Agency Proposals Reject *Madden* Holding: Six Things To Know

On November 18 and 19, 2019, the Office of the Comptroller of the Currency (OCC) and Federal Deposit Insurance Corporation (FDIC) provided long-awaited regulatory affirmation that a bank loan's rate of interest retains its non-usurious character when acquired by a third-party. The agencies each issued proposed rules that seek, as the OCC put it, to "codify what the OCC and the banking industry have always believed and address recent confusion about the impact of an assignment on permissible interest." In particular, the proposals would clarify that the interest charged on a loan that is permissible when the loan is made remains valid despite any sale, assignment, or other transfer of the loan (or, in the case of the FDIC proposal, a change in state law). The proposals bring the agencies' interpretive expertise to bear on an issue that was in flux after *Madden v. Midland Funding, LLC*, 786 F.3d 246 (2015), a Second Circuit decision that declined to recognize the "valid-when-made" doctrine.

1 The proposals respond to the Second Circuit's decision in *Madden*.

The proposals resulted primarily from the uncertainty and confusion wrought by the *Madden* decision, which had concluded – contrary to the "valid-when-made" doctrine – that a nonbank purchaser of a loan issued by a national bank could not rely on the original interest rate because it violated the borrower's home state's usury laws. The clarity that the proposals would provide serves an important interest given that some have argued that *Madden* could negatively impact loan sales for any purpose including securitization activity.

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2 The proposals interpret parallel statutes.

Although the proposals would ultimately produce similar results, they interpret different federal statutes. The OCC's rule would interpret section 85 of the National Bank Act, 12 U.S.C. § 85, and section 4(g) of the Home Owners' Loan Act, 12 U.S.C. § 1463(g), which govern permissible rates of interest (and interest rate exportation) by national banks and federal and state savings associations, respectively. The FDIC's rule, on the other hand, would interpret section 27 of the Federal Deposit Insurance Act, 12 U.S.C. § 1831d, which governs permissible rates of interest (and interest rate exportation) by state banks, and was modeled after and has been construed in the same manner as section 85 of the National Bank Act.

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3 The FDIC proposal would align with the OCC's interest rate exportation regulations, including its definition of interest.

The OCC's proposal would amend 12 C.F.R. § 7.4001, which generally sets forth the circumstances in which a national bank may charge the maximum rate of interest permitted in its home state for purposes of section 85 of the National Bank Act, and 12 C.F.R. § 160.110, which does the same for savings associations. The FDIC's proposal would adopt a new Part 331 to the FDIC's regulations that would not only address the valid-when-made doctrine, but also, like the existing OCC regulations, provide more general guidelines as to when a state bank may charge the maximum rate of interest permitted in its home state under section 27 of the Federal Deposit Insurance Act. if finalized as proposed, the FDIC and OCC rules regarding the charging of interest would be substantively identical. The FDIC proposal would also implement section 24(j)(1) of the Federal Deposit Insurance Act, 12 U.S.C. § 1831a(j)(1), by including provisions regarding the applicability to state banks' out-of-state branches of host state laws.

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4 Though they take different paths, the proposals seek similar results.

The OCC emphasized that its proposal simply seeks to codify the "valid-when-made" principle that has been well established in federal common law for over a century. The FDIC, however, asserted that the permissibility of interest must be determined when the loan is made, not because of the common law "valid-when-made" principle, but because such a rule protects the parties' expectations and reliance interests and promotes the safety and soundness of banks seeking to generate liquidity or reduce concentrations by selling loans.

5 The proposals could help stabilize the market for bank loans.

If finalized, the agencies' proposals could provide more legal certainty. In particular, if in the event the rules are challenged and courts defer to the agencies' interpretations of federal law under the *Chevron* doctrine, the proposals would not only affirm (whether explicitly or implicitly) the "valid-when-made" doctrine but also stabilize the expectations of banks, investors, debt collectors, fintech partners (including marketplace lenders, which the FDIC proposal specifically mentions), and consumers.

6 The proposals leave the "true lender" question for another day.

The proposals specifically declined to address the related "true lender" issue – that is, the question of which party is the true lender when a bank makes a loan in partnership with a third party that may be responsible for interacting with the borrower and may acquire the loan. The proposals do, however, acknowledge that courts have been grappling with this issue – for example, in the *Meade v. Avant of Colorado, LLC* case.

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