UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT
Thurgood Marshall U.S. Courthouse 40 Foley Square, New York, NY 10007 Telephone: 212-857-8500

MOTION INFORMATION STATEMENT

Docket Number(s): 14-2131-cv

Caption [use short title]

Saliha Madden, on behalf of herself and all others similarly situated, Plaintiff - Appellant v. Midland Funding, LLC, Midland Credit Management, Defendants-Appellees

Motion for: Leave to File a Brief as Amici Curiae In Support of Defendants-Appellees' Petition for Panel Rehearing and Rehearing En Banc

Set forth below precise, complete statement of relief sought:

The Structured Finance Industry Group, Inc. and the Securities Industry and Financial Markets Association request leave to file a brief as amici curiae in support of Defendants-Appellees' Petition for Panel Rehearing and Rehearing En Banc

MOVING PARTY: SFIG and SIFMA

☐ Plaintiff ☐ Defendant
☐ Appellant/Petitioner ☐ Appellee/Respondent

OPPOSING PARTY: Saliha Madden, on behalf of herself and all others similarly situated

MOVING ATTORNEY: Mark E. Haddad

OPPOSING ATTORNEY: Daniel Adam Schlanger

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Court-Judge/Agency appealed from: U.S. District Court for the Southern District of N.Y., Judge Cathy Siebel

Please check appropriate boxes:

Has movant notified opposing counsel (required by Local Rule 27.1):
☑ Yes ☐ No (explain): ____

Opposing counsel's position on motion:
☐ Unopposed ☑ Opposed ☐ Don't Know

Does opposing counsel intend to file a response:
☐ Yes ☐ No ☑ Don't Know

FOR EMERGENCY MOTIONS, MOTIONS FOR STAYS AND INJUNCTIONS PENDING APPEAL:

Has request for relief been made below? ☐ Yes ☐ No
Has this relief been previously sought in this Court? ☐ Yes ☐ No
Requested return date and explanation of emergency: ____

Is oral argument on motion requested? ☐ Yes ☑ No (requests for oral argument will not necessarily be granted)

Has argument date of appeal been set? ☑ Yes ☐ No If yes, enter date: March 19, 2015

Signature of Moving Attorney:
/s/ Mark E. Haddad **Date:** June 26, 2015 Service by: ☑ CM/ECF ☐ Other [Attach proof of service]

Form T-1080 (rev. 12-13)

14-2131-cv

United States Court of Appeals
for the
Second Circuit

SALIHA MADDEN,
ON BEHALF OF HERSELF AND ALL OTHERS SIMILARLY SITUATED,

Plaintiff-Appellant,

– v. –

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

Defendants-Appellees.

On Appeal From The United States District Court
for the Southern District of New York (Civ. No. 11-8149)
Before the Honorable Cathy Seibel, J.

MOTION FOR LEAVE TO FILE BRIEF OF THE STRUCTURED FINANCE INDUSTRY GROUP, INC., AND THE SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION AS *AMICI CURIAE* IN SUPPORT OF DEFENDANTS-APPELLEES' PETITION FOR REHEARING AND SUGGESTION FOR REHEARING *EN BANC*

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CORPORATE DISCLOSURE STATEMENT

The Structured Finance Industry Group, Inc. (SFIG) has no parent corporation and no publicly held corporation has any ownership interest in SFIG.

The Securities Industry and Financial Markets Association (SIFMA) has no parent corporation and no publicly held corporation has any ownership interest in SIFMA.

The Structured Finance Industry Group, Inc. (SFIG) and the Securities Industry and Financial Markets Association (SIFMA) respectfully move for leave to file a brief as *amici curiae* in support of the petition for panel rehearing and rehearing en banc filed by Defendants-Appellees Midland Funding, LLC, and Midland Credit Management, Inc. (collectively, Midland). The proposed brief addresses the fundamental importance of allowing investors in the secondary loan market to continue to collect the same interest rate that was lawful and permissible at the time of a loan's inception. This issue is critical to SFIG, SIFMA, and their members—and to the proper functioning of the securities markets they strive to protect. SFIG and SIFMA participate regularly as *amici curiae* in cases involving securities and securitization markets, and they believe that their proposed brief here will assist the Court in assessing Midland's petition.

SFIG is a member-based trade industry advocacy group focused on improving and strengthening the broader structured finance and securitization market. SFIG has over 250 members from all sectors of the securitization market, including investors, issuers, financial intermediaries, accounting, law, and technology firms, rating agencies, servicers, and trustees. SFIG's core mission is to support a robust and liquid securitization market, recognizing that securitization is an essential source of core funding for the real economy.

SIFMA is the voice of the U.S. securities industry, representing the broker-dealers, banks and asset managers whose 889,000 employees provide access to the capital markets, raising over $2.4 trillion for businesses and municipalities in the U.S., serving retail clients with over $16 trillion in assets and managing more than $62 trillion in assets for individual and institutional clients including mutual funds and retirement plans. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA).

As explained in the proposed brief, the panel's opinion cannot be squared with the preemptive scope of section 85 of the National Bank Act, which incorporates the centuries-old rule that loans that are valid as against a claim of usury when made are not rendered invalid under state usury laws due to some later event. Instead, the opinion effectively allows states to regulate national-bank loans by resurrecting state-by-state usury regulations the moment a national bank transfers a loan to any entity that is not itself a national bank. This holding, if allowed to stand, would set a profoundly disruptive precedent. The secondary loan market is vital to the national economy; it facilitates lending and, among other things, lowers costs to consumers and businesses and frees up capital for other lending and investments. This market has an impact upon numerous financial transactions of substantial importance to everyday life—including home loans, car loans, student loans, and credit cards—and accounted for over $650 million in

securitizations in 2014 alone. By exposing securitized loans to attack under state usury laws, the panel opinion will cause enormous disruption to that secondary loan market and inject uncertainty and confusion into a segment of the national economy that requires certainty. SFIG and SIFMA are uniquely situated to offer an industry-wide perspective of the potential implications of the panel opinion for secondary loan markets and, therefore, believe that the attached brief will help the Court in its consideration of Midland's petition.

Midland has consented to this motion and to the filing of the proposed brief. Plaintiff-appellant opposes the motion and does not consent to the filing of the proposed brief.

Respectfully submitted,

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June 26, 2015

BRIEF OF THE STRUCTURED FINANCE INDUSTRY GROUP, INC., AND THE SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION AS *AMICI CURIAE* IN SUPPORT OF DEFENDANTS-APPELLEES' PETITION FOR REHEARING AND SUGGESTION FOR REHEARING *EN BANC*

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STATEMENT OF IDENTITY, INTERESTS AND AUTHORITY

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[1] Pursuant to Second Circuit Rule 29.1, undersigned counsel hereby confirms that (i) no party's counsel has authored this brief in whole or in part; (ii) no party or party's counsel contributed money that was intended to fund the preparation or submission of this brief; and (iii) no person or entity, other than SFIG and SIFMA, made a monetary contribution to the preparation or submission of this brief.

Amici have an abiding interest in preserving a vibrant secondary loan market, which involves numerous types of securitization transactions and whole loan portfolio sales. Banks routinely serve as financial intermediaries by making loans to borrowers and selling or securitizing them in the secondary market. Investors in the secondary market provide important liquidity for banks to continue to originate additional loans and manage their balance sheets. The ability of investors to collect the interest rate for which loan originators lawfully contract is a cornerstone on which the secondary loan market is built.

The panel opinion does not follow the uniform rule of usury law that the purchaser of a loan is entitled to collect the same interest rate that the applicable usury law permitted the loan originator to charge. If not corrected, the decision will substantially disrupt the secondary loan market for many types of consumer and business loans, including student loans, automobile loans, and mortgage loans. It also could create unwarranted potential liability for market participants that justifiably relied on previously well-established usury laws. The decision will raise interest rates, reduce the availability of credit, and hinder banks from acting as financial intermediaries, all to the detriment of borrowers and the economy.

State usury laws which purport to impose rate limits on investors buying national bank loans are preempted if they conflict with the interest rate authorized by 12 U.S.C. § 85, the law that applied at the time of loan origination. The panel

opinion failed to apply the federal rule that usury is determined at the time of loan origination, and that plaintiff's claims were preempted by the straightforward application of Section 85. Instead, the panel improperly concluded that such state laws are preempted only if they significantly interfere with national bank operations. Even under the significant interference test, the Court should recognize that limiting the ability of national banks to sell defaulted loans does substantially impair the ability of national banks to exercise federally granted powers or, alternatively, expressly indicate that the Court did not consider whether prohibiting holders of national bank loans that were not charged off at the time of sale would significantly interfere with a national bank's exercise of its powers.

ARGUMENT

Amici recognize that this Court traditionally has been reluctant to exercise its discretion to rehear a civil case *en banc*. But the interpretation and application of the laws that affect this nation's financial institutions have long been of central importance to this Circuit. This case is exceptionally important because the panel's holding, if allowed to stand, will have an unintended but profound and pernicious economic impact, reducing significantly the availability of credit to borrowers and raising their costs of borrowing.

I. The Importance of Securitization to Banks, Borrowers, and the National Economy.

Before securitization, banks were largely "portfolio lenders."[2] They held most of the loans they originated, and funded those loans through deposits or other bank debt that did not involve a direct claim on the loans. Funding loans in this way, however, limited banks' ability to meet increased demand for credit. Portfolio lending also posed institutional risks to banks with portfolios that were not adequately diversified across geographic or other market sectors.

Securitization allows banks to address these limitations and risks by packaging loans or other receivables and selling them in the form of asset-backed securities. A bank that securitizes loans typically transfers them to a special purpose vehicle, which then issues securities to investors.

Securitizations first developed in the housing market. Securitizing mortgages enabled mortgage lenders to replenish their capital for use in making new mortgages and thus keep pace with rising demand for new housing loans. Many investors were eager to purchase residential mortgage-backed securities in a

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[2] For a discussion of the background of asset securitization, see Comptroller of the Currency, *Asset Securitization: Comptroller's Handbook* (Nov. 1997), *available at* http://www.occ.gov/publications/publications-by-type/comptrollers-handbook/assetsec.pdf ("*Comptroller's Handbook*"). *See also* Fed. Reserve Sys., *Report to Congress on Risk Retention* (Oct. 2010), *available at* http://www.federalreserve.gov/boarddocs/rptcongress/securitization/riskretention.pdf ("*Board Report*").

secondary market. As securitizations grew more sophisticated, the secondary market quickly grew to include the securitization of automobile, credit card and other loans and receivables.

The ability to securitize bank loans is fundamentally important to banks, borrowers, and the economy. Banks benefit substantially from securitization because the transactions allow banks to limit the credit and interest rate risk of holding a loan portfolio and instead generate origination fee-income for which the bank no longer has to maintain capital. Securitization thus functions to "lower borrowing costs, release additional capital for expansion or reinvestment purposes, and improve asset/liability and credit risk management." *Comptroller's Handbook* at 4.

The economy, too, including consumer and business borrowers, benefits substantially from securitizations. The secondary market effectively decreases borrowing costs for consumers and businesses, because it facilitates more lending; banks would originate fewer loans if they were required to conduct their lending business as portfolio lenders, and as the capital available to support lending is reduced, the cost of borrowing increases. The secondary market also lowers risks to the Federal Deposit Insurance Corporation ("FDIC") from bank failures because it transfers ownership risks of the loans away from federally-insured banks to

private investors that are not FDIC-insured. The benefits of lower interest rates and greater availability of credit, in turn, improve the nation's economy.

Federal regulatory agencies have repeatedly recognized these benefits from securitizations to banks and borrowers. They were specifically identified in a 2010 report to Congress on the securitization market from the Board of Governors of the Federal Reserve System (*see Board Report* at 8–9), and subsequently described by the Office of the Comptroller of the Currency, the Federal Reserve, the FDIC, the Federal Housing Finance Agency, the Securities and Exchange Commission and the Department of Housing and Urban Development in recent rule making on the requirement that banks retain risk in securitization transactions (*see* 79 Fed. Reg. 77602, 77604 (Dec. 24, 2014), adopting final rule under Section 15G of the Exchange Act, 15 U.S.C. § 78o-11).

The problems arising from the panel decision are not limited to national banks, but equally affect other depository institutions. State banks, federal and state savings associations, and federal and state credit unions, all have authority to charge interest based on statutes that are modeled after Section 85. *See* 12 U.S.C §§ 1831d (state banks), 1463(g) (savings associations) & 1785(g) (credit unions); *see also Greenwood Trust Co. v Massachusetts,* 971 F.2d 818 (1st Cir. 1992) (state bank); *Gavey Props./762 v. First Fin. Sav. & Loan Ass'n*, 845 F.2d 519, 521 (5th

Cir. 1988) (savings association). The decision undercuts the ability of these institutions to sell loans in the secondary market as well.

The extraordinary size of the market shows the importance of securitization to banks and borrowers. For example, although securitizations may involve originators other than banks, a leading rating agency estimates that in 2014 there were $178 billion in automobile loan securitizations, $135 billion in credit card securitizations, $216 billion in student loan securitizations and $136 billion in other consumer loan securitizations. *See* Moody's Investors Servs., *Securitization Provides Meaningful Funding to the US Economy* 4–5 (Mar. 11, 2015), *available at* http://www.moodys.com/viewresearchdoc.aspx?docid=PBS_1003586.

II. Section 85 Preempts State Usury Laws That Purport to Limit Interest Rates That May Be Collected On National Bank Loans.

Federal law governs the interest rate for which a national bank can contract on loans. *See* 12 U.S.C. § 85 (allowing banks to charge "interest at the rate allowed by the laws of the State . . . where the bank is located"); *Smiley v. Citibank (S.D.), N.A.*, 517 U.S. 735, 737 (1996). As usury laws are solely matters of statute (*e.g., Scientific Prods. v. Cyto Medical Lab., Inc.*, 457 F. Supp. 1373, 1375 (D. Conn. 1978)), whether Section 85 continues to apply to a loan after it is sold by a national bank is a matter of federal statutory construction.

Courts must interpret Section 85 in accordance with both the "historical context" of the National Bank Act, 12 U.S.C. § 21 *et seq*. ("NBA"), and "the basic policy foundations of the statute." *Marquette Nat'l Bank of Minneapolis v. First of Omaha Serv. Corp.*, 439 U.S. 299, 313-14 (1978). The considerations that *Marquette* requires leave no doubt that, as a matter of federal law, Section 85 continues to apply to a national bank loan sold into the secondary market and any state law that purports to prohibit the interest rate that federal law allows to be collected on that loan is preempted because it conflicts directly with federal law.

When Congress enacted the NBA in 1864, it already was well-established that loans that are valid under a usury law when made are not invalidated by a subsequent event. In 1833, the Supreme Court observed that "the rule of law is every where acknowledged, that a contract, free from usury in its inception, shall not be invalidated by any subsequent usurious transactions upon it." *Nichols v. Fearson*, 32 U.S. (7 Pet.) 103, 106 (1833). This rule, the Court stated, was one of the "two cardinal rules in the doctrine of usury which we think must be regarded as the common place to which all reasoning and adjudication upon the subject should be referred." *Id.* at 109.

Treatises have long reflected uniform adherence to this cardinal rule. Webb's seminal treatise from 1899 observes that "'it seems to be the well-settled doctrine both in England and in America . . . that a valid debt can never be avoided

by any subsequent usurious contract.'" J.A. Webb, *A Treatise On the Law of Usury* § 306, at 345 (1899) (citing cases and authorities). A more recent treatise concludes that "[t]he usurious nature of a transaction is established at the inception of the transaction. The essential elements of usury therefore must exist at the inception of the contract. It is the agreement to exact and pay usurious interest, and not the performance of the agreement, which renders it usurious." 44B Am. Jur. 2d *Interest and Usury* § 82 (2015) (footnotes omitted).

Amici are not aware of any decision that departs from this cardinal rule. Courts instead hold that loans, after assignment, continue to be governed by the usury law that applied prior to the assignment. *See, e.g.*, *FDIC v. Lattimore Land Corp.*, 656 F.2d 139, 148–49 & nn.17, 18 (5th Cir. Unit B Sept. 1981) (citing *Nichols,* and stating "the non-usurious character of a note should not change when the note changes hands"); *Olvera v. Blitt & Gaines, P.C.*, 431 F.3d 285 (7th Cir. 2005) (holding that the assignee has the same right to charge interest as the usury law permitted for assignor); *Strike v. Trans-West Disc. Corp.*, 155 Cal. Rptr. 132 (Cal. Ct. App. 1979) (holding that the purchaser of a loan from a bank is exempt from usury law because the bank was exempt).

Imposing state usury laws on assigned loans would deprive the assignor of substantial value that Section 85 provides. The value of a loan that a bank originates includes the value for which the bank can sell that loan; uncertainty over

the validity of the interest rate if the loan is sold thus severely compromises the value of the loan, eroding the protection that Section 85 provides. The Fifth Circuit has made plain that "Congress surely did not intend to disadvantage National banks" by denying them the protection of "one of the 'cardinal rules in the doctrine of usury.'" *Lattimore*, 656 F.2d at 149–50 nn.17, 18 (quoting *Nichols*, 32 U.S. at 109). A rule that denies assignees the right to collect interest allowed assignors "would in effect prohibit – make uneconomical – the assignment or sale by banks of their commercial property to a secondary market [which] would be disastrous in terms of bank operations and not conformable to the public policy exempting banks in the first instance." *Strike*, 155 Cal. Rptr. at 139.

Congress did not intend such disastrous results. Rather, "Congress intended [the NBA] to facilitate . . . a 'national banking system.'" *Marquette,* 439 U.S. at 314-15. Achieving that purpose requires faithful adherence to the cardinal rules of usury that underpin Section 85 and the preemption of conflicting state laws.

III. Applying State Usury Laws to National Bank Loans After a Transfer Is Preempted for the Additional Reason That It Significantly Interferes With Federally Granted Powers.

The panel applied a test for preemption that looks at whether application of state law would "significantly interfere" with a national bank's business, which is the test traditionally applied to determine whether application of a state law is preempted because it frustrates the exercise of federally granted powers. The

Court need not reach the significant interference test because, as explained above, the conflict here between state usury laws and Section 85 is dispositive.

Nonetheless, it is also true that application of state usury laws to a national bank's participation in secondary market transactions would "significantly interfere with the national bank's exercise of its powers." *Barnett Bank of Marion Cty., N.A. v. Nelson*, 517 U.S. 25, 33 (1996). The panel erred by considering only the narrow question of whether the sale of the specific debt in this case would significantly interfere with a national bank's powers. The proper question is whether the rule advocated by plaintiff would significantly interfere with national banks' powers when applied more broadly. The answer to the preemption question, properly framed, is yes.

Securitizations and other secondary market transactions are founded on the ability of national banks' assignees to charge interest at the rates allowed for national banks. Subjecting national bank loans to a separate state usury analysis after they are transferred would disrupt securitizations to the substantial detriment of national bank operations. The ability of national banks to manage their balance sheets, and to reduce the credit and interest rate risks of loan ownership, would be substantially impaired. Without a robust securitization market, national banks will originate fewer loans, be less profitable and be prevented from fully carrying out their purpose under the NBA. The reduction in national bank lending also will

result in higher borrowing costs and fewer borrowers (especially borrowers who are less creditworthy) being able to obtain credit, all to the detriment of the economy. As the Seventh Circuit has explained, "push[ing] debt buyers out of the debt collection market" would impair "the credit market" and impose "higher costs of collection" that "customers [would bear] in the form of even higher interest rates." *Olvera*, 431 F.3d at 288.

If, as the panel's opinion suggests, national bank loans must comply independently with state usury laws after assignment, the interference with national bank powers will be profound. Fewer investors will be willing or able to purchase national bank loans. Many institutional investors may not be entitled under state usury laws to collect the same interest rates as national banks and will be excluded from participating in the secondary market. The complexity and risks of applying state usury laws to national banks also will substantially dampen secondary loan markets. Instead of simply looking at whether the originating bank complied with Section 85, such investors would need to evaluate the usury laws independently to determine which applied to that investor for every single loan included in the transaction. That is a hopelessly complex task, unworkable as a practical matter, not only because it involves evaluating a vast and heterogeneous portfolio of loans against the evolving laws of fifty states, but also because state usury laws vary widely from state to state, often setting different interest rate limits (including

limits for periodic interest and for other interest charges) for different types of loans. The costs of non-compliance with usury laws can be severe, including the loss of all interest and, in some cases, principal. *See, e.g.,* N.Y. Gen. Oblig. Law § 5-511; Conn. Gen. Stat. § 37-8.

Investors in the secondary market have justifiably relied on a "cardinal rule" of usury law that has been recognized for hundreds of years. The Court should enforce that traditional rule because it is an integral part of Section 85. Should it reach the significant interference test, the Court should hold that the application of state usury law to a debt buyer will substantially impair national bank operations by significantly disrupting the secondary loan market. At the very least, the Court should recognize that the application of state usury laws to securitizations and other secondary market transactions involving *performing* loans originated by national banks would constitute an extraordinary departure from settled law that would significantly interfere with a national bank's exercise of its powers. The panel also did not appear to have considered whether to expressly limit any conclusion that state usury laws may be applied to national bank loans to the narrow facts here, where a debt collector purchases defaulted consumer loans, and to describe that conclusion as a newly created exception to the long-standing general rule. *Amici* respectfully suggest, however, that having preemption turn on a fact-based inquiry into the degree of impairment posed by a particular loan

portfolio is an unmanageable rule that will inject substantial uncertainty and litigation risk that itself will significantly interfere with the exercise of national bank powers.

CONCLUSION

The petition for rehearing or rehearing *en banc* should be granted.

Respectfully submitted,

/s/ Mark E. Haddad

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June 26, 2015

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