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Charles M. Horn
Melissa R.H. Hall

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THE CURIOUS CASE OF MADDEN V. MIDLAND FUNDING AND THE SURVIVAL OF THE VALID-WHEN-MADE DOCTRINE

CHARLES M. HORN AND MELISSA R. H. HALL*

I. INTRODUCTION

In May 2015, the U.S. Court of Appeals for the Second Circuit handed down a curious decision, Madden v. Midland Funding, LLC,\(^1\) that many in the banking industry believe has challenged a longstanding and fundamental principle of American bank usury law, namely, the principle of “valid-when-made.” This principle says, in simple terms, that a loan or contract with a non-usurious interest rate when it is made cannot become usurious if the loan or contract subsequently is transferred to another person, even if the interest rate would have been usurious if the transferee originated the loan. In Madden, however, the Second Circuit, apparently disregarding the valid-when-made principle, concluded that a defaulted and uncollected credit card debt originated and later sold by a national bank to a debt collector that carried an interest rate that was permitted under the usury laws of the bank’s home state, may have become usurious under the laws of the debtor’s home state or governing law of the state specified in the credit card agreement when the debt collector sought to collect on the debt. By effectively invalidating the collection of post-default interest on a lawful loan agreement by reason of its transfer, Madden has created substantial uncertainty in the reliability of the valid-when-made doctrine in the Second Circuit. The outcome of the Madden decision involves a somewhat specific interaction of usury and federal preemption principles, discussed below, that may not necessarily be broadly

* Mr. Horn is a Partner and Ms. Hall is Of Counsel in the Washington, D.C. office of Morgan, Lewis & Bockius LLP. The authors would like to thank Shawn Tang for his assistance in drafting this article.

replicated in many types of commercial and consumer loan transactions. *Madden*, however, has cast at least a temporary pall on loan sales and trading activity, and has forced bank and nonbank buyers and sellers of loans to review critically their loan sales and trading policies and procedures, and in many cases revise their business practices.

The ultimate issue that *Madden* raises, however, is how far-reaching are its holdings and their ramifications, and whether the decision will materially affect the interpretation and application of longstanding principles of usury and the validity of loan agreements that are integral to banking transactions and bank lending activities. If, for example, banks cannot sell their loans to third parties without the collectability of those loans being called into question on usury grounds, the legal and commercial landscape for loan origination and sales activities would become, at the very least, materially less predictable. Or, if securitizers of loan pools cannot reasonably assure their investors that the terms of their pooled loans are enforceable according to their terms, what implications will that have for the loan markets in general?

Our goal in this Article is to explore the facts and holdings of *Madden*, and its short-term and longer-term legal and commercial implications. In doing so, we conclude that *Madden* was wrongly decided due to a misplaced primary focus by the defendants on federal bank preemption principles, causing the Second Circuit to all but ignore the valid-when-made doctrine. Although *Madden* is having an adverse short-term impact,2 we believe that ultimately it will be properly limited in its scope and impact,3 will not be embraced across the board by other state or federal courts,4 and will not result in significant changes to the law and principles of bank lending and usury.5 In other words, notwithstanding the *Madden* decision, the valid-when-made doctrine should remain alive and well.

II. THE INGREDIENTS OF *MADDEN*

Before discussing the *Madden* case itself, we will discuss the legal principles at issue in *Madden* to assist in understanding the
specifics and implications of the decision.

A. A Brief Introduction to the Law of Usury

Although the case law on usury, for a variety of reasons, is extensive and can be complex, the basic concept of usury is straightforward, namely, that the charging of an excessive ("usurious") interest rate on a loan is illegal. Importantly, under our U.S. federal system, the regulation of usury is left to the states, and each state addresses the issue by establishing a maximum interest rate that may be charged on loans that a state decides should be subject to the maximum rate cap. Predictably, there is a wide variation among the states as to what interest rate is "excessive," what types of loans are covered by the usury limits, and the legal consequences of making a usurious loan. And, complicating the usury question is the fact that usury limits may have exceptions for certain types of businesses (e.g., banks, pawnbrokers, licensed nonbank lenders) or types of loans (e.g.,

6. The modern law and practice of usury have longstanding moral, religious, and philosophical underpinnings, which more recently have been supplemented by contemporary notions of consumer protection and fairness. In religious terms (primarily Christian, Judaic, and Islamic), usury is viewed as a sin. See, e.g., Exodus 22:25 (King James) ("If thou lend money to any of my people that is poor by thee, thou shalt not be to him as an usurer, neither shalt thou lay upon him usury."); Leviticus 25:36, 37 (King James) ("Take thou no usury of him, or increase: but fear thy God; that thy brother may live with thee. Thou shalt not give him thy money upon usury, nor lend him thy victuals for increase."); Quran 2:275 (Sahih International) ("Those who consume interest cannot stand [on the Day of Resurrection] except as one stands who is being beaten by Satan into insanity. That is because they say, 'Trade is [just] like interest.' But Allah has permitted trade and has forbidden interest.").

7. E.g., N.C. GEN. STAT. § 24-1.1 (2016) (maximum interest rate for personal loans is 16%); ALA. CODE § 8-8-1 (2016) (maximum interest rate for personal loans is 8%); CAL. CONST. art. XV, § 1 (maximum permissible rate for personal loans is 10%); UTAH CODE ANN. § 15-1-1 (West 2016) (absent a contract in which the parties can set any rate of interest, the maximum permissible interest rate is 10%).

8. Among other things, the legal consequences of usury can be criminal, for example, ARIZ. REV. STAT. § 13-2208 (2016); CAL. Civ. CODE § 1916-3 (West 2016); CONN. GEN. STAT. § 37-7 (2016); MASS. GEN. LAWS ch. 271, § 49 (2016); N.Y. PENAL LAW § 190.40 (2016), or civil, for example, CAL. CIV. CODE § 1916-3 (West 2016); CONN. GEN. STAT. § 37-8 (2016); N.J. STAT. ANN. § 31:1-3 (West 2016); VT. STAT. ANN. tit. 9, § 50 (2016), may result in the usurious loan’s interest being uncollectible, for example, DEL. CODE ANN. tit. 6, § 2304(b) (2016); MIC. COM. LAWS § 438.32 (2016); N.J. STAT. ANN. § 31:1-3 (West 2016); OHIO REV. CODE ANN. § 1343.04 (West 2016), or may result in the loan being declared void ab initio, see, for example, CONN. GEN. STAT. § 37-8 (West 2016); N.Y. GEN. OBLIG. LAW §§ 5-511, 5-513 (McKinney 2016).

9. E.g., CAL. CONST. art. XV, § 1(2); ARIZ. REV. STAT. §§ 6-601, 6-602(B) (2016); OHIO REV. CODE § 1321.131(West 2016); TEX. FIN. CODE ANN § 342 (West 2016); VA. CODE
Federal law currently does not specify a federal usury rate, other than in limited circumstances where, for example, loans that are made at grossly excessive rates of interest can result in criminal liability, or where certain types of loans are made to military servicemembers or their families. Further, interest rates charged on loans made by federally regulated banks and nonbank lenders are subject to interest rate disclosure requirements under the Truth in Lending Act, and there are consumer regulatory provisions that are designed to prevent unfair, deceptive, or abusive acts and practices in connection with, among other things, the charging of interest rates on consumer credit.

Federal banking law, however, does contain two important provisions that allow a bank insured by the Federal Deposit Insurance Corporation (“FDIC”) to comply with the usury limits of its respective home state for all loans, including those that are made outside of the bank’s home state. For national banks that are chartered and regulated by the Office of the Comptroller of the Currency (“OCC”), National Bank Act section 85 (“Section 85”) provides that a national bank “may take, receive, reserve, and charge on any loan or discount made, or upon any notes, bills of exchange, or other evidences of debt, interest at the rate allowed by the laws of the State, Territory, or District where the bank is located.” Correspondingly, section 27 of the Federal Deposit Insurance Act (“Section 27”) provides that a state-chartered, FDIC-insured depository institution (a bank or a savings bank)

§ 6.2-1520(A) (2016).
12 10 U.S.C. § 987(b) (2015) (capping interest rate to military servicemembers and their dependents at 36%).
16 Id.
may, notwithstanding any State constitution or statute which is hereby preempted for the purposes of this section, take, receive, reserve, and charge on any loan or discount made, or upon any note, bill of exchange, or other evidence of debt, interest . . . at the rate allowed by the laws of the State, territory, or district where the bank is located.\footnote{Id. (providing further that “[i]f the rate prescribed in [this section] exceeds the rate such State bank or such insured branch of a foreign bank would be permitted to charge in the absence of this section, and such State fixed rate is thereby preempted by the rate described in subsection (a) of this section, the taking, receiving, reserving, or charging a greater rate of interest than is allowed by subsection (a) of this section, when knowingly done, shall be deemed a forfeiture of the entire interest which the note, bill, or other evidence of debt carries with it.”). As noted, this section also applies to FDIC-insured U.S. branches of foreign banks (of which there are very few).\textit{Id.})}

The National Bank Act takes the applicability of the federal law to the interest rate exportation statute one specific step further by providing an exclusive federal cause of action and remedy for a violation of Section 85.\footnote{National Bank Act § 30, 12 U.S.C. § 86.} In this manner, a national bank is not subject to any state action or remedy for the making of a usurious loan.\footnote{See Farmers’ & Mechanics’ Nat’l Bank v. Dearing, 91 U.S. 29, 33 (1875) (holding that the sole cause of action against a national bank for a usurious loan is a federal cause of action); Beneficial Nat’l Bank v. Anderson, 539 U.S. 1, 10–11 (2003) (holding that, under 12 U.S.C. §§ 85 and 86, there is no state law usury claim available against a national bank).} It is not as clear, however, whether this exclusive federal remedy is equally available to state banks that rely on the interest rate exportation provisions of Section 27.\footnote{See Discover Bank v. Vaden, 489 F.3d 594 (4th Cir. 2007), rev’d on other grounds \textit{sub nom.} Vaden v. Discover Bank, 489 F.3d 594 (4th Cir. 2007), held that Section 27 completely preempts state law claims against federally insured state banks; \textit{see also} Greenwood Trust Company v. Massachusetts, 971 F.2d 818, 827 (1st Cir. 1992) (holding that Section 27 expressly preempts countervailing state law). \textit{But see} Saxton v. Capital One Bank, 392 F. Supp. 2d 772, 783 (S.D. Miss. 2005) (holding that, unlike Section 85, Section 27 does not provide for complete preemption of state causes of action). The \textit{Saxton} decision was subsequently criticized in the \textit{Vaden} case. \textit{Vaden}, 489 F.3d at 605 n.12. The U.S. Supreme Court has not directly addressed the Section 27 issue.} Therefore, an FDIC-insured commercial bank or savings institution that engages in lending activities in more than one state is not burdened with the dilemma of addressing and resolving the differences in state usury laws and the need to decide which law it needs to obey, because it need only observe the usury limits of the state where it is...
located. This outcome was confirmed for national banks by the U.S. Supreme Court in 1978 in Marquette National Bank of Minneapolis v. First Omaha Service Corp.\(^{22}\) The Marquette court interpreted the phrase “where the bank is located” in Section 85 to mean the bank’s home state, and held that a national bank located in one state could charge a loan customer in another state the maximum rate of interest allowed by the bank’s home state.\(^{23}\) This has been recognized in various federal courts as applying to state banks under Section 27.\(^{24}\) This solution, however, is not available to nonbank financial firms that originate loans in multiple states, leaving such firms with the task of complying with the usury limits of each state where it conducts a lending business.

However, if a loan carries a lawful interest rate at inception, what is the legal status—and enforceability—of the loan when it is sold or otherwise transferred to another person? This is the issue that has been addressed by the valid-when-made doctrine as applied to questions of usury. This doctrine, in simple, substantive terms, states: “The non-usurious character of a note should not change when the note changes hands.”\(^{25}\) Its application is relatively straightforward in practice, in that the primary—or perhaps only—legal inquiry that must be made concerning the validity of a loan that is subsequently transferred is whether the loan, at inception, was lawfully made. Whether a loan, however, was validly made, and at what interest rate, is an entirely different question, and one that is not always easily addressed or answered. But, as discussed below, there is no dispute in Madden concerning the validity of the credit card that the defendant bank gave to the plaintiff, or the interest that was charged by the bank on the card. Consequently, issues surrounding the initial validity of a loan agreement are beyond the scope of this Article.\(^{26}\)

The valid-when-made principle is a subset of a basic principle


\(^{23}\) Id. at 318–19.

\(^{24}\) See, e.g., Vaden, 489 F.3d at 605–06.


\(^{26}\) We do note that the valid-when-made doctrine has its opposite iteration, which is also reflected in a substantial body of case law, namely, that a loan that is usurious at inception remains usurious until purged by a new contract. See, e.g., Westman v. Dye, 214 Cal. 28 (1931); Heide v. Hunter Hamilton Ltd. P’ship, 826 F. Supp. 224 (E.D. Mich. 1993).
of U.S. contract law, and has been acknowledged as such by the federal
courts in the context of a non-usurious loan transfer since at least the
early 19th century. As Judge Richard Posner observed: “[O]nce
assignors were authorized to charge interest, the common law kicked in
and gave the assignees the same right, because the common law puts the
assignee in the assignor’s shoes, whatever the shoe size.”

Although there is substantive federal and state case law that affirms the
applicability of the valid-when-made principle to the enforceability of
the initial legal interest rate on a transferred loan, one is struck by the
fact that much of the case law is well-dated, and modern case law that
applies the valid-when-made doctrine is relatively sparse. The age of
the governing case law that discusses and applies valid-when-made,
however, does not mean that the principle is irrelevant or antiquated,
inasmuch as there appears to be no case that expressly disaffirms the
principle (and, as we discuss below, we do not believe that Madden
falls within the disaffirmance category). Rather, the relative paucity of
modern case law (that is, decisions from the mid-20th century and later)
more likely reflects the fact that valid-when-made is a core, and
generally accepted, principle of the law of loans and contracts that
litigants have not felt necessary to challenge, or the courts to decide.

Certainly, as a business matter, the valid-when-made principle has been
universally relied on in the lending business, inasmuch as the ability of
a loan transferee to rely upon the enforceability and collectability in full
of a loan that is validly made is central to the stability and liquidity of
the domestic loan markets, to say nothing of core principles of
commercial dealing. And, prior to Madden, there was no reason to
believe that the courts viewed the matter otherwise.

27. See, e.g., Nichols v. Fearson, 32 U.S. 103, 106 (1833) (7 Pet.) (“Yet the rule of law
is everywhere acknowledged, that a contract free from usury in its inception, shall not be
invalidated by any subsequent usurious transactions upon it.”); Gaither v. Farmer & Mechs.
(13 Pet.).


29. In addition to the cases cited in note 27, see, for example, Huntsman v. Longwell, 4
F.2d 105 (5th Cir. 1925); Hirsch v. Smith, 262 Wis. 75 (1952); General Motors Acceptance
Co. v. Weinrich, 218 Mo. App. 68 (1924); Thomson v. Koch, 62 Wash. 438 (1911);
McDonald v. Aufdengarten, 41 Neb. 40 (1894); Van Beil v. Fordney, 79 Ala. 76 (1885).

30. See, e.g., FDIC. v. Tito Castro Constr., Inc., 548 F. Supp. 1224 (D.P.R. 1982);
Lattimore, 656 F.2d 139; Schreiber v. Thistle, Inc., 437 N.Y.S.2d 596 (1981); Shalit v. Inv’r
B. National Bank Preemption in Proper Perspective

Much has been said—by the OCC, the courts, and the legal community—about the nature, scope, and implications of national bank preemption, and a significant portion of the trade and scholarly commentary on *Madden* to date has focused on the National Bank Act preemption elements of the decision. Therefore, a concise discussion of these principles, and which elements of them apply to the facts and reasoning of *Madden*, can be of assistance in understanding the significance of the *Madden* decision.

The fundamental legal basis of federal preemption in the national bank context is that because national banks are organized under and derive their powers from federal law, it is federal, and not state, law that principally governs their activities and operations. The principle of preemption is grounded in the Supremacy Clause of the U.S. Constitution, which says that the Constitution and laws of the United States are the “supreme Law of the Land,” “any[t]hing in the Constitution or Laws of any State to the Contrary notwithstanding.”31 In turn, the basic principle of preemption is applied to national banks through the National Bank Act.32 As the OCC has stated:

> Since its establishment in 1863 and 1864, the national banking system, operating under uniform federal standards across state lines, has fostered an open financial marketplace, the growth of national products and services in national and multi-state markets, sound operating practices and efficient product delivery to bank customers. At the core of the national banking system is the principle that national banks, in carrying on the business of banking under a Federal authorization, should be subject to uniform national standards and uniform federal supervision. The legal principle that produces such a result is the “preemption” of state law.33

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31. U.S. CONST. art. VI, cl. 2. *See, e.g.*, Easton v. Iowa, 188 U.S. 220 (1903) (holding invalid an Iowa state statute which attempted to control the operations of national banks).
33. Press Release, John C. Dugan, Comptroller of the Currency, April 2010 Hearing
In turn, the OCC and the federal courts have repeatedly affirmed this core principle, and the broad applicability of federal preemption to national banks in general, as well as to a substantial variety of national bank (and national bank subsidiary) activities.\textsuperscript{34} In fact, the extent to which the OCC and the courts were willing to use federal preemption as a basis to override conflicting state laws—especially state consumer laws—generated a congressional counter-reaction in the wake of the 2008 financial crisis. This counter-reaction led to provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”) that limit the scope of federal preemption for operating subsidiaries of national banks and federal savings institutions, as well as the OCC’s authority to expand the limits of federal preemption, specifically as it pertains to state consumer laws.\textsuperscript{35}

With respect to the charging by national banks of interest rates—rates of interest, of course, being at the heart of the usury analysis—the preemption issue plays itself out in a slightly different manner. As noted above, Section 85 allows a national bank to charge its customers any interest rate that is permitted under the laws of the state where the national bank is located.\textsuperscript{36} This provision thus allows the bank to “export” its permitted home state interest rate to customers in other states. In order to maintain parity of competition between federally charted depository institutions and state depository institutions, Section 27 similarly allows a state bank to export its home state interest rate to customers in other states.\textsuperscript{37} This interest rate exportation authority, however, is often discussed as deriving from principles of federal preemption, a notion that is only partially accurate. In fact, the interest rate exportation authority in Section 85 and Section 27 (collectively, the “Exportation Provisions”) constitutes federal “preemption” only in the sense that it allows an insured depository institution to rely on its \textit{home state} usury law in setting the rate(s) of

\begin{footnotesize}
\begin{itemize}
  \item \textsuperscript{34} See, e.g., OCC Interpretive Letter No. 623, [1993-1994 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,512 (May 10, 1993) (establishing that a state law requiring licensing of annuity sellers was preempted as to national banks).
  \item \textsuperscript{36} National Bank Act § 30, 12 U.S.C. § 85.
  \item \textsuperscript{37} Federal Deposit Insurance Act § 27, 12 U.S.C. § 1831d(a)(2015).
\end{itemize}
\end{footnotesize}
interest for loans to customers in other states rather than the usury law of the customer’s state of residence. In other words, the interest rate Exportation Provisions do not require or impose a separate federal interest rate, but instead allow a depository institution to rely on a single state interest rate.

Of course, there is substantially more to the scope and interpretation of the federal interest rate exportation laws, not the least of which are issues such as what constitutes “interest,” and the manner in which a governing state usury limitation is applied by a depository institution. At this point in time, it is reasonably well settled that these collateral questions are questions of federal, and not state, law, and to that extent federal law does have an outright preemptive impact on countervailing state laws. At the same time, however, it would be a mistake to treat the Exportation Provisions as fully “preempting” state law, because what is in fact “preempted” under the Exportation Provisions is one state law over other countervailing state laws.

Why does this matter? It matters because the broader law and practice of federal preemption in the commercial bank context focuses to a significant extent on how broadly a federally chartered depository institution can cast its federal preemptive “net” over other organizations (e.g., operating subsidiaries or third-party service providers) and activities (e.g., insurance, operating ATMs, credit card operations), an inquiry that is broader than—and, as we discuss below, not relevant to—the more limited preemption inquiry under the Exportation Provisions, as discussed in the Madden decision. For instance, the OCC decided several years ago that national bank preemption extended to the activities of a national bank operating subsidiary, a position that was upheld by the Supreme Court in Watters v. Wachovia Bank, N.A., but was congressionally overturned by provisions of the Dodd-Frank Act.

With respect to operating subsidiary activities, the Dodd-Frank Act eliminated the preemption of state consumer laws that provided greater

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protections to consumers than federal laws.\textsuperscript{43}

With respect to unaffiliated firms that provide services to national banks, the extent to which the service organization can rely on the preemptive authority of a national bank to conduct activities for the national bank that may otherwise be impermissible under state law is less certain. The prevailing interpretive principle, however, appears to be that the applicability of national bank preemption turns on whether the national bank has some sort of continuing involvement or interest in the activities of the service provider such that subjecting the service provider’s activity to state law would significantly interfere with the national bank’s lawful exercise of its federal authority.\textsuperscript{44}

To explore this last point in greater depth, one important preemption-related issue that has been litigated to a considerable extent in the usury context has been what some have called the “true lender” or “real party in interest” principle in bank loan origination activities. This issue arises whenever a bank contracts with a third party for loan marketing, underwriting assistance, and servicing and administration services. Typically, these arrangements are structured in such a manner that a third-party nonbank loan intermediary sources the borrowers and negotiates (or assists in negotiating) the loan agreement, and may also service and administer the loan. Its bank partner, however, is responsible for actually underwriting the loan (either directly or through the imposition of loan underwriting requirements that the intermediary must apply), extending the credit and booking the loan on its balance sheet. While the loan may be sold to the intermediary a short time after origination, the process is configured to assure that the bank is treated as the legal creditor (or “true lender”), which, among other things, enables the intermediary to avoid at least some (if not all) state laws applicable to consumer lenders (including state licensing requirements), and just as importantly, assures that the bank is deemed the creditor for state usury.

\textsuperscript{43} Id.

\textsuperscript{44} See, e.g., SPGGC, LLC v. Ayotte, 488 F.3d 525, 532 (1st Cir. 2007) (“The National Bank Act explicitly states that a national bank may use ‘duly authorized officers or agents’ to exercise its incidental powers.”); cert. denied, 552 U.S. 1185 (2008); Pac. Capital Bank, N.A. v. Connecticut, 542 F.3d 341, 354 (2d Cir. 2008) (holding that a state law limiting interest rates on national bank-originated refund anticipation loans did not apply to third-party tax preparation companies offering the loans because the laws “would significantly, albeit indirectly, curtail authorized national bank activities and would thereby conflict with federal law.”).
purposes.

The “true lender” principle is straightforward in theory, but has been shown to be anything but that in practice. In turn, a substantial body of federal and state case law has developed that attempts to sort through, under diverse sets of facts and circumstances, whether a particular bank-lender intermediary arrangement results in the bank, rather the intermediary, being treated as the actual lending party-in-interest, or “true lender.”

The case law has generally taken two different approaches. In one approach (the “contractual approach”), the courts look to the structure of the arrangement between the bank and the intermediary, and to which party is deemed to be the lender in the agreements and in the contract with the borrower. To that end, the courts allow the parties to establish by contract the various responsibilities, and determine not to call those commercial decisions into question. In a contrasting approach (the “predominant economic interest approach”), the courts look to the “economic substance” of the relationship between the bank and the intermediary. In order for the bank to be the “true lender,” the totality of the facts and circumstances of the loan transaction must show that the bank has a “predominant economic interest” in the loan, the “key and most determinative factor” of which is whether the bank “placed its own money at risk at any time during the transactions, or whether the entire monetary burden and risk of the loan program” was borne by the intermediary. If the bank does not have a predominant economic interest, the courts are inclined to rule that the nonbank-lender

intermediary, and not the bank, is the actual lender.\textsuperscript{50} This finding exposes the intermediary to an array of undesirable legal and regulatory consequences, not the least of which is the intermediary’s legal inability to rely on the validity of the interest rate on the loan as if it had been originated by the bank under its home state usury laws.

The contractual approach to the “true lender” principle has developed as an indispensable bedrock principle in the loan origination, sales and securitization markets, as much contemporary finance and structured finance activity involves the participation of banks, loan brokers, loan servicers, purchasers, purchaser intermediaries, and loan servicers. In turn, the commercial finance markets require the legal assurance that a bank loan is just that—a bank loan that benefits from broad exemptions from state licensing, as well as the ability of the bank to export its home state interest rate under the Exportation Provisions. Recent cases have caused uncertainty as to which of the two approaches is the proper approach, with courts sometimes so finely distinguishing cases as to almost appear contradictory.\textsuperscript{51}

As we discuss below, however, the issue in \textit{Madden} is not a “true lender” issue. There is no dispute in \textit{Madden} that a national bank properly originated the consumer debt at issue and was the “true lender.” Therefore, commercial interests and legal practitioners who worry about the potential impact of \textit{Madden} on the “true lender” principle need not be overly concerned.

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\textbf{C.  The Blending of Valid-When-Made and Interest Rate Exportation Principles}
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In principle, the application of the valid-when-made doctrine to the enforceability of a commercial bank loan originated under the laws of the bank’s home state should be straightforward: if the bank can be

\textsuperscript{50} \textit{CashCall}, 2016 WL 4820635 at *7–8.

\textsuperscript{51} Compare \textit{id.} (applying the predominant economic approach to find \textit{CashCall} and not the originating bank to be the “true lender”), with Beechum v. Navient Sols., Inc., No. EDCV 15-8239-JGB-KKx, 2016 WL 5340454, at *8 (C.D. Cal. Sept. 20, 2016), \textit{judgment entered}, No. CV 15-8239 JGB (KKx), 2016 WL 5329553 (C.D. Cal. Sept. 21, 2016) (distinguishing earlier cases applying the predominant economic interest approach as being limited to whether a transaction satisfied the elements of usury or fell under a common law exemption to the usury prohibition, and then applying the contractual approach to find that bank-originated loans are exempt from state usury statute).
considered the legal lender or “true lender” and the interest rate is valid under the interest rate limits of the bank’s home state laws, the loan and its interest rate are valid at inception, under either Exportation Provision (depending on whether the bank is a national or state bank). In turn, under the valid-when-made doctrine, the subsequent transfer of the loan to a nonbank-loan intermediary, servicer, or debt collector should have no bearing on the enforceability of the loan’s interest rate by a transferee.

Certainly, the integrity and benefits of the federal interest rate exportation statutes do depend on the ability of a bank to transfer a valid loan that is enforceable by its terms in the hands of the transferee. However, in order to protect this integrity while also upholding these benefits, there is likely no need to resort to principles of federal preemption beyond those that are embedded in the Exportation Provisions. Moving this logic forward, there should be no need to inquire, as the Second Circuit in *Madden* did, as to whether the originating bank has a continuing interest in the loan after its transfer, because it plainly has none; the loan becomes the exclusive property of the transferee, and it is the transferee, not the bank, that has the exclusive interest in enforcing the loan according to its terms.

Nor should it matter whether the bank has charged off the loan: the act of charging off a loan is a balance sheet and income statement event (in accounting terms, a loss recognition event) that is dictated by federal and state financial regulatory and supervisory requirements, and generally accepted accounting principles.\(^{52}\) The bank’s act of charge-off, however, does not affect the legal right of the loan holder to enforce the loan, or the obligation of the borrower to repay it according to its terms.\(^{53}\) Stated otherwise, the sale or transfer of a defaulted loan does not make it any less valid from a legal enforceability standpoint, although of course the loan may be less collectible than a performing loan.

Because of the ways they can interrelate, one can easily see how

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53. In this regard, the *charge-off* of an uncollected loan is legally distinct from the *discharge* of a loan in bankruptcy; the latter action typically legally relieves the debtor of any obligation to repay the loan, whereas the former action does not.
principles of federal bank preemption, valid-when-made, “true lender,” and usury create a sometimes confusing, and often misunderstood, mish-mash of legal doctrines. This is the general legal context in which the Madden decision arose. With that, we turn now to a discussion of the decision itself.

III. MADDEN V. MIDLAND FUNDING—THE SECOND CIRCUIT’S DECISION

We begin with a brief summary of the case and its procedural history. Madden is a class action and debt collection case. Saliha Madden, a New York resident, had a credit card account with Bank of America, N.A., a national bank headquartered in Charlotte, North Carolina. Bank of America subsequently sold that credit card program to another unaffiliated national bank, FIA Card Services, N.A. (“FIA”).54 Two years later, Madden had an unpaid balance on her card of approximately $5,000 with a default annual interest rate of 27%.55 Madden’s unpaid balance was charged off by FIA and sold in its entirety to Midland Funding, LLC, a debt purchaser and collector.56 After Midland Funding purchased Madden’s debt, Midland Credit Management, its consumer debt collection affiliate, sent a letter to Madden seeking to collect payment on her debt.57 Neither Midland Funding nor Midland Credit Management is a state or national bank, and neither Bank of America nor FIA retained any interest in Madden’s debt upon sale.58

Madden filed a class action in the U.S. District Court for the Southern District of New York (“District Court”) against both Midland entities (“Midland”), alleging that they (1) violated the Fair Debt Collection Practices Act by engaging in abusive and unfair debt collection practices, and (2) were attempting to collect a rate of interest that was usurious under New York law59 (only the interest charged after Midland purchased the debt was argued to be usurious).60 The District Court denied both Madden’s motion for class certification and the

54. Madden v. Midland Funding, LLC, 786 F.3d 246, 247–48 (2d Cir. 2015).
55. Id. at 248.
56. Id.
57. Id.
58. Id.
59. Id.
60. Id. at 253.
defendants’ motion for summary judgment, each on a number of grounds. Notably, the District Court found that Midland was “entitled to the protection” of the National Bank Act. Madden appealed the decision to the Second Circuit.

On appeal, the Second Circuit reversed the decision of the District Court. In its opinion, the court discussed general principles of national bank preemption under Section 85, and the applicability of preemption to non-national bank entities. The court examined prior national bank preemption cases, including Watters v. Wachovia Bank and SPGGC v. Ayotte, and concluded that “[i]n most cases in which [National Bank Act] preemption has been applied to a non-national bank entity, the entity has exercised the powers of a national bank—i.e., has acted on behalf of a national bank in carrying out the national bank’s interest.” The Second Circuit distinguished two cases from the Eighth Circuit cited by Midland, Krispin v. May Department Stores and Phipps v. FDIC, as inapplicable to Midland because those cases involved either a continuing interest of a national bank (Krispin), or interest charged by a national bank or fees paid to an agent of a national bank (Phipps). The Second Circuit did not discuss the valid-when-made doctrine. In the end, the court held that the preemption principles of the National Bank Act did not apply to Midland because neither defendant is a national bank nor a subsidiary or agent of a national bank, or is otherwise acting on behalf of a national bank, and because application of the state law on which Madden’s claim relies would not significantly interfere with any national bank’s ability to exercise its powers under the [National Bank Act].

61. Id. at 248.
62. Id.
63. Id.
64. Id. at 250.
66. SPGGC, LLC v. Ayotte, 488 F.3d 525, 532 (1st Cir. 2007).
67. Madden, 786 F.3d at 251.
68. Krispin v. May Dep’t Stores, 218 F.3d 919 (8th Cir. 2000).
69. Phipps v. FDIC, 417 F.3d 1006 (8th Cir. 2005).
70. Id. at 252–53.
71. Id. at 253.
72. Id. at 249.
The Second Circuit then reversed and vacated the District Court’s judgment, and remanded the case to the District Court to determine whether New York law (the state of Madden’s residence) or Delaware law (the contractual choice of law in the credit card agreement) applied. Both Madden and Midland agreed that the 27% interest rate charge would be permissible under Delaware law, but would be criminal usury under New York law.

The defendants petitioned for a rehearing of the case en banc but the Second Circuit denied the request. The defendants then filed a petition for certiorari with the Supreme Court, which was also denied. Therefore, the holding of the Second Circuit remains in effect and the District Court will decide on remand the question of which state’s law (New York or Delaware) should apply to Madden’s contract. On February 27, 2017, as this Article was going to press, the District Court issued an opinion ruling on the questions remanded to it by the Second Circuit. A brief discussion of the District Court’s ruling appears at the end of this article.

What is particularly curious about the Madden decision is its singular focus on the application of National Bank Act preemption to the nonbank defendants without also taking into account the valid-when-made principle. Because it is undisputed (including by Madden herself) that FIA was permitted under Section 85 to charge Madden an interest rate of 27%, the various federal preemption arguments in

73.  Id. at 254.
74.  Del. Code Ann. tit. 5, § 943 (West 2016). As the Madden court notes, this section allows banks to charge any interest rate allowable by contract, and the court expresses no opinion as to whether this statute would apply to Midland as nonbank entities. Madden v. Midland Funding, LLC, 786 F.3d 246, 253 (2d Cir. 2015), reh'g en banc denied, Case No. 14-213-cv, ECF No. 140 (2d Cir. Aug. 12, 2015), cert. denied, 136 S. Ct. 2505 (2016).
75.  N.Y. Penal Law § 190.40 (McKinney 2016).
76.  Madden, 786 F.3d 246, reh'g en banc denied, No. 14-2131-cv, ECF No. 140 (2d Cir. Aug. 12, 2015).
79.  Infra Part VII.
80.  Madden, 786 F.3d at 250 (“FIA is incorporated in Delaware, which permits banks to charge interest rates that would be usurious under New York law, FIA’s collection at those rates in New York does not violate the [National Bank Act] and is not subject to New York’s stricter usury laws, which the [National Bank Act] preempts.”).
Madden at the District Court and Second Circuit levels crowd out and distract from the equally if not more important argument that the valid-when-made principle, if properly applied, would allow Midland to collect on a bank-issued credit card at the agreed-upon interest rate regardless of the applicability of National Bank Act preemption.

Part of this distraction appears to stem from the focus in the Madden decision on Phipps and Krispin, that both de-emphasize the valid-when-made principle. In Krispin, a nonbank entity, May Department Stores, issued credit cards, but assigned all the credit card accounts to a wholly owned subsidiary of May Department Stores that was a national bank. After the assignment, May Department Stores continued to purchase its subsidiary bank’s credit card receivables on a daily basis, and was substantially involved in account collection. Plaintiffs filed a class action lawsuit against May Department Stores alleging that the late fees charged on the overdue accounts exceeded permissible state usury limits and that the National Bank Act preemption principles did not apply because May Department Stores, not the bank, owned the receivables, and the only entity with which the customers interacted was May Department Stores, not the bank.

The Eighth Circuit acknowledged in Krispin that the National Bank Act would preempt any claims against May Department Stores’ subsidiary bank for violations of state usury laws, and stated that “it makes sense to look at the originating entity (the bank), and not the ongoing assignee (the store), in determining whether the [National Bank Act] applies.” However, the court also focused on the ongoing relationship between May Department Stores and the bank, and found that the “real party in interest” was the bank, even though May Department Stores owned the receivables. This focus on structural relationships between the parties led the Second Circuit in Madden to distinguish Krispin and conclude that, because FIA no longer had an interest in Madden’s debt, National Bank Act preemption no longer

81. Phipps v. FDIC, 417 F.3d 1006 (8th Cir. 2005).
82. Krispin v. May Dep’t Stores, 218 F. 3d 919 (8th Cir. 2000).
83. Id. at 922.
84. Id. at 923.
85. Id. at 921–22.
86. Id. at 924.
87. Id.
applied to that debt.88

Krispin is indeed distinguishable from the facts in Madden. The focus in Krispin on the structural relationship between the bank and the nonbank entity is arguably misplaced. As discussed above, whether a national bank or state bank has a continuing interest in a validly made loan is irrelevant to the question of whether such a valid loan can be enforced on its terms by a nonbank entity. Both principles of federal preemption and the Exportation Provisions are applied at the origination of the loan, not on an ongoing basis. The valid-when-made principle clearly establishes that a validly made loan is enforceable by the nonbank entity even if the nonbank entity could not have originated the loan on the same terms.

Interestingly, Krispin does mention the issue of valid-when-made, but only in a passing reference to another federal decision, FDIC v. Lattimore Land Corp.89 Krispin summarized the Fifth Circuit’s holding in Lattimore in a parenthetical: “stating, in [the] context of determining whether [the National Bank Act] governs [a] loan assigned by originating entity to entity in another state, that ‘[t]he non-usurious character of a note should not change when the note changes hands.’”90 Krispin’s cursory treatment of valid-when-made was not addressed by the Second Circuit in Madden, nor did the Second Circuit discuss valid-when-made at all.

The Second Circuit distinguished another case from the Eighth Circuit, Phipps v. FDIC, that was relied upon by Midland in its arguments.91 In Phipps, the plaintiffs alleged that a national bank improperly charged fees on second mortgage loans in violation of state law.92 The court in Phipps determined that certain fees charged by a national bank upon originating a mortgage loan (including origination fees that were then paid to a third-party nonbank) were properly considered interest because they were charged by the national bank and the National Bank Act permitted categorizing those fees as interest.93

90. Krispin v. May Department Stores, 218 F. 3d 919, 924 (8th Cir. 2000).
91. Madden, 786 F.3d at 253.
92. Phipps v. FDIC, 417 F.3d 1006, 1009 (8th Cir. 2005).
93. Id. at 1011–12.
Relying in part on Krispin, the court found that the fact that the mortgage loans were sold by the bank to third parties did not render the treatment of the fees as interest—which was permissible under the National Bank Act—invalid or unenforceable by the nonbank.\(^9^4\) The Phipps court again looked to the nature of the originating entity (here, a national bank) and not the assignee to determine whether the National Bank Act applied.\(^9^5\) Madden distinguished Phipps by observing that the entity charging interest or fees in Phipps was a national bank, and that the plaintiff in Madden only objected to the interest charged after the account was sold to Midland, not the interest charged by a national bank.\(^9^6\)

*Phipps* is properly distinguished from *Madden*, but, again, not for the reasons stated by the Second Circuit. *Phipps* is not a valid-when-made case; the validity of the underlying second mortgage loan or the enforceability of the loan in the hands of an assignee was not at issue. The plaintiffs in *Phipps* were seeking a refund of the alleged improper fees, as well as a prohibition on the assignee of the loan collecting stated interest on the loan in excess of state usury caps.

The holding in *Madden* evidences that the way in which the legal arguments in the case were framed arguably dictated the result. The defendants in *Madden* framed the case as a preemption case, and then relied on precedent focusing on preemption principles that were easily distinguishable and held inapplicable. If one views *Madden* as a case about national bank preemption, as the Second Circuit did, then the logical conclusion is that principles of preemption do not apply to activities of nonbank entities who purchase bank-originated loans. If a national bank operating subsidiary cannot avail itself of federal preemption principles with respect to consumer laws, it makes sense that an entity unaffiliated with a bank would similarly not be able to invoke federal preemption. If, however, one views *Madden* as a valid-when-made case, the only logical conclusion is that an interest rate that was valid at origination under the Exportation Provisions can be enforced by a nonbank assignee, regardless of whether the assignee is affiliated with the originating bank or whether the bank has an ongoing

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\(^9^4\) Id. at 1011.

\(^9^5\) Id. at 1013.

\(^9^6\) *Madden*, 786 F.3d at 253.
interest in the loan.

Did the Second Circuit misread the lower court’s decision? Notably, in its opinion in *Madden*, the District Court relied not only on *Krispin* and *Lattimore*, but also on foundational valid-when-made cases such as *Nichols v. Fearson* 97 in finding that Midland could properly seek to collect a debt with a 27% interest rate. 98 It is the framing of *Madden* as a valid-when-made case that led the District Court to conclude that the 27% interest rate could be validly enforced and collected by Midland. Why that particular point was not discussed in the Second Circuit decision is not clear.

In its amicus brief to the Supreme Court in connection with Midland’s petition for writ of certiorari, which the OCC joined, the U.S. Solicitor General and the OCC recognized that the failure to view the case as involving the valid-when-made doctrine led the Second Circuit to the wrong result: “The court of appeals’ failure to recognize the full scope of powers granted to national banks under Sections 85 and 24(Seventh), and the court’s failure to appreciate the potential significance of the valid-when-made rule, may be attributable at least in part to the lack of clarity in the briefing.” 99 The Solicitor General and the OCC concluded that the Second Circuit wrongly decided *Madden*, mostly due to the lack of discussion of valid-when-made. 100

Although we cannot conclude that consideration of valid-when-made was dispositive for the District Court, the Solicitor General, and the OCC, it clearly tipped the scales in favor of the nonbank parties seeking to enforce bank-originated contracts. In turn, one of the important lessons from *Madden* is for future defendants in similar cases to carefully craft their arguments to incorporate valid-when-made principles when appropriate, as valid-when-made remains a powerful, fundamental principle. In other words, a properly briefed case (i.e., one that invokes the valid-when-made doctrine when applicable) can prevent the spread of *Madden* to other district courts and circuit courts.

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98. *See supra* Part II.
100. *Id.* at 6–8, 11–12.
IV. IMPACT OF MADDEN ON LOAN ORIGINATION, SALES AND SERVICING ACTIVITIES

Despite the general consensus that Madden was wrongly decided, it remains the law in the Second Circuit. Therefore, banks, nonbank lenders, purchasers of secondary loans, and other third-party intermediaries in lending programs have had to review and, in many instances, change their business practices. At the outset, Madden caused a good deal of anxiety and disruption, although for now the marketplace appears to have adjusted to Madden as the law in the Second Circuit.

We have seen a variety of reactions in the marketplace to Madden. Some lenders have decided to exclude the Second Circuit states (New York, Connecticut, and Vermont) from their marketing and lending programs, or have decided to cap interest rates in those states in accordance with state usury limits. In securitization transactions, loans to borrowers in New York, Connecticut, and Vermont are sometimes excluded from the pools of loans to be purchased by the securitization vehicle. Alternatively, the securitization vehicle only purchases those loans with borrowers in New York, Connecticut, and Vermont that have interest rates that comply with state usury caps. A few lenders have decided to obtain state lending licenses instead of relying on National Bank Act preemption, which, in some states, has the added advantage of allowing the lender to charge interest rates above the default general usury limit.¹⁰¹

Due to Madden’s focus on the ongoing involvement (or lack of involvement) of a bank in order for National Bank Act preemption to apply, some lending programs and marketplace lenders have restructured their bank relationships so that the bank retains an interest in all the loans rather than selling the loans outright to the nonbank purchaser.¹⁰² This “skin in the game” structure may also help with any “true lender” claims that are raised in connection with these lending programs. There is, however, no clear guidance on how great an interest a bank needs to have in a loan for a court to find that federal

¹⁰¹. CAL. FIN. CODE § 22050 (West 2016).
¹⁰². See, e.g., LendingClub Corp., Quarterly Report (Form 10-Q) (Nov. 9, 2016).
preemption would apply.

Additionally, there has been a renewed focus by all participants on state usury laws, which previously were not of much concern to marketplace lenders, secondary market loan purchasers, and other participants. Usury laws are often complex and rather arcane, making it difficult at times to determine the proper rate applicable to certain loans. In addition, the penalties for usury violations vary from refunding excess interest charged to the borrower to criminal penalties. Participants in loan programs possibly affected by Madden have had to assess and report the possible risk and penalties if state usury laws (other than the laws of the bank’s home state) are found to apply to the loans.

Finally, there has been talk of a possible legislative solution from Congress (see discussion below) that would clarify that valid-when-made applies to bank-originated loans sold to any third party. Given the number of competing priorities in financial services for the new administration, the prospects for a legislative solution at this point are uncertain at best.

V. THE BROADER IMPLICATIONS OF MADDEN

As discussed above, the Second Circuit, sitting en banc, declined to reconsider the initial Madden decision, and the Supreme Court has declined to hear the matter at this time. As a result, the case has been sent back to the District Court at the direction of the Second Circuit for consideration of choice-of-law and contractual provisions which may fully resolve the specific controversy. Regardless of how the District Court rules on the matter, the Second Circuit’s decision remains in place, meaning that Madden is binding precedent within the Second Circuit and persuasive authority in other federal court jurisdictions. In this respect, at least, the legal uncertainty created by

103. For example, the California Civil Code sets the maximum permissible interest rate at 12%, but that statute is overridden by the California Constitution which sets the maximum permissible interest rate at 10%. Compare CAL. CIV. CODE § 1916-2 (West 2016), with CAL. CONST. art. XV, § 1. Florida law allows for a maximum interest rate of 18% to 30%, depending in part on whether the lender holds a consumer finance license. FLA. STAT. §§ 516.01, 516.031, 687.02, 687.03 (2016).
104. See supra note 8 and accompanying text.
105. See infra Part V.
Madden continues to exist.

But what are the most realistic consequences of the decision? There is little question that, in effectively denying the applicability of the valid-when-made principle to the transfer of a legally valid loan—which was generally viewed as settled law—Madden was an unexpected ruling. It has injected a level of uncertainty into the law of lending and usury, especially in light of the fact that Madden was decided in the Second Circuit, which historically has held a leading position among the federal courts of appeals on matters of commercial law. The Madden decision has had an impact on a variety of loan intermediation activities, such as marketplace lending, bank/loan intermediary partnerships, debt collection activities, loan securitization activities, and simple loan transfers, and has obliged loan market participants to reexamine their activities and structures.

At the same time, the broader impact of Madden on the law of lending in general thus far has been more limited. Although Madden has been cited without discussion on subsequent occasions in the Second Circuit itself\textsuperscript{106} and in a small handful of district court decisions in the Second and Third Circuits,\textsuperscript{107} these citations to Madden have not referenced the core holding of the case. Moreover, there have been, to date, no spillover effects of the Madden decision into other courts of appeals. Whether that spillover effect ultimately will occur remains to be seen, but plainly, there has been no judicial rush thus far to adopt the holdings or reasoning of Madden in other federal—or state—jurisdictions.

Are there broader regulatory consequences that may emerge from Madden? As we have discussed, a proper reading of Madden should not call into question any principles of federal preemption that may apply to loan origination, transfer, and servicing activities other than the narrower principles reflected in the Exportation Provisions. As discussed above, in the various—and increasing—number of “true


lender” court decisions that address the availability of federal preemption for third-party lending activities (origination, transfer, servicing) that are conducted pursuant to a formal business relationship with a state or national bank, the substantive federal preemption question has revolved around which party is the “real party in interest” in a lending partnership relationship. In turn, this question had led to an examination of the nature and quality of a lending intermediary’s relationship with a bank partner, and whether the national bank has some form of economic or financial interest in a loan that is originated, acquired, or serviced by a lending intermediary. As the Solicitor General and the OCC (correctly) observed in their Madden brief opposing certiorari in the Supreme Court, the questions presented in the three court decisions advanced by Midland in support of its position did not go to the legality of the interest rate on a loan originated by a national bank where the bank expressly relinquished any continuing interest in the loan after its transfer to Midland Funding.

Stated otherwise, Madden should have no material relevance to federal preemption issues and principles that arise in bank and intermediary lending partnerships, where “true lender” issues may arise. Madden is not a “true lender” decision, and therefore should not be cause for concern among those banks and loan originators and servicers that work in cooperation with one another on loan origination and servicing activities. Similarly, Madden should have no relevance to federal preemption issues arising from the legal characterization of late fees and other charges associated with a transferred or serviced loan, because Madden does not address in any respect the characterization or treatment of non-interest loan charges.

At the same time, as discussed above, Madden does call into question the legal validity of the interest rate on a loan that has been sold outright to a third party, which is a transactional framework that is integral to the proper functioning of the loan origination, sales, and securitization markets. Although the decision and its legal

108. Specifically, Phipps v. FDIC, 417 F.3d 1006 (8th Cir. 2005), which dealt with the legal characterization as interest of mortgage loan charges; Krispin v. May Dep’t Stores, 218 F. 3d 919, 924 (8th Cir. 2000), which addressed the validity of late fees charged to a retail store credit card holder; and FDIC v. Lattimore Land Corp., 656 F.2d 139 (5th Cir. 1981), which involved the usurious nature of a loan originated by a nonbank lender that was transferred to a national bank.

consequences thus far have been limited to the Second Circuit, *Madden* could pose a continuing legal risk to bank loan sales transactions. For that to occur, however, other jurisdictions would need to adopt the decision’s holding and reasoning, and thus far that has not come to pass.

There is enough concern over the impact of *Madden*, however, that there has been discussion of federal legislation to resolve any legal uncertainty created by the decision. In July 2016, a two-page bill was introduced in the U.S. House of Representatives that would amend the Exportation Provisions to expressly codify the valid-when-made principle for loans sold by national and state insured banks.\(^{110}\) Although no further action has been taken on this legislation, there may be renewed interest in this legislation in the 115th United States Congress, although so far no similar legislation has been introduced and a number of other competing financial regulatory priorities make any prediction on this issue speculative at best.

VI. CONCLUSION

The banking and lending industries have focused closely on the implications of *Madden*, and whether it has changed fundamental principles of bank lending law. In our view, *Madden* did not overturn the valid-when-made principle but rather overlooked it, resulting in a wrongly decided case. Despite the decision, however, the scope of federal preemption and the Exportation Provisions would appear to remain substantively unchanged. Further, if one sorts through the legal clutter surrounding *Madden*, notwithstanding the more immediate effects of *Madden* on the lending industry, valid-when-made should continue to be a valid and dependable legal principle for the loan origination, sales, and securitization markets. However, business interests operating within the Second Circuit do need to approach the issue with caution. Correspondingly, *Madden*’s impact on the application of state usury limitations similarly should not be material in the long term, unless there is a move in other federal courts—which

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\(^{110}\) The “Protecting Consumers’ Access to Credit Act of 2016” federal bill proposed to amend the Exportation Provisions by adding the following language to each section: “A loan that is valid when made as to its maximum rate of interest in accordance with this section shall remain valid with respect to such rate regardless of whether the loan is subsequently sold, assigned, or otherwise transferred to a third party.” H.R. 5724, 114th Cong. (2016).
thus far has not emerged—to adopt the case’s holding and reasoning in other federal jurisdictions.

One significant lesson that can be learned from Madden, however, is the importance of careful briefing of one’s case on federal preemption matters. In our view, it is quite likely that, had Midland placed a greater emphasis on the valid-when-made principle when arguing its case to the District Court and the Second Circuit, the Second Circuit might well have reached a different and more palatable decision with respect to the enforceability of the higher interest rate. Consequently, one is left hoping that the next case similar to Madden will appropriately emphasize valid-when-made as the primary governing legal principle.

VII. RECENT DEVELOPMENTS

As this Article was going to press, the U.S. District Court for the Southern District of New York issued a February 27, 2017 opinion addressing the choice-of-law and class certification questions remanded to it by the Second Circuit.111

On defendants’ summary judgment motion, the District Court found that where, as in the Madden case, the debt was in default, the plaintiff/borrower cannot assert violations of New York’s civil usury statute as a defense, but could assert violations of New York’s criminal usury statute as a defense.112 The District Court also held plaintiff did not have an affirmative claim for usury, and dismissed her claims of civil and criminal usury.113 The District Court, however, found that the violation of the New York criminal usury law could be used as a predicate in support of her claims under the Fair Debt Collection Practices Act (“FDCPA”) and the New York General Business Law (“GBL”), and therefore denied defendants’ summary judgment motion.114 Consequently, the underlying loan remains valid, but attempts to collect interest rates that violate New York’s criminal usury statute serve as a predicate for FDCPA and GBL claims.

112. Id. at *25.
113. Id. at *43.
114. Id.
On the choice-of-law issue, the District Court applied New York law rather than Delaware law because it found New York has a fundamental public policy to prevent criminal usury.\textsuperscript{115} Hence, the District Court did not enforce the Delaware law set forth in the cardholder agreement.\textsuperscript{116} The District Court also granted plaintiff’s motion for class certification on her FDCPA and GBL claims.\textsuperscript{117}

Because the valid-when-made doctrine was not an issue that had been brought before the District Court, its decision made no mention of the doctrine, nor did the decision address any substantive issues regarding the nature and extent of national bank preemption in the loan transfer context. Therefore, the District Court’s limited opinion does not shed any further meaningful light on the application of valid-when-made, or national bank interest rate preemption, to loan sale and transfer activities.

\textsuperscript{115} Id. at *25.
\textsuperscript{116} Id.
\textsuperscript{117} Id. at *43.