the borrower makes payments on the loan. For a discussion of the Federal Reserve Board's attempt to curb predatory loan flipping, see Michael J. Pyle, Comment, *A "Flip" Look at Predatory Lending: Will the Fed's Revised Regulation Z End Abusive Refinancing Practices?*, 112 YALE L.J. 1919, 1924 (2003) (analyzing the Federal Reserve Board's Regulation Z prohibiting certain forms of loan flipping).

38. In mortgage lending, equity stripping refers to two related practices. One is the practice of lending to individuals with considerable equity in their home who have no means to repay the loan. *See* Better Business Bureau, *Beware of Predatory Practices in Home Mortgage Lending*, *at* http://bbb.org/alerts/article.asp?ID=240 (last visited Nov. 4, 2004). When the homeowner defaults the lender forecloses and sells the home, stripping the borrower of his equity. *Id.* The term also applies to the practice where lenders charge excessive fees at closing that are paid out of the borrower's equity. *See* ERIC STEIN, QUANTIFYING THE ECONOMIC COST OF PREDATORY LENDING 4 (2001), *available at* http://www.predatorylending.org/pdfs/Quant10-01.pdf. This practice is particularly deceptive because when paid out of equity the borrower "does not feel the pain of counting out thousands of dollars in cash. The borrower parts with the money only later, when the loan is paid off and the equity value remaining in his or her home is reduced by the amount of fees owed." *Id.*

39. *See* Eggert, *supra* note 35, at 513.

40. *See, e.g.*, *id.* at 512-14; ASSOCIATION OF COMMUNITY ORGANIZERS FOR REFORM NOW, SEPARATE AND UNEQUAL 2002: PREDATORY LENDING IN AMERICA (2002) (outlining the scope of predatory lending in the subprime market) [hereinafter ACORN, SEPARATE AND UNEQUAL 2002], *available at* http://www.acorn.org/index.php?id=102.

tion, since it encompasses loan terms and products that, on their face, are impossible to differentiate from legitimate lending practices.[41] These commentators instead characterize predatory lending on a "you know [it] when you see it"[42] basis, recognizing that any practice "targeted at vulnerable populations [that causes] devastating personal losses, including bankruptcy, poverty, and foreclosure" is predatory.[43]

Another problem in defining predatory lending arises because predatory lending occurs primarily in the subprime market.[44] Subprime loans are loans with higher interest rates designed for borrowers who would not qualify for loans at the prime rate because of a blemished, or nonexistent, credit history.[45] The emergence and growth of the subprime market is considered a national economic success,[46] and has given low-income borrowers access to credit where they did not have access before.[47] By allowing families and individuals who are ineligible for prime rate loans to obtain subprime rate mortgages, the increased availability of subprime credit has been critical in aiding a recent increase in rates of homeownership.[48] Subprime lending has also been credited with increasing mortgage lending to minority borrowers, particularly Hispanics and African-Americans during the 1990s.[49] The difficult question is whether regulators can proscribe predatory lending while at the same time encouraging beneficial subprime lending.

While not all subprime lenders are predatory, nearly all predatory loans are subprime.[50] Although predatory loans constitute only a subset of subprime lending, the whole is sometimes mis-

41. *See* Eggert, *supra* note 35, at 513.

42. Kathleen C. Engel & Patricia A. McCoy, *A Tale of Three Markets: The Law and Economics of Predatory Lending*, 80 TEX. L. REV. 1255, 1260 (2002).

43. *Id.*

44. *See id.* at 1261.

45. *See id.*

46. *See* ROBERT E. LITAN, UNINTENDED CONSEQUENCES: THE RISKS OF PREMATURE STATE REGULATION OF PREDATORY LENDING (2003) (noting that national subprime mortgage originations increased from $34 billion in 1994 to over $173 billion in 2001), *available at* http://www.aba.com/NR/rdonlyres/D881716A-1C75-11D5-AB7B-00508B95258D/28871/PredReport200991.pdf.

47. *See* Charles W. Calomiris & Robert E. Litan, *Homeownership That's Too Important to Risk*, N.Y. TIMES, Aug. 20, 2001, at A17.

48. *Cf.* Litan, *supra* note 46, at 4 (noting that subprime mortgage lending increased from $34 billion in 1994 to over $160 billion in 1999).

49. *See id.*

50. *Prepared Testimony of John. D. Hawke, Jr. Comptroller of the Currency: Before the House Comm. on Banking and Fin. Servs.*, 106th Cong. (May 24, 2000) [hereinafter *Testimony of Comptroller Hawke*].

taken for the part, resulting in an overly-broad and inaccurate definition.[51] A primary distinction between subprime and predatory lending lies in the lender's intent in extending the loan.[52] Predatory lenders profit from intentionally and systematically taking advantage of unsophisticated borrowers, and purposefully structure loans to cause economic harm to the borrower--at a significant profit for the lender.[53] Non-predatory subprime lenders lend with a different intent, that is, to provide valuable credit to individuals with a higher risk of default. The higher interest and foreclosure rates that accompany subprime loans result from the additional risk inherent in lending to an individual with imperfect credit, not from intentional planning on the part of the lender. The substance of "ground level" interactions between the lender and the borrower is often indicative of a lender's intent.[54] Some lenders intentionally seek out vulnerable loan candidates,[55] going so far as to review public property lien records to find homeowners with serious debt.[56] After identifying their victims, these lenders become salesmen, aggressively promoting loans that the frequently desperate borrowers cannot afford.

Predatory lenders prey on the most vulnerable members of society.[57] Their typical victims are financially unsophisticated individuals[58] who are often "disconnected" from the traditional credit

---

51. *See id.*

52. *See* Engel & McCoy, *supra* note 42, at 1260. Engel & McCoy have set forth a list of five characteristics that distinguish predatory lending from legitimate subprime lending:

> 1) loans structured to result in seriously disproportionate net harm to borrowers,
> 2) harmful rent seeking,
> 3) loans involving fraud or deceptive practices,
> 4) other forms of lack of transparency in loans that are not actionable as fraud, and
> 5) loans that require borrowers to waive meaningful legal redress.

Id.

53. *See id.*

54. Williams & Bylsma, *supra* note 1, at 118.

55. Intentionally targeting low-income borrowers for high cost loans is commonly referred to as "reverse redlining." *See* Anne-Marie Motto, Note, *Skirting the Law: How Predatory Mortgage Lenders Are Destroying the American Dream*, 18 GA. ST. U. L. REV. 859, 860-61 (2002).

56. *See* Sandra Block, *Guidelines Can Help Reduce Risk of Foreclosure*, USA TODAY, Sept. 20, 2002, at 3B.

57. *Cf.* ACORN, SEPARATE AND UNEQUAL 2002, *supra* note 40, at 1 (showing that the poor and minorities are victims of predatory lending at significantly higher rates than white and more affluent individuals).

58. *See* Michelle W. Lewis, *Perspectives on Predatory Lending: The Philadelphia Experience*, 12 J. AFFORDABLE HOUS. & CMTY. DEV. L. 491, 508 (2003). Financially

economy,[59] in that they have limited experience with banks and often have not developed an official credit history.[60] Often, these borrowers have relied on the "fringe" credit market: check cashing establishments, pawnshops, and other local businesses that offer credit and limited financial services at significantly higher fees than traditional banks.[61]

Victims of predatory lending are also generally from low-income communities.[62] This is partly because low-income borrowers often seek loans when they are desperate for cash, and may not have the information or ability to properly compare lenders,[63] making them more susceptible to aggressive predatory lenders.[64] In addition, this class of borrowers makes up a greater percentage of the class of victims adversely affected by predatory lenders, because low-income individuals generally have fewer resources than more affluent individuals, and are more liable to default.[65]

B. The Role of the Office of the Comptroller of the Currency

Concerns about the growth of predatory lending abuses prompted action by the OCC,[66] a bureau of the U.S. Department of the Treasury charged with regulating the national banking system.[67] The OCC, under the direction of Comptroller Hawke, charters new banks and has exclusive "visitorial powers" to examine and supervise the affairs of existing national banks.[68] Its primary goal is to maintain stability and fair competition within the banking system.[69] The agency breaks this goal down into four objectives. The first is to ensure the safety and soundness of the national bank-

---

unsophisticated victims fall into three categories: "[T]hose who know too little (who need education and information), those who know too much (who are afraid to ask questions), and those who expect something for nothing (who are attracted to promises of 'buy now, don't pay until 2005')." *Id.*

59. *See* Engel & McCoy, *supra* note 42, at 1281.

60. For purposes of this Comment, "official credit history" refers to an individual's credit history as recorded on their credit report.

61. *See* Engel & McCoy, *supra* note 42, at 1281.

62. *See id.*

63. *Id.* at 1282.

64. *Id.* at 1281-82.

65. *Id.*

66. *See supra* text accompanying notes 5-18.

67. *See* The National Bank Act, 12 U.S.C. § 93 (1864) (authorizing the Comptroller to hire a staff to supervise and examine national banks).

68. *See* 12 U.S.C. § 484(a) (2004).

69. *See About the OCC, at* http://www.occ.treas.gov/aboutocc.htm (last visited Nov. 16, 2004).

ing system.[70] That is, to maintain the financial health of banks and the integrity of the banking system.[71] Second, the agency aims to foster competition by allowing banks to offer new products and services.[72] The third goal is to improve the efficiency and effectiveness of the OCC.[73] Finally, the agency strives to ensure fair and equal access to financial services for all Americans.[74] This Comment focuses on the first and last of these objectives.

The OCC is not the sole federal regulator of the national banking system.[75] The Federal Reserve and the Federal Deposit Insurance Corporation also have regulatory authority.[76] Banks pick their primary regulator when they elect to have either a national or a state charter.[77] The OCC is responsible for the nationally chartered banks,[78] whereas the Federal Reserve and the Federal Deposit Insurance Corporation regulate the state chartered banks.[79] Some commentators believe that this competition influences the substance of banking regulations[80] because banks' ability to choose their regulator creates a competitive atmosphere[81] by "enabl[ing] banking organizations to shop for the most lenient regulator."[82] These commentators believe that this competition fuels a "race to the bottom,"[83] where the regulators, in an attempt to

70. *See id.*

71. Safety and soundness regulations aim to control a bank's exposure to risk, often by imposing financial safeguards such as minimum capital requirements and limitations on risky endeavors. *See* JONATHAN R. MACEY ET AL., BANKING LAW AND REGULATION 75 (3d ed. 2001).

72. *See About the OCC*, *supra* note 69.

73. *Id.*

74. *Id.*

75. *See* MACEY ET AL., *supra* note 71, at 70.

76. *See id.*

77. *See id.* at 75; *see also* John A. Weinberg, *Competition Among Bank Regulators*, 88 FED. RES. BANK RICHMOND ECON. Q. 19 (2002).

78. *See* MACEY ET AL., *supra* note 71, at 70.

79. State chartered banks are also subject to regulation by the state in which they are chartered. *See* Weinberg, *supra* note 77, at 19.

80. *See* MACEY ET AL., *supra* note 71, at 70.

81. *See* Weinberg, *supra* note 77, at 19.

82. MACEY ET AL., *supra* note 71, at 74-75.

83. Weinberg, *supra* note 77, at 20 (discussing how proposals to restructure and consolidate bank regulation are partly based on the idea that regulators are currently engaged in a race to the bottom). *But see* RICHARD J. ROSEN, DO REGULATORS SEARCH FOR THE QUIET LIFE? THE RELATIONSHIP BETWEEN REGULATORS AND THE REGULATED IN BANKING (2001) (explaining that competition can be beneficial, as banks tend to improve their performance following a switch from one regulator to another and that under certain conditions, regulatory competition leads to optimal standard setting), *available at* http://www.chicagofed.org/publications/workingpapers/papers/wp2001-05.pdf.

attract new banks to their constituency and to retain the banks that they already regulate,[84] will comply with industry demands.[85] Commentators claim that this often results in regulations that disproportionately favor the industry at the expense of the agency's interest in managing bank operations[86] and the public interest.[87] The OCC is particularly susceptible to the pressures of competition because, unlike most federal agencies, it is funded entirely by the banks it regulates, in the form of examination fees.[88]

II. THE OCC'S RESPONSE TO THE PREDATORY LENDING PROBLEM

The OCC has made clear its position that predatory lending practices "whether in connection with mortgage lending or other national bank activities . . . have no place in the national banking system."[89] Such practices are inconsistent with the agency's goals of fair access to credit for all Americans, community development and renewal, and increased opportunities for homeownership.[90]

In February 2003, the OCC issued an Advisory Letter addressing its views on predatory lending ("Advisory Letter").[91] The Advisory Letter communicated the OCC's position that predatory lending would not be tolerated in the banking system.[92] It provided banks with notice of what practices the agency considered predatory, and guidlines for avoiding the purchase of predatory loans originated by third parties.[93] It also advised banks as to what lend-

84. *See* Weinberg, *supra* note 77, at 20.

85. *See, e.g., Congressional Review of OCC Preemption: Before the House Comm. on Fin. Servs. Subcomm. on Oversight and Investigations*, 108th Cong. (2004) (statement of Thomas J. Miller, Attorney General of Iowa), *available at* http://financialservices.house.gov/media/pdf/012804tm.pdf.

86. *See* Weinberg, *supra* note 77, at 20.

87. *See* ROSEN, *supra* note 83, at 5.

88. MACEY ET AL., *supra* note 71, at 70. Since the agency's budget depends exclusively on the number of banks it regulates, there is a great incentive for the OCC to make its regulations lenient and favorable to industry, so as not to lose "market share" to another regulator. *Id.* at 75; *see also* Jess Bravin & Paul Beckett, *Dependent on Lenders' Fees, the OCC Takes Banks Side Against Local Laws*, WALL ST. J., Jan. 28, 2002, at A1.

89. Bank Activities and Operations, 12 C.F.R. § 7.4008 (2004); Real Estate Lending and Appraisals, 12 C.F.R. § 34.3 (2004).

90. *See* Office of the Comptroller of the Currency, OCC Advisory Letter 2003-2, Guidelines for National Banks to Guard Against Predatory and Abusive Lending Practices (Feb. 21, 2003) [hereinafter OCC Advisory Letter 2003-2], *available at* http://www.occ.treas.gov/ftp/advisory/2003-2.pdf.

91. *Id.*

92. *Id.*

93. *Id.*

ing practices may be considered unfair and deceptive under Section 5 of the FTC Act.[94] According to the Comptroller, the purpose of the Advisory Letter was to provide guidance "to deal effectively with predatory lending without setting up a rigid system that creates burdens and obstacles to serve low-income customers."[95]

Despite the Comptroller's previous interest in avoiding a "rigid system," the OCC issued the Final Rule on January 7, 2004,[96] contradicting its previously stated intent.[97] The Rule sets forth a single anti-predatory lending standard ("Standard"), which provides that "[a] national bank shall not make a consumer loan . . . based predominantly on the bank's realization of the foreclosure or liquidation value of the borrower's collateral, without regard to the borrower's ability to repay the loan according to its terms."[98] Notably missing from the rule is any reference to the bank's intent in extending the loan. Under the Standard a lender who intends to take advantage of a borrower is treated the same as a lender who lends in the possibly negligent, though earnest, hope that the borrower will be able to fulfill the terms of the loan.

A. Analysis of the Standard and the OCC's Objectives

The OCC relies on two agency objectives in support of its adoption of the Final Rule: the maintenance of the safety and soundness of the national banking system, and the provision of fair and equal access to financial services for all Americans.

---

94. *Id.* According to the Advisory Letter, practices may be labeled deceptive if "[t]here is a representation, omission, act or practice that is likely to mislead; [t]he act or practice would likely mislead a reasonable consumer [in the targeted audience]; and the representation, omission, act, or practice is likely to mislead in a material way." *Id.* In addition, a practice may be labeled unfair for purposes of the FTC Act if "[t]he practice causes substantial consumer injury such as monetary harm; [t]he injury is not outweighed by benefits to the consumer or to competition; and the [i]njury caused by the practice is one that consumers could not reasonably have avoided." *Id.*

95. Press Release, Office of the Comptroller of the Currency, *OCC Issues Guidelines to National Banks to Guard Against Abusive Lending Practices; Invites Comments on Request to Determine that Georgia Law is Preempted* (Feb. 21, 2003), *available at* http://www.occ.treas.gov/scripts/newsrelease.aspx?Doc=EMRDRG7D.xml.

96. The Final Rule amends Bank Activities and Operations, 12 C.F.R. § 7 (2003), and Real Estate Lending and Appraisals, 12 C.F.R. § 34 (2003).

97. Administrative rules promulgated through the notice and comment process (as was this OCC Final Rule) are considered "legislative," are binding as law on the regulated industry, and are given *Chevron* deference during judicial review. *See* Chevron U.S.A. Inc., v. Natural Res. Def. Council, Inc., 467 U.S. 837 (1984). By contrast, Advisory Letters are nonbinding and do not carry the force of law.

98. 12 C.F.R. §§ 7.4008, 34.3.

1. *Principles of Safety and Soundness*

The OCC relied upon a safety and soundness rationale for preempting state regulation of national banks. The Comptroller stated that

> "[w]hen national banks are unable to operate under uniform, consistent and predictable standards, their business suffers and so does the safety and soundness of the national banking system . . . . The application of multiple and often unpredictable state laws interferes with their ability to plan and manage their business, as well as their ability to serve the people . . . and the economy of the United States."[99]

Safety and soundness goals are common to all of the federal bank regulators.[100] In general terms, maintaining safety and soundness refers to maintenance of the financial health of banks and the integrity of the banking system.[101] Safety and soundness regulations aim to control a bank's exposure to risk, often by imposing financial safeguards such as minimum capital requirements, limitations on risky lending, and other safeguards.[102]

The OCC also relied on a safety and soundness rationale for adopting the Standard. The press release that accompanied the Final Rule states: "The prohibition on basing loans on the foreclosure value of the borrower's collateral is grounded in safety and soundness principles."[103] As applied to predatory lending, the OCC takes the position that loans extended with the expectation of foreclosing on the borrower's collateral for repayment are inherently unsafe and unsound[104] because loans extended in reliance on the foreclosure value of the borrower's collateral carry a greater risk of default than loans extended after a careful calculation of the borrower's ability to repay through future income and other financial resources.[105] The OCC believes that repeat origination or purchase of such loans from brokers would constitute a threat to the safety and soundness of the banking system because these loans carry a high risk of default,[106] and defaults expose a bank to loss when the sale of the collateral does not cover the balance of

99. OCC Final Rule Press Release, *supra* note 12.
100. *See* MACEY ET AL., *supra* note 71, at 75.
101. *Id.*
102. *Id.*
103. OCC Final Rule Press Release, *supra* note 12.
104. Bank Activities and Operations, 12 C.F.R. § 7.4008 (2004); Real Estate Lending and Appraisals, 12 C.F.R. § 34.3 (2004).
105. OCC Final Rule Press Release, *supra* note 12.
106. OCC Advisory Letter 2003-2, *supra* note 90.

the loan after accounting for all the costs associated with liquidation.[107] Yet, while safety and soundness concerns may justify the preemption of state laws, they do not justify the adoption of the Standard. Predatory lending is not prevalent in the national banking system, and therefore is not a significant threat to its Safety and Soundness. Furthermore, application of the Standard will not prohibit most predatory lending practices.

a. Most National Banks Are Not Engaged in Predatory Lending

Many American communities are plagued by predatory lending,[108] but national banks are not the primary offenders because most national banks do not originate predatory loans.[109] According to the Comptroller, there are only "isolated cases of abusive practices"[110] among regulated banks.[111] The Standard is a "preventative measure," to ensure regulated banks do not become involved in predatory lending.[112]

The OCC has also expressed concerns that national banks could inadvertently facilitate predatory lending by purchasing predatory loans from brokers and other third parties.[113] This is a legitimate concern and was addressed by the OCC in its February 2003 Advisory Letter.[114] The Advisory Letter outlined common abusive lending practices and advised banks to exercise caution in purchasing brokered and third party originated loans.[115] The OCC urged national banks only to do business with companies that have strong anti-predatory lending policies in connection with loans they sell or pool for securitization.[116]

---

107. *Id.*

108. *See generally*, ACORN, SEPARATE AND UNEQUAL 2002, *supra* note 34 (documenting the increase in predatory lending that has accompanied increased subprime lending).

109. *See* James M. Rockett, *Contradictory Laws*, NAT'L L.J., Dec. 1, 2003, at 47 (stating that consumer advocates do not cite national banks as predatory lenders); *see also Spitzer Threatens to Sue U.S. Regulator Over Loan Exemption*, N.Y. TIMES, Dec. 11, 2003, at C7 ("According to [a spokesman for the OCC] most of the predatory lending occurs among non-bank institutions"). *But see* Michael Hudson, *Banking on Misery: Citigroup, Wall Street, and the Fleecing of the South*, S. EXPOSURE (2003) (discussing Citigroup's involvement in predatory lending), *available at* http://www.southernstudies.org/reports/bankingonmisery.pdf.

110. OCC Final Rule Press Release, *supra* note 12.

111. *But see* Hudson, *supra* note 109 (noting charges of predatory lending against Citigroup).

112. *See* OCC Final Rule Press Release, *supra* note 12.

113. *See* OCC Advisory Letter 2003-2, *supra* note 90.

114. *Id.*

115. *Id.*

116. *Id.*

b. Application of the Standard Will Not Prohibit Most Predatory Lending Practices

For those isolated cases where national banks engage in predatory lending,[117] the Standard will do little to stop them. As discussed earlier, defining predatory lending is difficult because it consists of a multitude of abusive lending practices.[118] Application of the Standard will only prohibit one practice, equity stripping, where a lender extends a loan to a borrower who has no reasonable means to repay, and upon the anticipated default, the lender forecloses on the collateral and strips whatever equity remains in the property.[119] Comptroller Hawke has referred to equity stripping as "the most egregious aspect of predatory lending,"[120] because it involves a deliberate seizure of the borrower's collateral and the valuable equity therein. A lender, who is aware that the borrower cannot afford the loan but extends the loan anyway, anticipating the borrower's default, is in clear violation of the Standard.

Application of the Standard will do little to prohibit other predatory practices in secured lending. It will not prohibit lenders from charging unjustifiably high interest rates and service fees, so long as it is reasonable for the bank to believe that the borrower will be able to repay the loan from future income. For the same reason, the Standard will not affect loan packing, a practice in which credit insurance premiums are incorporated into the principal and financed over the span of the loan.[121] (This practice is labeled predatory when the lender either does not inform the borrower of the cost of the insurance and/or that it is optional.)[122] Similarly, it will have no effect on negative amortization, where the borrower's principal balance increases monthly because the scheduled payments are so low that they do not cover the monthly interest.[123] In effect, onerous terms are permissible according to the OCC rule, so long as the borrower can afford the monthly payments. Yet all

117. *See, e.g.*, Hudson, *supra* note 109.

118. *See supra* notes 30-36 and accompanying text.

119. *See id.*

120. Statement of Comptroller of the Currency John D. Hawke, Jr. Regarding the Issuance of Regulations Concerning Preemption and Visitorial Powers (Jan. 7, 2004) [hereinafter Statement of Comptroller Hawke], *available at* http://www.occ.treas.gov/2004-3aComptrollersstatement.pdf.

121. *See* Motto, *supra* note 55, at 864 ("[O]ne noted subprime lender sets quotas on credit insurance, which is 'pure profit,' mainly because the lender itself underwrites it.").

122. *See id.*

123. *See id.* at 865.

these practices are predatory; they take advantage of the borrower, jeopardizing his financial welfare, at a significant profit for the lender.[124]

The OCC may be able to take action against such behaviors under its FTC Act enforcement authority,[125] if they qualify as unfair and deceptive trade practices under that Act.[126] Yet, the effect of this authority is questionable. Under the Act, the Federal Reserve Board has exclusive authority to promulgate regulations against unfair and deceptive banking practices.[127] The OCC merely has enforcement authority, the power to sanction national banks for violating the Act.[128] Whether this authority will effectively prohibit those types of predatory lending that are not proscribed by the Standard depends largely on the OCC's use of the authority. Strict enforcement of the Act is unlikely, because as noted earlier, the competitive nature of banking regulation creates a strong financial incentive for the OCC to support lenient regulation as it derives all of its funding from the banks it regulates.[129]

Moreover, application of the Standard will not prohibit predatory lending practices in unsecured lending. The Standard provides that banks cannot grant a loan based predominantly on the "foreclosure or liquidation value of the borrower's collateral, without regard to the borrower's ability to repay."[130] Therefore, the Standard requires banks to investigate a borrower's ability to repay the loan from income only when the bank is extending a *secured* loan.[131] The Standard is inapplicable to unsecured loans.[132] Accordingly, a bank can be in full compliance with the Standard yet make unsecured loans to individuals who have no foreseeable means to repay the debt.[133]

2. *Fair and Equal Access to Financial Services for All Americans*

To further support the regulation, OCC representatives have stated that the Standard is consistent with the agency's fair and

124. *See* Engel & McCoy, *supra* note 42, at 1261 (explaining that loans structured to result in serious financial harm to the borrower are predatory).
125. 12 C.F.R. §§ 7.4008(c), 34.3(c).
126. 15 U.S.C. 45(a)(1).
127. *Id.*
128. 12 C.F.R. §§ 7.4008(c), 34.3(c).
129. *See supra* text accompanying notes 80–88.
130. *See* 12 C.F.R. §§ 7.4008(b), 34.3(b).
131. *Id.*
132. *Id.*
133. *Id.*

equal access objectives and will not adversely affect access to financial services.[134] Comptroller Hawke argues that application of the Standard will deal with the predatory lending problem without impeding access for low-income borrowers to legitimate subprime credit.[135] Hawke has also stated that predatory lending practices are inconsistent with the OCC's fair-lending goals,[136] because they are often discriminatory. Low-income individuals, minorities, and the elderly are the most vulnerable to aggressive lending tactics and are often specifically targeted by predatory lenders.[137] By combating predatory lending, the OCC hopes to reduce this discrimination within the banking system,[138] but by squeezing banks to prevent predatory lending, the OCC may unintentionally foster the growth of predatory lending in minority communities.

a. The Pre-Standard Condition: An Unequal Distribution of Financial Services

Individuals seeking subprime loans often do not have access to legitimate subprime loans from banks for two reasons: banks often do not service low-income neighborhoods,[139] and those banks with branches in low-income neighborhoods often do not offer subprime loans.[140] According to a study by the Association of Community Organizations for Reform Now ("ACORN"), banks have effectively abandoned low-income and minority communities.[141] The study analyzed Federal Reserve data, and found that the number of branch offices in low and lower-middle class neighborhoods fell twenty-one percent from 1975 to 1995, while the total number of banks rose twenty-nine percent during that same time.[142] Physi-

134. *See* Press Release, Office of the Comptroller of the Currency, *OCC Takes Steps to Keep Abusive Practices Out of National Banking System While Ensuring Continued Access to Credit for Low-Income Americans* (July 31, 2003), *available at* http://www.occ.treas.gov/scripts/newsrelease.aspx?Doc=9YWB2OJB.xml.

135. *Id.*

136. *See Testimony of Comptroller Hawke, supra* note 50.

137. *See, e.g.*, Calomiris & Litan, *supra* note 47; Motto, *supra* note 55, at 860-61; *Spitzer Threatens to Sue U.S. Regulator Over Loan Exemption*, *supra* note 109.

138. *See Spitzer Threatens to Sue U.S. Regulator Over Loan Exemption*, *supra* note 109.

139. *See* ACORN, SEPARATE AND UNEQUAL 2002, *supra* note 40.

140. Despite the growth of subprime lending, some banks remain cautious and often unwilling to originate subprime mortgage loans. *See* Office of the Comptroller of the Currency, OCC Working Paper, Economic Issues in Predatory Lending, July, 2003 [hereinafter OCC Working Paper], *available at* http://www.occ.treas.gov/workingpaper.pdf.

141. ACORN, SEPARATE AND UNEQUAL 2002, *supra* note 40.

142. *Id.*

cal presence is important; the study notes that "the proximity of a bank's branches to low and moderate income neighborhoods is directly related to the level of lending made by the bank in those neighborhoods."[143]

Furthermore, national banks are not major players in the subprime market.[144] Most subprime lenders are non-bank mortgage and finance companies that are not regulated by the OCC[145] (and aside from consumer protection laws, are subject to little federal regulation). A report by the Department of Housing and Urban Development ("HUD") shows that in 2001 only twenty percent of the lenders whose business focus was subprime mortgage lending were banks or their affiliates.[146] Banks are cautious of extending subprime credit, either because bank management is risk averse or because they fear potential damage to the bank's reputation if they lend to higher risk customers.[147]

While finance companies and non-bank mortgage lenders extend the majority of subprime credit,[148] some banks have realized the value in subprime lending.[149] The Center for Responsible Lending ("CRL") disagrees with the HUD analysis, stating "many of the depository institutions doing *primarily* prime lending are also doing some subprime lending. Given that many national banks are prime mortgage originators, a national bank could be a large subprime lender without being classified as such by HUD."[150] The predatory non-bank lenders, however, are present and thriving.

---

143. *Id.*

144. *See* OCC Working Paper, *supra* note 140, at 4 (noting that in 2001 there were 178 subprime mortgage lenders, and only 36 were banks or their affiliates); *see also* Litan, *supra* note 46, at 6 (documenting the market share for the top twenty largest subprime lenders for first quarter of 2002). Citigroup, however, is an exception to this generalization. *See generally* Hudson, *supra* note 109 (documenting Citigroup's involvement in predatory subprime lending).

145. *See* OCC Working Paper, *supra* note 140, at 5.

146. *Id.* at 4.

147. *See* Litan, *supra* note 46, at 5. Bank management is also wary of the increased safety and soundness regulatory scrutiny that comes along with charging higher interest rates and the increased foreclosure rates that often accompany subprime lending. *Id.*; *see also* OCC Working Paper, *supra* note 136, at 4.

148. *See supra* notes 144-52 and accompanying text.

149. Litan, *supra* note 40, at 4. Banks are becoming increasingly more involved in the subprime market. *Id.* For the first quarter of 2002 only one of the top five subprime lenders, comprising approximately sixty percent of the market share, was a bank. *Id.* That bank, however, holds over twenty-one percent of the market share. *Id.*

150. Center for Responsible Lending, *Comments on OCC Working Paper*, at 7, *available at* http://www.predatorylending.org/pdfs/CRLCommentsonOCCWorking Paper.pdf.

b. The Standard May Further Impede Access to Legitimate Subprime Credit

The OCC is aware that many state anti-predatory lending laws have had the unintended effect of making non-predatory credit inaccessible for many creditworthy subprime borrowers.[151] In an analysis of the effect of state anti-predatory lending laws on national banks, both OCC and independent empirical studies document the fact that these laws restrict the availability of credit to subprime borrowers.[152] Specifically, after the enactment of North Carolina's anti-predatory lending law in 1999,[153] the origination of subprime mortgages in North Carolina decreased by fourteen percent,[154] and fell fifty percent for borrowers with incomes below $25,000.[155] Similarly, Chicago's anti-predatory lending drove many seeking a subprime mortgage into the non-bank sector,[156] and in Philadelphia, a law targeting predatory lenders caused many legitimate subprime lenders to withdraw from the market.[157]

The agency used these unintended effects of state anti-predatory lending laws as support for its decision to preempt state regulation of national banks.[158] The OCC's position is that they were "avoid[ing] the overbroad and unintended adverse effects of . . . one-size-fits-all [state] laws."[159] The OCC, however, has failed to explain why the federal Standard will not similarly affect access to legitimate subprime credit.

In addition to the geographic unavailability of banks, and the general reluctance of banks to make subprime loans, application of

---

151. *See* Hawke, *supra* note 34; *see also* OCC Working Paper, *supra* note 140, at 20.

152. *See* ACORN, SEPARATE AND UNEQUAL 2002, *supra* note 40.

153. N.C. Sess. Law 1999-332 at §§ 1-5.

154. Gregory Elliehausen & Michael Staten, Credit Research Center Working Paper No. 66, *Regulation of Subprime Mortgage Products: An Analysis of North Carolina's Predatory Lending Law* (Nov. 2002), *available at* http://www.msb.edu/prog/crc/pdf/RevisedWP66.pdf.

155. *See* Calomiris & Litan, *supra* note 47. *But see* ROBERTO G. QUERCIA ET AL., THE IMPACT OF NORTH CAROLINA'S ANTI-PREDATORY LENDING LAW: A DESCRIPTIVE ASSESSMENT (2003) (arguing that there was no reduction in access to credit for subprime borrowers as a result of North Carolina's laws), *available at* http://www.kenanflagler.unc.edu/assets/documents/CC_NC_Anti_Predatory_Law_Impact.pdf.

156. Hawke, *supra* note 34.

157. *Id.*

158. *See id.* According to Comptroller Hawke, "[in] preemption situations, the only relevant issue is whether the state law would impair or interfere with the national bank's exercise of powers granted to it under federal law. If such an impact is found to exist, federal law must prevail." *Id.*

159. *Id.*

the Standard may act as an additional obstacle to legitimate subprime credit. It has the potential to prohibit access to bank loans for an entire class of individuals; those borrowers with equity in their homes, or other valuable collateral, but with low incomes.

Recall the story about Mr. Campbell in the Prologue.[160] He is a prime example of an equity-rich, cash-poor individual who, because of the new federal Standard, will not have access to subprime credit from national banks. A bank complying with the Standard might well deny his application for a loan, notwithstanding the considerable equity in his home. First, even if the bank reasonably believed that despite Mr. Campbell's low income he would be able to make the payments on the loan, loan officers might be reluctant to grant the loan to prevent any appearance that they were basing the loan on the foreclosure value of his home. Extending a loan to a borrower on a fixed income would send out a red flag for closer OCC scrutiny of the bank's lending practices. Banks do not want to risk an OCC audit, or be labeled a predatory lender, even if only for the interim during an investigation; the effect could be devastating and cause them to lose prime market customers.

Second, if the bank extended the loan, and was later forced to foreclose on Mr. Campbell's home, an OCC investigation could potentially reach a different conclusion than the bank as to Mr. Campbell's ability to repay the loan from income. In hindsight, an examination into the ability of a low-income individual to pay from his income would seem questionable, especially in the case of many low-income individuals who face unexpected interruptions in their cash flow. For example, suppose circumstances arose where the Social Security administration stopped Mr. Campbell's SSI checks on the mistaken grounds that he was no longer disabled. Mr. Campbell would lose his sole source of income, and have no option but to default on the loan. The question is whether OCC examiners would consider such an interruption in income foreseeable, and conclude that the bank provided the loan despite Mr. Campbell's uncertain future income.

The OCC's goal in adopting the Standard is to prohibit the "most egregious" type of predatory lending: loans where the lender grants the loan with the intent of foreclosing on the borrower's collateral.[161] The potential result, however, will be to effectively ban loans to otherwise eligible subprime borrowers who, despite low incomes, have collateral that would traditionally support a loan.

160. *See supra* notes 2-8 and accompanying text.

161. *See* Statement of Comptroller Hawke, *supra* note 114.

This cannot be reconciled with the OCC's objective of ensuring fair and equal access to financial services for all Americans, at least as it applies to low-income Americans.

c. The Potential to Increase Predatory Lending

The institutional denial of credit to this class of subprime borrowers creates a larger pool of potential victims for the unscrupulous lenders. When denied a bank loan, desperate borrowers turn to the non-bank lenders, concentrated in low-income and minority communities.[162] A study by HUD found that subprime lending is three times more prevalent in low-income communities than higher income communities.[163] Since these non-bank lenders are not subject to federal oversight and examination, there exists a great potential for abuse.[164] According to the ACORN study, predatory lenders systematically rely on banks to deny credit to large numbers of low-income individuals;[165] they have found their niche.

III. PROPOSAL FOR OCC INTERPRETATION AND ENFORCEMENT OF THE STANDARD

The OCC has broad discretion to interpret and apply the Standard as it sees fit. As noted by one commentator, the results of the regulation "will only be known as the examiners roll into banks and . . . give [it] practical definition."[166] While there is some comfort in having a single federal standard, substitution of the OCC's Standard to replace state anti-predatory lending laws may have the negative consequence of reducing access to subprime credit. In order to ameliorate this problem, the OCC should narrowly construe the Standard so that it only prohibits intentional equity stripping without preventing legitimate asset-based lending to low-income borrowers.

Not all risk-priced, asset-based loans should be labeled predatory, and it is important for homeowners to benefit from the equity in their homes and use it to meet their credit needs. The OCC has the authority to interpret and apply the Standard as it deems appropriate. The OCC should focus less on how the bank calculated

162. *See* Press Release, U.S. Dep't of Hous. and Urban Dev., *Unequal Burden in Atlanta: Income and Racial Disparities in Subprime Lending* (2000), *available at* http://www.hud.gov/library/bookshelf18/pressrel/subpratl.html. HUD performed similar studies in Baltimore, Los Angeles, New York, and Chicago. *Id.*

163. *See id.*; *see also* OCC Working Paper, *supra* note 140, at 2.

164. *Testimony of Comptroller Hawke*, *supra* note 50.

165. *See* ACORN, SEPARATE AND UNEQUAL 2002, *supra* note 40.

166. Rockett, *supra* note 109.

the borrower's eligibility and how heavily the bank relied upon the borrower's collateral, and instead construe the Standard so that it prohibits only intentional equity stripping, where the lender had the requisite bad intent and "an eye out" to take the borrower's home.

Addressing the difficulties that exist in assessing a bank's intent in extending a loan, I propose that the OCC take the following factors into consideration when examining a bank's compliance with their anti-predatory lending standard:

1. *The time lapse before foreclosure.*

A relatively short period of time between origination of a loan and foreclosure may be an indication that the loan was not based predominantly on the borrower's ability to repay the loan from future income, and that the bank relied too heavily on the value of the borrower's collateral. According to a study documenting trends in loan foreclosures in Boston, the median age of subprime loans at foreclosure is three years.[167] The OCC should conduct a similar survey to determine a span of time before foreclosure that is characteristic of a predatory loan.

2. *The forseeability of an interruption to income.*

When examining a bank's investigation into the borrower's ability to repay the loan from future income, the OCC should not hold the bank responsible for unforeseeable future interruptions to the borrower's income. The determination should be made based on the information available to the bank at the time it extended the loan. Furthermore, the OCC should give deference to the bank's determination, made before extending the loan, regarding a borrower's ability to repay the loan from his future income. Since banks co-exist with their customers, they are better able to assess their customers' present and anticipated future financial situations than remote federal regulators.

3. *Whether the borrower was well informed before entering into the loan agreement.*

As noted earlier, one characteristic that distinguishes predatory lending from legitimate subprime lending is what happens at

167. *See* DEBBIE GRUENSTEIN & CHRISTOPHER E. HERBERT, ANALYZING TRENDS IN SUBPRIME ORGANIZATIONS AND FORECLOSURES: A CASE STUDY OF THE BOSTON METRO AREA (2000), *available at* http://www.abtassociates.com/reports/2000804000192_87267.pdf.

"ground level" interactions between the borrower and the lender.[168] The OCC should investigate whether the borrower was informed of, and understood, the terms of the loan. While unsophisticated borrowers are not expected to have a comprehensive understanding of a complex loan agreement, the lender should be charged with a duty to ensure that the borrower has a basic understanding of his obligations under the agreement and the consequences of default. A lender who fails to ensure that the borrower has this minimal level of understanding is engaging in behavior illustrative of predatory intent.

CONCLUSION

The OCC's anti-predatory lending standard, which preempts state lending laws, places an unjustifiable restriction on the ability of banks to extend loans to low-income individuals. By restricting access to legitimate bank loans, application of the Standard may effectively increase the predatory lending problem outside of the national banking system, as borrowers are forced to seek credit in the largely unregulated non-bank lending market, where predatory lending is rampant. In addition, the efficacy of replacing state anti-predatory lending laws with a single federal standard is questionable. The consequences of the regulation depend in large part upon the OCC's interpretation and enforcement of the Standard. Thus, the OCC should interpret the Standard so that it does not prohibit banks from extending loans to all low-income borrowers, and prohibits only those loans extended with an intent to foreclose on the borrower's collateral.

168. *See supra* note 48 and accompanying text.