

# Chapman Client Alert

February 28, 2017

Current Issues Relevant to Our Clients

## Madden Remand Decision

On Monday, February 27, 2017, the U.S. District Court for the Southern District of New York issued its long-awaited remand decision in *Madden v. Midland Funding, LLC*. The Second Circuit held in its May 2015 decision in *Madden* that a non-bank assignee of loans originated by a national bank was not entitled to the federal preemption afforded to the bank with respect to claims of usury. This controversial decision raised significant questions for the ability to enforce loans in accordance with their terms for non-bank marketplace lenders purchasing loans from an originating bank.

The Second Circuit remanded to the lower court to determine whether New York or Delaware law governed the contractual relationship of the parties. The account agreement specified Delaware law as the governing law, and the national bank that issued and administered the credit card account involved in *Madden* prior to default and assignment of the debt to Midland Funding had its principal place of business in Delaware. Delaware law authorizes creditors to charge any interest rate agreed upon by the borrower in a written contract. On remand, the district court held that applying Delaware law per the account agreement would violate a fundamental public policy of New York—namely, its criminal usury statute, which limits interest to 25% per year. Broadly interpreted, this decision could prevent the enforcement of choice of law provisions in credit agreements against New York consumers when the interest rate exceeds 25%, as is the case for many credit cards and other consumer loans.

The district court also found that although the New York criminal usury law does not provide a private right of action, Midland Funding's violation of the usury limit could serve as a predicate for Madden's Fair Debt Collection Practices Act ("FDCPA") and state unfair and deceptive acts and practices ("UDAP") claims, which the court allowed to proceed on a class basis.

The lower court's holding compounds the uncertainty created by the Second Circuit's decision in *Madden* by further undermining common law principles that are routinely relied upon by creditors and their assignees. While the Second Circuit's decision undercuts the doctrine that loans are "valid when made" and do not become invalid when they are assigned to a third party, the district court has now called into question the enforceability of a choice of law provision in a credit contract against New York consumers where the interest rate exceeds the state law usury limits. However, the court did not directly address what happens when federal preemption and state public policy conflict. How similar cases in the Second Circuit (New York, Vermont and Connecticut) will be decided remains to be seen, as *Madden* has not been adopted specifically by any other court to date.

## For More Information

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