DREHER TOMKIES LLP

ALERT

FOR CLIENTS AND FRIENDS OF DREHER TOMKIES LLP

February 16, 2022

FDIC WINS ITS "MADDEN-FIX" LAWSUIT

Following its ruling upholding the OCC's *Madden*-fix rule, the District Court for the Northern District of California has likewise ruled in favor of the Federal Deposit Insurance Corporation's ("FDIC") cross-motion for summary judgment, upholding the FDIC's parallel Madden-fix rule. *See* Order Resolving Cross-Motions for Summary Judgment, *California v. Federal Deposit Insurance* Corporation, No. 20-cv-05860-JSW (N.D. Cal. filed Feb. 8, 2022); *see also* our ALERT of Feb. 10, 2022. In 2020, seven states and the District of Columbia ("Plaintiffs") sued the FDIC challenging the validity of the FDIC's rule, titled *Federal Interest Rate Authority Rule* ("Rule"), that was promulgated in the wake of the U.S. Court of Appeals for the Second Circuit's ruling in *Madden v. Midland Funding, LLC*, 786 F.3d 246 (2d Cir. 2015), *cert. denied*, 136 S. Ct. 2505 (2016). *See* our ALERTS of Sep. 26, 2019 and June 26, 2020. The FDIC's Rule similarly provides that the determination regarding the permissibility of interest on a loan occurs as of the date the loan was made and will not be affected by the sale, assignment or other transfer of a loan. 12 C.F.R. § 331.4(e).

Section 27 of the Federal Deposit Insurance Act grants federally insured state-chartered banks ("FDIC Banks") the same privilege as national banks to export their home state's interest rate to states where their borrowers live "in order to prevent discrimination against [FDIC Banks] with respect to interest rates." 12 U.S.C. § 1831d(a); *see Greenwood Trust Co. v. Massachusetts*, 971 F.2d 818, 827 (1st Cir. 1992). States may opt out of Section 27; if a state opts out, FDIC Banks making loans in that state could not charge interest exceeding the opt-out state's rate cap. *Id.* § 1831d, note.

The FDIC argued that it promulgated the rule to address: (i) a statutory gap in Section 27 regarding "the time at which the validity of an interest rate should be assessed" ("timing gap"), (ii) a statutory gap in Section 27 regarding "the components of the right to make loans at rates permitted by an FDIC Bank's home state, including the impact of transfer on the validity of a loan" ("transfer gap") and (iii) the uncertainty created by the *Madden* decision regarding "the ability of an assignee to enforce the interest rate provisions of a loan originated by a bank."

Finding that *Chevron* deference applies, the court turned to plaintiffs' argument that there were no statutory gaps to fill because Section 27 unambiguously applies only to FDIC Banks while they hold loans. The court disagreed, finding nothing in the text of Section 27 that speaks to either of the issues addressed in the Rule. Additionally, the court incorporated relevant portions of its decision in the preceding OCC "Madden-fix" case, holding that because Section 27 was modelled on Section 85 of the National Bank Act and the two statutes have always been construed together, plaintiffs' repeated argument that the statutes speak to interest rates on loans rather than entities is unpersuasive. The court stated that the FDIC's interpretation of Section 27, which is "consistent with" the valid-when-made principle (which the court agreed was subject to argument), was not arbitrary or capricious or manifestly contrary to the law because, in part, it is "consistent with" the principle than an assignee steps into the shoes of an assignor.

Lastly the court addressed plaintiffs' argument that the Rule was arbitrary and capricious under *State Farm*, which provides that rules promulgated by administrative agencies are arbitrary and capricious if the agency entirely failed to consider an important aspect of the problem. Plaintiffs asserted that the FDIC failed to consider the impact of the rule on "rent-a-bank schemes" and, relatedly, how the "true lender" doctrine will apply to the Rule. The FDIC indicated that it considered the true lender issue, but ultimately determined that the issues were not so intertwined that they must be addressed simultaneously, as non-banks are not always involved in making loans. Likewise, the FDIC indicated that if states are concerned with "rent-a-bank schemes", they can opt-out of Section 27. Because the FDIC did not fail to consider an important aspect of the problem, the court held that the Rule is not arbitrary and capricious under *State Farm*.

This decision is another major win for the financial services industry, even though it may be subject to appeal. The court reinforces both the contractual principle of assignees stepping into the shoes of their assignors and the concept that, where parallel, federal regulation of state banks and national banks should be construed together, granting state banks the same privileges as national banks. Nonbank lenders and creditors can hope that further judicial recognition of this principle may put to bed future *Madden*-like challenges; however, states may choose to opt-out of Section 27 or impose restrictions on assignees, such as "holder" licensing, in an attempt to regain control of interest rates within the state. ❑

✧ *Mike Tomkies and Mercedes Ramsey*

Darrell L. Dreher
ddreher@dltlaw.com

Elizabeth L. Anstaett
eanstaett@dltlaw.com

Nathan D. Copeland
ncopeland@dltlaw.com

Susan L. Ostrander
sostrander@dltlaw.com

2750 HUNTINGTON CENTER
41 S. HIGH STREET
COLUMBUS, OHIO 43215
TELEPHONE: (614) 628-8000 FACSIMILE: (614) 628-1600
WWW.DLTLAW.COM

Michael C. Tomkies
mtomkies@dltlaw.com

Benjamin J. Hurford
bhurford@dltlaw.com

Mercedes C. Ramsey
mramsey@dltlaw.com

Judith M. Scheiderer
jscheiderer@dltlaw.com

Robin R. De Leo
robin@deher-la.com