FDIC Issues Final Rule Codifying Valid When Made Doctrine, Cites McGlinchey Attorney

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At long last, the FDIC has issued its **final rule** codifying the "valid when made" doctrine. **The rule was finalized on June 25, 2020, and clarifies that the interest rate lawfully assessed by an originating depository institution may not be impacted by the sale, assignment, or other transfer of the loan or a change in state law.** The FDIC also confirmed that an originating depository institution may apply the law of any state in which it maintains a branch, not simply the law of the state where the bank is chartered. Within the rule, the FDIC clarifies that one component of federal interest rate exportation authority is the right to assign the loans under the preemptive authority of Section 27 of the Federal Deposit Insurance Act.

As the FDIC noted, although banks' power has traditionally been viewed as carrying with it the power to assign loans, certain courts have issued opinions that lack awareness of the broader context within which Section 27 was enacted and fail to address the significant ramifications of their decisions, one of which occurred earlier this month in Colorado, and was discussed in a **prior alert**. The FDIC's rulemaking makes this understanding an express one that carries with it the weight of the FDIC's authority, which confirmed longstanding historical precedent. The FDIC also clarified the additional fees and charges included within the definition of interest under federal law.

A key policy reason behind the FDIC's rulemaking is that a contrary position necessarily results in a safety and soundness concern for banks because it **increases the risk that depository institutions would not be able to sell loans and recover full value** when needed to satisfy liquidity requirements. In times of financial stress and reduced liquidity, this makes it more likely that depository institutions will fail because of the inability to recover full value for bona fide loans, which would, of course, place a greater burden on the FDIC when resolving failed banks. By issuing its final rule, the FDIC returns the legal status of loans originated by FDIC insured state-chartered banks to the historical status quo that has been accepted for decades.

There are some key limitations to the impact of the FDIC's final rule, however. The FDIC specifically called out that its rulemaking **does not address the question of whether a state-chartered bank is a real party in interest (i.e. the true lender) with respect to a loan** or has an economic interest in the loan under state law. Thus, the FDIC has not addressed regulatory actions seeking to assert that the originating bank is not the true lender. The FDIC also reiterated that it **will not favor partnerships** established with state-chartered depository institutions by non-depository entities **for the sole purpose of evading a lower interest rate** established under the law otherwise regulating the non-depository entity. We anticipate actions asserting these claims to continue.

The rule becomes effective 30 days after publication in the federal register, which will happen shortly.

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McGlinchey also notes that the FDIC cited member **Robert Savoie**, author of this alert, in both its proposed and final rulemakings. In December 2015, Robert published an article in the American Bar Association's Consumer Financial Services Committee newsletter titled ***Madden v. Midland Funding: A Sea Change in Secondary Lending Markets***, which articulated the negative impacts the decision had on banks and FinTech companies. As illustrated by the citations, the article was instrumental in prompting the FDIC to take action and resolve this issue.

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