

Statement by FDIC Chairman Jelena McWilliams

on the

Notice of Proposed Rulemaking: Federal Interest Rate Authority

**FDIC Board Meeting
November 19, 2019**

The proper functioning of financial markets is paramount to the ability of our financial system to prosper. When markets operate in a fair, equitable, and transparent manner, they allow capital and credit to be allocated efficiently and effectively. When markets are disrupted, it impacts the ability of individuals, financial institutions, and businesses to manage risk—including capital and liquidity risk—and limits the availability of credit necessary to maintain economic growth. As a prudential regulatory matter, market disruptions can pose significant safety and soundness concerns. This proposal seeks to remedy an ongoing market anomaly and also satisfies the goal of codifying longstanding supervisory guidance.

This notice of proposed rulemaking proposes regulations implementing sections 27 and 24(j) of the Federal Deposit Insurance Act (FDI Act). Specifically, it would codify guidance regarding interest rates that may be charged by State-chartered banks and insured branches of foreign banks.

While this guidance has been in effect for over 20 years, recent developments in the courts have challenged longstanding notions of the federal interest rate regime and have called into question longstanding Supreme Court precedents regarding the validity of loans assigned by banks. Specifically, the 2015 decision of the U.S. Court of Appeals for the Second Circuit in *Madden v. Midland Funding, LLC* called into question the validity and enforceability of the interest rate terms of a loan agreement following the assignment of that loan from a national bank to a non-bank third party. The Court found that the National Bank Act did not permit the assignee of the loan to charge interest at the rate of the original promissory note. This decision deviates from prior interpretations of the National Bank Act, and is contrary to over one-hundred years of Supreme Court precedent regarding sanctity of contracts.

This decision has interjected significant uncertainty to the secondary markets for loan sales in the Second Circuit, which raises safety and soundness concerns for financial institutions that may be unable to sell loans to manage liquidity and capital on their balance sheets. Banks and financial institutions rely on a robust secondary market to manage exposure. For example, banks may need increased liquidity in a time of financial stress or to meet unusual deposit demands, or to make additional credit available in times of increased demand. If the secondary market is not available, it calls into question the value of loans on bank balance sheets, and could lead to significant safety and soundness concerns.

The *Madden* decision was an unnecessary deviation from longstanding notions of contract law and created market instability in the Second Circuit. This proposed rule would correct this anomaly by establishing in regulations implementing section 27 of the FDI Act that the

permissibility of the interest rate would be determined when a loan is made and is not impacted by subsequent assignment, sale, or transfer.

In reaffirming and codifying in regulation the valid-when-made doctrine, the proposal does not address the question of whether a State bank or insured branch of a foreign bank is a “real party in interest” with respect to a loan or has an economic interest in the loan under state law, *e.g.* which entity is the “true lender.” Moreover, the FDIC views unfavorably the arrangements in which an entity partners with a State bank for the sole purpose of evading a lower interest rate established under the law of the entity’s licensing state(s).

I support this proposed rule and thank all the staff for the hard work and coordination with the Office of the Comptroller of the Currency to publish this proposed rule.

Thank you.