No. 15-610

In the Supreme Court of the United States

MIDLAND FUNDING, LLC, MIDLAND CREDIT MANAGEMENT, INC., PETITIONERS,

v.

SALIHA MADDEN

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF OF THE CLEARING HOUSE ASSOCIATION L.L.C., FINANCIAL SERVICES ROUNDTABLE, CONSUMER BANKERS ASSOCIATION, LOAN SYNDICATIONS AND TRADING ASSOCIATION, AND THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA AS *AMICI CURIAE* SUPPORTING PETITIONERS

JEREMY R. NEWELL
PAIGE E. PIDANO
THE CLEARING HOUSE ASSOCIATION L.L.C.
1101 Pennsylvania Avenue, N.W.
Suite 720 North Tower
Washington, DC 20004
(202) 649-4600

H. RODGIN COHEN
MICHAEL M. WISEMAN
SHARON L. NELLES
Counsel of Record
MATTHEW A. SCHWARTZ
STANTON R. GALLEGOS
SULLIVAN & CROMWELL LLP
125 Broad Street
New York, New York 10004
(212) 558-4000
nelless@sullcrom.com

(*Additional counsel listed on inside cover*)

RICHARD FOSTER
THE FINANCIAL
SERVICES ROUNDTABLE
600 13th Street, N.W.
Washington, DC 20004
(202) 289-4322

ELLIOT GANZ
THE LOAN SYNDICATIONS
AND TRADING ASSOCIATION
366 Madison Avenue
15th Floor
New York, New York 10017
(212) 880-3000

STEVEN I. ZEISEL
CONSUMER BANKERS
ASSOCIATION
1225 Eye Street, N.W.
Suite 550
Washington, DC 20005
(202) 552-6380

KATE COMERFORD TODD
STEVEN P. LEHOTSKY
U.S. CHAMBER LITIGATION
CENTER
1615 H Street, NW
Washington, DC 20062
(202) 463-5337

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

Page(s)

Cases

INTERESTS OF *AMICI CURIAE*

The Clearing House (TCH). Established in 1853, TCH is the United States' oldest banking association.[1] It is owned by the world's largest commercial banks, which collectively employ 1.4 million people in the United States and hold more than half of all U.S. deposits. TCH is a nonpartisan advocacy organization representing, through regulatory comment letters, *amicus* briefs, and white papers, the interests of its member banks on a variety of systemically important banking issues.

Financial Services Roundtable (FSR). As advocates for a strong financial future™, FSR represents 100 integrated financial services companies providing banking, insurance, and investment products and services to the American consumer. FSR's members provide fuel for America's economic engine, accounting directly for $98.4 trillion in managed assets, $1.1 trillion in revenue, and 2.4 million jobs.

Consumer Bankers Association (CBA). The CBA is the trade association for today's leaders in retail banking—banking services geared toward consumers and small businesses. The nation's largest financial

---

[1] Pursuant to Rule 37.6, *Amici* affirm that no counsel for a party authored this brief in whole or in part, and that no person other than *Amici* or their counsel contributed any money to fund its preparation or submission. *Amici* provided timely notice to the parties of its intent to file this brief. Petitioners and Respondent have consented.

institutions, as well as many regional banks, are CBA corporate members, collectively holding two-thirds of the industry's total assets. CBA's mission is to preserve and promote the retail banking industry as it strives to fulfill the financial needs of the American consumer and small business.

Loan Syndications and Trading Association (LSTA). The LSTA is a financial trade association whose mission is to promote a fair, orderly, efficient, and growing corporate loan market and to provide leadership in advancing and balancing the interests of all market participants. Among its 380 members are national and state-chartered banks as well as institutional lenders such as insurance companies and fund managers who make, purchase, and trade hundreds of billions of dollars in corporate loans.

The Chamber of Commerce of the United States of America (Chamber). The Chamber is the world's largest business federation. It represents 300,000 direct members and indirectly represents the interests of more than 3 million companies and professional organizations of every size, in every industry sector, and from every region of the country.

For nearly two centuries, courts (including this Court) have recognized as a "cardinal rule" of usury law that a loan is determined to be usurious or not only at the time of its origination. As this Court has explained, this rule is an important subject of "general mercantile interest." *Nichols* v. *Fearson*, 32 U.S. 103, 108 (1833). Indeed, the modern, multi-trillion dollar U.S. credit markets rely on the certainty the cardinal rule provides purchasers of loans in the face of a myriad of conflicting state usury laws that otherwise might be applicable.

The court of appeals below departed from this well-established and crucial legal precedent. In doing so, it undermined Section 85 of the National Bank Act (NBA), 12 U.S.C. 85, which (a) indisputably allows a national bank to charge on any loan it originates the rate of interest allowable under the usury laws of the state in which the bank is located, and (b) had always been understood to allow a secondary purchaser of the loan to maintain that same rate without fear of loss of interest, principal, and/or potential criminal sanctions under usury laws of other states. A similar result applies to Congress's decision to extend these protections to state banks in Section 27 of the Federal Deposit Insurance Act (FDIA), 12 U.S.C. 1831d.

Amici's members—which include banks and other institutions that routinely originate, purchase, and sell loans (both directly and through securitization), as well as businesses that benefit from the proper functioning of the credit markets—have a substantial interest in this action because the decision below (i) contradicts the long-settled industry and market expectations regarding usury law on which *Amici*'s members rely, and thereby (ii) (a) poses serious challenges to the efficient functioning of the credit markets in which *Amici*'s members participate, and (b) reduces the access of consumers and small- and medium-size businesses to credit. By ignoring this Court's decisions holding that the usurious nature of a loan does not change through assignment, the decision below threatens to make the "credit market operate less efficiently," and to impose "higher interest rates" on customers. *Olvera* v. *Blitt &*

Gaines, PC, 431 F.3d 285, 288 (7th Cir. 2005) (Posner, J.).

An essential role of *Amici*'s members is to provide credit on efficient terms to the consumers and small- and medium-size businesses which form the backbone of the American economy. *Amici* submit that a court should not, irrespective of the specific circumstances of the case before it, repudiate basic legal principles, and thereby disrupt established market expectations at substantial cost to the public well-being.

SUMMARY OF ARGUMENT[2]

I. A. Since the first half of the nineteenth century, this Court has recognized the "cardinal rule" that a loan that is not usurious in its inception cannot be rendered usurious subsequently, including by being sold or transferred to a third party. The cardinal rule is critically important to the functioning of the multi-trillion dollar U.S. credit markets, as it enables banks and financial institutions to buy and sell loans without fear that the loans will become subject to usury challenges because the assignee or purchaser of the loans may be subjected to different state usury laws.

---

[2] *Amici* agree with petitioners that, under the Second Circuit's decision, the application of state usury laws will make it far more difficult (or conceivably impossible) for institutions to sell or securitize loans they have originated, and thus will "substantially interfere" with the purpose of the NBA. Pet. at 14-21. *Amici* submit this brief to further explain to this Court (i) the bases for reversing the Second Circuit's decision, and (ii) the national importance of this issue.

The cardinal rule was well entrenched in American common law when Congress enacted Section 85 of the NBA in 1864—under which a loan originated by a national bank is subject only to the usury law of the bank's home state—and thus was presumptively incorporated into that provision. Moreover, since the enactment of the NBA, lower courts and regulatory agencies have consistently applied this "cardinal rule," and it remains a cornerstone of the credit markets. Accordingly, for over a hundred and fifty years, the multi-trillion dollar U.S. credit markets have functioned on the understanding that a loan originated by a national bank under the NBA is subject only to the usury law applicable at origination, regardless of whether and to whom it is subsequently sold or assigned.

By ignoring this rule, the decision below injects significant uncertainty into an area of the law that the credit markets have long viewed as settled and upon which they have relied.

B. Although the Second Circuit's decision on its face addresses only Section 85, the court's refusal to apply the cardinal rule casts doubt on the propriety of *any* validly originated loan that is sold or transferred. For example, the logic of the decision below applies directly to Section 27 of the FDIA, which provides state-insured banks the same certainty as to the application of their home state usury laws that is provided to national banks by Section 85.

C. The Second Circuit's decision also conflicts with decisions from the Fifth, Seventh, and Eighth Circuits. This conflict adds to the uncertainty generated by the decision below, because the same exact loan could be deemed usurious by a court in the

Second Circuit due to a post-origination sale of the loan, while courts in these other circuits would conclude that the loan is valid so long as it was lawful at origination. The decision also creates uncertainty as to how the other nine courts of appeals might rule, with grave effect in the interim, whereas previously there were no contrary decisions.

II. A. The consistent and certain application of this Court's "cardinal rule" under the NBA and the FDIA is essential to the proper functioning of the credit markets. By departing from that rule, the decision below has injected significant uncertainty into the purchase and sale (directly or through securitization) of all types of loans (not just charged-off credit card debt), whether by national banks, state-chartered banks, or non-bank entities and whether through a single transaction between counterparties, the secondary credit markets, securitizations, or participations. In the event of a sale, the validity of such loans can no longer be determined based solely on the circumstances at origination; it now may depend on the state in which the borrower resides, the state in which the loan purchaser resides, the law chosen to govern the agreement, and/or the circuit in which the borrower files suit.

B. The availability and accessibility of credit is a "crucial ingredient" for the growth of the nation's economy. Banks provide trillions of dollars in credit and are the primary source of loans for consumers and small businesses. Because of this central role in the financial markets, commentators have recognized that decreases in banks' ability to extend credit can negatively affect the entire economy.

C. The uncertainty caused by the decision below already threatens to decrease the availability and increase the cost of credit. If the decision below were allowed to stand, potential purchasers of loans and interests in loan securitizations will face the significant risk that a loan that was valid at origination may have been rendered usurious through assignment. This increased risk is likely to make purchasers less willing, if not entirely unwilling, to buy loans or interests in certain securitizations of loans that may turn out to be subject to additional state usury limits (including criminal penalties), or even a change in the usury law of the state in which the loan was originated. Credit market participants may respond by reducing the origination of loans (especially those to individuals or businesses within certain circuits), increasing the original rate of interest, or simply refusing to purchase or securitize certain loans. This potential decrease in the liquidity and value of loans threatens to increase the cost and decrease the availability of credit, particularly for small businesses and lower-income families. Because loans to such borrowers carry greater credit risk, such loans require higher interest rates, thus creating greater exposure to usury limits. The cost of credit, particularly to those closer to usury limits, will likely increase, because banks are likely to be less able to resell or securitize such loans on their balance sheet to finance additional lending. Moreover, the disruption of the credit markets and reduction of liquidity and value of loan portfolios held by banks could have ramifications for the safety and soundness of the banking system.

D. The effects of the decision below are already being felt. Multiple financial institutions have begun limiting their exposure to loans that were valid when made, but could potentially be deemed usurious if sold or assigned. This trend will only increase when interest rates rise from the current historic lows and usury ceilings become more relevant.

In light of the market's need for predictability and certainty regarding the ongoing validity of credit obligations, the potential impact on the nation's credit markets from ongoing uncertainty as to the validity of transferred loans and this Court's direct teaching, and the conflict among the lower courts on this important issue of law, this Court's review is imperative.

ARGUMENT

The decision below creates a divide among the courts of appeals as to the vitality under Section 85 of the NBA of the "cardinal rule" that the determination as to whether a loan is usurious is made only on its inception, and a subsequent sale or assignment to a third party cannot alter that determination. The cardinal rule is relied on continuously in the credit markets and is critical to their proper functioning. This Court should therefore grant review in this case, provide the now-necessary confirmation to litigants, lower courts, and the multi-trillion dollar national credit markets that rely heavily on this rule for their proper functioning, and reverse the decision below.

I. THE DECISION UPSETS LONG-SETTLED EXPECTATIONS CONCERNING USURY LAW AND THUS THREATENS DISARRAY IN THE MARKETPLACE.

A. For Almost Two Hundred Years, It Has Been Well-Established That a Valid Loan Cannot Be Rendered Usurious by Selling or Assigning the Rights to the Loan to a Third Party.

1. As early as 1828, this Court held that a non-usurious loan could not become usurious by reason of its sale. *Gaither* v. *Farmers & Mechs. Bank of Georgetown*, 26 U.S. 37, 43 (1828) ("[F]or the rule cannot be doubted, that if the note free from usury, in its origin, no subsequent usurious transactions respecting it, can affect it with the taint of usury."). And in 1833, the Court confirmed that it was a "cardinal rule" of usury that the determination of whether a loan is usurious occurs at the time of origination. *Nichols*, 32 U.S. at 109. To hold otherwise would mean that "a contract, wholly innocent in its origin, and binding and valid, upon every legal principle, [would be] rendered, at least, valueless, in the hands of the otherwise legal holder." *Id.* at 110. Even prior to this Court's decisions in *Gaither* and *Nichols*, other American and English courts had recognized this cardinal rule.[3]

[3] See, *e.g.*, *Watkins* v. *Taylor*, 16 Va. 424, 436 (1811) ("[I]f it was not usury *at the time* when the contract was entered into, no *after* circumstance can make it so; and any argument, therefore, drawn from after circumstances, would be improper." (emphasis in original)); *Tuttle* v. *Clark*, 4 Conn. 153, 157 (1822) (holding that "this

2. As this Court's decisions make clear, because this "cardinal rule" was firmly entrenched in American jurisprudence by the time of Congress's enactment of Section 85 in 1864, Congress is presumed to have incorporated that rule in Section 85. See *Astoria Fed. Sav. & Loan Ass'n* v. *Solimino*, 501 U.S. 104, 108 (1991) ("[W]here a common-law principle is well established, * * * the courts may take it as given that Congress has legislated with an expectation that the principle will apply 'except when a statutory purpose to the contrary is evident.'" (quoting *Isbrandtsen Co.* v. *Johnson*, 343 U.S. 779, 783 (1952)) (internal quotation marks and citations omitted)); see also *Lozano* v. *Montoya Alvarez*, 134 S. Ct. 1224, 1232 (2014) (citing *Astoria*, 501 U.S. at 108).

Accordingly, the credit markets have always functioned on the understanding that the cardinal rule was incorporated into and formed an integral part of Section 85. Indeed, given that loans, for hundreds of years, had been routinely purchased and sold, see generally John Munro, *The Origins of the Modern Fin. Revolution: Responses to Impediments from*

---

note, free from the taint of usury, in its origin," did not become usurious by the subsequent sale); *Tate* v. *Wellings*, 100 Eng. Rep. 716, 721 (K.B. 1790) (opinion of Buller, J.) ("Here the defence set up is that the contract itself was illegal; and in order to support it, it must be shewn that it was usurious at the time when it was entered into; for if the contract were legal at that time, no subsequent event can make it usurious."); see also 1 William Blackstone, *Commentaries on the Laws of England* 379-80 n.32 (18th London ed., W.E. Dean 1838) ("The usury must be part of the contract in its inception . . . .").

Church and State in W. Eur., 1200-1600 (Dep't of Econ. & Inst. for Policy Analysis, Univ. of Toronto, Working Paper No. 2, 2001), Section 85's protection would have been materially reduced had it not provided certainty that loans validly originated by a national bank could be sold or transferred without a buyer's becoming subject to state-law usury claims to which the national bank was not subject. See *Olvera*, 431 F.3d at 288-89; *Mono* v. *DH Capital Mgmt. Inc.*, 2014 WL 6845592, at *5 (Ky. Ct. App. Dec. 5, 2014).

3. The "cardinal rule" enunciated in *Nichols* has been officially recognized by the Office of the Comptroller of the Currency, the regulator of national banks, see OCC, Interpretive Letter No. 115 (Aug. 10, 1979) (citing *Nichols*), and has been consistently followed by courts around the country, see *Olvera*, 431 F.3d at 288-89; *Krispin* v. *May Dep't Stores Co.*, 218 F.3d 919, 924 (8th Cir. 2000); *FDIC* v. *Lattimore Land Corp.*, 656 F.2d 139, 148-49 & n.17 (5th Cir. Unit B Sept. 1981); 44B Am. Jur. 2d Interest and Usury 82, 205.[4]

4. In fact, the district court below specifically cited the cardinal rule in *Nichols* when it rightly held that Section 85 extends to purchasers of loans originated under that provision. (Pet. App. at 28a.) The combination of Section 85's plain textual rule that the applicable usury law at origination was that of the national bank's home state, and the background cardinal rule created the level of legal certainty necessary for a national credit market. Yet, the

---

[4] See also *Mono*, 2014 WL 6845592, at *5.

Second Circuit ignored this well-settled legal regime altogether—contradicting the decisions of this Court and upsetting the long-established expectations of the credit markets.

B. The Effects Of The Second Circuit's Decision Extend To Any Validly Originated Loan.

The importance of the Second Circuit's decision is amplified because its impact is not limited to loans originated by national banks; by refusing to apply the cardinal rule, the Second Circuit casts doubt on whether *any* loan that is sold or transferred by its original lender remains free of usury.

For example, just as Section 85 allows national banks to originate loans according to the laws of their home states, Section 27 of the FDIA provides insured state-chartered banks with the same power. See Federal Depository Insurance Corporation, Interpretive Letter No. 93-27, *12 U.S.C. § 1831d Preempts Contrary State Common Law Restrictions on Credit Card Loans*, 1993 WL 853492, at *1 (July 12, 1993) ("[Section 27] was intended to give state-chartered FDIC-insured banks the same * * * right to export interest enjoyed by national banks under [Section 85]."). Indeed, Congress "borrowed from [Section 85] and incorporated" its language into Section 27 of the FDIA. *Greenwood Trust Co.* v. *Massachusetts*, 971 F.2d 818, 827 (1st Cir. 1992). By calling into question the application of the "cardinal rule" of usury to loans originated by national banks under Section 85, the decision has a similar effect on loans originated by insured state banks under Section 27, as well as loans made by non-bank lenders.

C. The Decision Below Conflicts with Decisions Of Other Courts of Appeals.

Before the Second Circuit's decision, each court of appeals to have considered the issue, as well as numerous district courts, had followed the "cardinal rule" of usury law that a valid loan cannot be rendered usurious merely by being sold or assigned to a third party.

1. In *Lattimore*, for example, the Fifth Circuit faced the very same issue presented here: whether a loan that was valid in its inception could be rendered usurious simply by being bought or sold. 656 F.2d at 146-47. In *Lattimore*, a national bank in Tennessee obtained an interest in a loan made to a Georgia corporation. *Id.* at 140-41, 147. The loan was subject to Georgia law at its inception. *Ibid.* Although it was undisputed that the loan was not usurious under Georgia law, plaintiff argued that once the national bank obtained an interest in the loan, Section 85 of the NBA subjected the bank to the more restrictive usury laws of its home state of Tennessee. *Id.* at 146-47. Citing this Court's "cardinal rule" decision in *Nichols*, the Fifth Circuit rejected the borrowers' argument, explaining that "[t]he non-usurious character of a note should not change when the note changes hands." *Id.* at 148-49 & n.17 (citing *Nichols*, 32 U.S. at 109-11).

2. The Eighth Circuit relied on the cardinal rule and *Lattimore* to hold that the NBA preempted borrowers' state-law usury claims against a department store that purchased receivables from credit cards originated by a national bank on a daily basis. *Krispin*, 218 F.3d at 921-24. In *Krispin*, the

borrowers alleged that late fees charged were usurious under Missouri law. *Id.* at 922. The Eighth Circuit concluded that Section 85 preempted their claims, holding that a court must "look to the originating entity (the bank) and not the ongoing assignee (the store) in determining whether the NBA applies." *Id.* at 924 (citing *Lattimore*, 656 F.2d at 147-49). The Eighth Circuit reiterated this principle when it affirmed the dismissal of another action claiming that late fees charged by the assignee of a national bank violated state usury laws in *Phipps* v. *FDIC*, 417 F.3d 1006, 1013 (8th Cir. 2005) (quoting *Krispin*, 218 F.3d at 924).

3. Finally, in *Olvera*, plaintiffs brought an action alleging that purchasers of bad debts violated the federal Fair Debt Collection Practices Act by charging usurious interest under Illinois law. 431 F.3d at 286-87. The purchasers had acquired loans from licensed entities that were permitted under Illinois law to charge the rates at issue. *Id.* at 287. Plaintiffs argued that although the rates charged by the debt purchasers were "no higher (actually lower) than the original, lawful interest rates," the charges were usurious because the debt purchasers were not subject to the same interest rate exemptions as the originators. *Ibid.* Writing for the Seventh Circuit, Judge Posner affirmed the dismissal of these claims, explaining that "once assignors were authorized to charge interest, the common law . . . gave the assignees the same right, because the common law puts the assignee in the assignor's shoes, whatever the shoe size." *Id.* at 289. Judge Posner described the consequences of a contrary decision as "higher interest rates" for customers and a "credit market

[that would] operate less efficiently," and concluded that, "even if the plaintiffs have a decent technical argument for their preferred interpretation, its unreasonable consequences weigh heavily against it." *Id.* at 288-89.

4. *Lattimore*, *Krispin*, and *Olvera* clearly recognized the vitality and necessity of the cardinal rule that the law governing the loan at origination is the law that applies throughout the loan's life. Unfortunately, the court below failed even to acknowledge, much less properly apply, that rule.

II. THE DECISION BELOW CREATES SERIOUS PROBLEMS FOR THE AVAILABILITY AND PRICING OF CREDIT AND THE EFFICIENT FUNCTIONING OF THE CREDIT MARKETS.

A. The Decision Below Creates Uncertainty in the Credit Markets.

By departing from the "cardinal rule" of usury enunciated by this Court, the decision below injects confusion into the market for all types of loans (not just charged-off debt), because the determination of whether a loan is usurious after sale will now depend on the state in which the borrower resides, the state in which the purchaser resides, the law chosen to govern the agreement, and/or the circuit in which the borrower files suit. If, for example, a plaintiff files usury claims against a purchaser of loans in the Fifth Circuit (or any other circuit that follows this Court's decision in *Nichols*), courts will apply *Lattimore* and assess the usurious nature of the loan at origination. Conversely, if the same plaintiff files suit in the Second Circuit, courts applying the decision below will look to see whether the loan was rendered usurious through assignment or sale.[5]

Thus, the decision below threatens to alter significantly the legal protections of purchasers and assignees of loans when (i) the loan purchaser or borrower is a resident of a state with lower usury limits, or even a different methodology of calculating or defining interest, and (ii) the purchaser or assignee is subject to suit in the Second Circuit.

This uncertainty is particularly problematic in the context of the financial markets, which require predictability to function properly. See, *e.g.*, *Pinter* v. *Dahl*, 486 U.S. 622, 652 (1988) (noting that the securities laws are "an area that demands certainty and predictability"). The fact that New York City—the country's primary financial center—is in the Second Circuit magnifies further the confusion.

B. The Availability of Credit Plays a Central Role in the Operation of the Nation's Economy.

The doubt the decision below creates could seriously harm the U.S. financial system and economy. "Credit availability is a crucial ingredient in any advanced economy's recipe for economic growth because credit can support investment in productive enterprises and can smooth household spending from fluctuations in income." James

---

[5] In this respect, the Second Circuit's decision enables forum shopping by plaintiffs, who will be encouraged to bring usury claims in the Second Circuit in an effort to avoid this Court's ruling in *Nichols*.

McAndrews, Dir. of Research, Fed. Reserve Bank of N.Y., Credit Growth and Econ. Activity after the Great Recession, Remarks at the Econ. Press Briefing on Student Loans, Fed. Reserve Bank of N.Y. (Apr. 16, 2015)[6]; see also Elizabeth A. Duke, Fed. Reserve Bd. of Governors, Fostering a Healthy Credit Environment Speech (June 30, 2010) ("Credit plays a critical role in our economy.").[7] And, commercial banks provide vital access to capital and credit, especially for small businesses and consumers.[8]

As of June 30, 2015, FDIC-insured institutions held over $8 trillion in outstanding loans.[9] That does not include the additional almost $9 trillion in securitized loans that were originated by various

[6] *Available* at https://www.newyorkfed.org/newsevents/speeches/2015/mca150416.html.

[7] *Available* at http://www.federalreserve.gov/newsevents/speech/duke20100630a.htm.

[8] See Bd. of Governors of the Fed. Reserve System, Report to the Congress on the Availability of Credit to Small Business, 2 (Sept. 2012), http://www.federalreserve.gov/publications/other-reports/files/sbfreport2012.pdf; *Consumer Credit & Payments Statistics*, Fed. Reserve Bank of Philadelphia (October 22, 2015), https://www.philadelphiafed.org/consumer-credit-and-payments/statistics/.

[9] *Statistics on Depository Institutions Report—Net Loans and Leases*, FDIC (June 30, 2015), https://www5.fdic.gov/SDI/SOB/; see also Trefis Team, *U.S. Banks Witness Highest Post-Recession Growth In Loans Over 2014*, Forbes (Mar. 11, 2015), http://www.forbes.com/sites/greatspeculations/2015/03/11/u-s-banks-witness-highest-post-recession-growth-in-loans-over-2014/.

lenders, including banks,[10] or the undoubtedly trillions of dollars in the unreported volume of loans sold outside of securitizations. These loans include consumer loans (*e.g.*, credit card loans, auto loans, other personal loans), residential loans (primarily home mortgages), and loans to businesses of all sizes. See *id.* Because of banks' central role in these vitally important credit markets, economists have recognized that "the impairment of banks' ability to extend credit * * * has the potential to hinder investment and adversely affect the overall economy," including small businesses and the labor markets. McAndrews, *supra*; Burcu Duygan-Bump et al., *Fin. Constraints & Unemployment: Evidence from the Great Recession* 1 (Fed. Reserve Bank of Bos. Working Paper No. QAU10-6, 2011) ("Unlike larger firms, which have broader access to capital markets, small businesses are highly dependent on bank financing. An important implication is that any kind of disruption in the flow of bank credit may have significant real effects on the labor market.").

C. The Freedom to Sell or Assign Loans Is Essential to the Availability and Affordability of Credit.

1. Banks depend on the ability to sell or assign the loans they originate to provide liquidity to support their lending operations and to foster their safety and

---

[10] See Second Quarter 2015 Research Report, SIFMA Res. Q., at 8-9, *available at* http://www.sifma.org/research/item.aspx?id=8589956067 (SIFMA Report).

soundness. If loans could not be resold by banks, or the ability to do so was severely restricted, banks would be required to reduce vastly the amount of credit they extend and increase the costs for the reduced amount of credit they do extend.

2. The decision below greatly complicates all loan sales by forcing market participants to consider the following factors in originating and purchasing loans that they did not have to consider before:

- How easily will the original lender, or a subsequent purchaser, be able to sell, or resell, the rights to the loan to another party?
- What state law will govern the rate (and definition) of interest collectible on the loan?
- Will the purchaser be able to collect based on the original loan terms?
- Will the assignee be subject to suit in the Second Circuit, or only in courts that apply the traditional *Nichols* rule?

The multiple uncertainties will likely constrict the availability of liquidity in the credit markets, because market participants will likely be less willing, indeed sometimes unwilling, to purchase loans or interests in securitizations of loans that may be subject to state-law usury limits that are lower than the stated rate of the loan. And, to the extent market participants do purchase such loans or interests in loan securitizations, they are likely to discount the value to reflect the risk they take of receiving lower rates of interest than allowed on the face of the loan, or even the voiding of the loan.

For example, numerous types of loans, particularly smaller loans, are often securitized, *i.e.*, loans are pooled together and then interests in the pools (securities) are sold to various investors to spread the risk and the reward of owning those loans. See, *e.g.*, SIFMA Report, at 8-9. To do so, banks typically transfer the loans to a third-party entity to hold the loans before they are securitized. The decision below could be read to remove the "cardinal rule" of usury protection for these and other securitized loans on their sale to the third-party entity and potentially even on the sale of the interests in the securitizations to ultimate purchasers.

In addition, sales of loans usually include representations and warranties that the loan is collectible in accordance with its terms and that the sale does not violate any law. However, in light of the decision below, sellers may now be unable to make those representations and warranties, which could further depress the price of any loans sold by originators or, at worst, render such sales infeasible.

Moreover, the impact of the decision below is not limited to future loan sales. Any entity that has purchased or sold loans in the past now faces the possibility that those prior transactions—entered into in reliance on this Court's "cardinal rule" of usury—may now become the subject of innumerable disputes, including lawsuits against purchasers for collecting interest as permitted in loan agreements valid at origination and claims by purchasers against loan sellers seeking to recover for the loss in value of the loans they purchased. Purchasers may even be subject to criminal sanctions in a number of states.[11]

3. By threatening to reduce the value and liquidity of the multi-trillion-dollar portfolio of loans that banks currently hold, the decision could reduce the capital of banks, and ultimately have implications for the safety and soundness of the banking system. Moreover, if loans are rendered illiquid, banks may be forced to compensate for the greater attendant risk by originating fewer loans, and, ironically, imposing higher interest rates on the loans they still do originate. See *Olvera*, 431 F.3d at 288-89. That could lead to significant negative effects for consumers and small businesses, which may be unable to obtain loans, or able to obtain loans only at considerably higher rates.

An example of the negative consequences that can result when a court or legislature creates friction in the loan markets by departing from long-established precedent occurred in Georgia in the early 2000s. In 2002, Georgia passed a statute that, among other things, imposed unrestricted liability for assignees of certain higher-cost mortgages for any claim that could be asserted against the originator. See 2002 Ga. Laws 455, § 7-6A-6. In response, ratings agencies ceased rating securities backed by mortgage loans originated in Georgia, explaining that they could not evaluate the potential risk to investors resulting from this law.

---

[11] See, *e.g.*, Mich. Comp. Laws Ann. 438.41 (interest in excess of 25% is punishable by up to five years imprisonment and/or $10,000 fine); N.Y. Penal Law 190.40 (interest in excess of 25% is a felony punishable by up to four years imprisonment and/or $5,000 fine).

Henry Unger & Robert Luke, *Compromise Reached on Georgia Lending Law*, Atlanta J. Const., Feb. 1, 2003, 2003 WLNR 19578731. Financial institutions refused to buy mortgage loans originated in the state, and a number of lenders withdrew or substantially limited their operations in the state. *Ibid.* Faced with an impending crisis and enormous harm to consumers, Georgia amended the law to limit assignee liability. See *ibid.*; 2003 Ga. Laws 1, § 1.

The decision below creates similar uncertainty for sellers and buyers of all forms of loans, and threatens to have similar effects. And lower-income individuals and small businesses are likely to be most affected by the credit crunch generated by this uncertainty. As scholars have long pointed out with respect to consumer loans, "restrictions in credit markets hurt highest-risk borrowers the most." William F. Baxter, *Section 85 of the Nat'l Bank Act and Consumer Welfare*, 1995 Utah L. Rev. 1009, 1023 (1995). Small businesses likely will be similarly affected because they lack access to the broader capital markets, and are more dependent on bank financing than large corporations. See Karen Gordon Mills & Brayden McCarthy, *The State of Small Business Lending: Credit Access during the Recovery and How Tech. May Change the Game* (Harvard Bus. Sch. Working Paper No. 15-004, 2014).

D. The Decision Is *Already* Affecting The Ability Of Market Participants To Sell And Securitize Loans.

Only months after its issuance, the impact of the court of appeals' decision below is *already* being felt in the marketplace. For example, some financial institutions are reported to have imposed restrictions on credit facilities used to finance consumer lending, prohibiting loans to borrowers in the Second Circuit if those loans bear interest at rates higher than the state-enacted usury rates. See Joy Wiltermuth, *Usury worries hit Avant collateral*, Int'l Fin. Rev., Aug. 21, 2015, 2015 WLNR 24859283. Similar effects have been felt in the securitization market, as firms have removed loans made to borrowers in the Second Circuit from asset-backed securitizations due to usury concerns. Will Caiger-Smith, *Prospect Capital may rejig ABS deals amid usury worries*, Sept. 4, 2015, Int'l Fin. Rev., 2015 WLNR 26337187; see also Michael Tarkan, et al., Compass Point Research & Trading LLC, *Will Evolving Institutional Demand Prompt Changes to the P2P Issuance Model?* 1 (2015). These adverse effects will inevitably grow if this Court does not grant petitioner's request for *certiorari* and reverse the decision below.

In the current low interest rate environment, many loans are made at rates that would not be deemed usurious under many states' laws. But, as interest rates rise, more loans will necessarily be made at rates that may be considered usurious in the numerous states that have fixed usury rates.[12] In turn, banks and other lenders—as a result of the opinion below—will likely have to impose tighter restrictions on lending to ensure that the loans they make will not be subject to usury if sold. See Brian

[12] For example the standard usury rate is 12% in Virginia, see Va. Code Ann. 6.2-303(A), and 17% in Arkansas, see Ark. Const. Amend. 89 § 3.

Knight, *Congress Should Act to Preserve Financial Innovation*, Roll Call, Sept. 1, 2015, 2015 WLNR 25885469.[13]

---

[13] The decision below also threatens to have a significant effect on online marketplace lenders. See Matt Scully, *Peer-to-Peer Lenders Face Legal Blow in Usury Ruling*, BloombergNews (Aug. 31, 2015). The Department of the Treasury recognized that these lenders are filling a need for consumers "by often delivering lower costs and faster decision times than traditional lenders" and providing additional credit for small businesses. Department of Treasury, *Public Input on Expanding Access to Credit Through Online Marketplace Lending*, 80 Fed. Reg. 42,866, 42,867 (July 20, 2015). After the decision below, some analysts have raised concerns that nearly 60% of the loans made by some marketplace lenders may be exposed to usury claims. Matt Scully, *Wall Street Said to Limit Support for Online Lenders*, BloombergNews (Aug. 31, 2015). Further, financial institutions are reportedly considering limiting their financing to these types of lenders, and at least one firm has already withdrawn from upcoming bond sales. *Ibid*; see also Tarkan, *supra*.

CONCLUSION

For the reasons set forth above, the petition for a writ of *certiorari* should be granted.

Respectfully submitted.

JEREMY R. NEWELL
PAIGE E. PIDANO
THE CLEARING HOUSE
ASSOCIATION L.L.C.
1101 Pennsylvania Avenue, N.W.
Suite 720 North Tower
Washington, DC 20004
(202) 649-4600

H. RODGIN COHEN
MICHAEL M. WISEMAN
SHARON L. NELLES
Counsel of Record
MATTHEW A. SCHWARTZ
STANTON R. GALLEGOS
SULLIVAN & CROMWELL LLP
125 Broad Street
New York, New York 10004
(212) 558-4000
nelless@sullcrom.com

RICHARD FOSTER
THE FINANCIAL
SERVICES ROUNDTABLE
600 13th Street, N.W.
Washington, DC 20004
(202) 289-4322

ELLIOT GANZ
THE LOAN SYNDICATIONS
AND TRADING ASSOCIATION
366 Madison Avenue, 15th Floor
New York, New York 10017
(212) 880-3000

STEVEN I. ZEISEL
CONSUMER BANKERS ASSOCIATION
1225 Eye Street, N.W., Suite 550
Washington, DC 20005
(202) 552-6380

KATE COMERFORD TODD
STEVEN P. LEHOTSKY
U.S. CHAMBER LITIGATION
CENTER
1615 H Street, NW
Washington, DC 20062
(202) 463-5337

DECEMBER 10, 2015