

Advocates Praise Rent-a-Bank Ruling Upholding State Interest Rate Caps

Colorado Court Follows “Madden” Decision that Banks Can’t Assign Bank Privileges to Nonbank Lenders

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Washington, D.C. – Consumer advocates praised yesterday’s ruling by a Colorado court upholding the Colorado Attorney General’s claim that an online lender, Marlette Funding (dba Best Egg), must abide by Colorado’s interest rate limits when it purchases loans originated by a bank, Cross River Bank, that is exempt from the state’s rate caps. The National Consumer Law Center (NCLC) filed an amicus brief supporting Colorado in the case.

“The Colorado ruling makes clear that federal banking laws do not give banks a license to sell their bank privileges to nonbank lenders that charge rates above state limits,” said **Lauren Saunders, associate director of the National Consumer Law Center**. The Colorado court quoted the Second Circuit *Madden* decision in holding that extending federal banking laws “to third parties would create an end-run around usury laws for non-national bank entities.” “The decision upholds the power that states have had since the time of the American Revolution to cap interest rates to protect people from predatory lending,” **Saunders added**.

Marlette offers loans on its Best Egg website, but the fine print says that “Best Egg loans are unsecured personal loans made by Cross River Bank” Rates go up to 29.99% and loans may be as large as \$35,000, or even \$50,000 in some instances. Colorado allows 12% annual interest for consumer loans by unlicensed lenders and 21% for licensed lenders.

At least 45 states* and DC impose interest rate caps on many loans, but banks are generally exempt from state rate caps. In the last couple of years, high-cost lenders – some charging rates as high as 160% — have begun trying to take advantage of this exemption by entering into rent-a-bank schemes where they launder their loans through banks and then purchase back the loans or receivables and continue to charge high rates that would be illegal for the non-bank lenders to charge directly.

The Colorado Attorney General’s win this week follows the filing last week of a complaint by the District of Columbia Attorney General against another online lender, Elevate, that through its Rise and Elastic brands charged annual interest rates between 99% and 251% despite D.C. law capping rates at 6% to 24%. The National Consumer Law Center’s (NCLC) website has a Predatory Rent-a-Bank Loan Watch List that describes high-cost rent-a-bank schemes and where they operate.

“Colorado and D.C. are showing how states can defend their interest rate caps and protect borrowers from high-rate lending despite the lack of federal protection. Rent-a-bank lenders pick and choose where they lend, and they tend to stay out of states that enforce their laws,” **Saunders explained**.

The ruling also puts into question the legality of proposed rules by the Federal Deposit Insurance

Corporation (FDIC) and Office of the Comptroller of the Currency (OCC), which the OCC recently finalized, that would overturn the *Madden* decision and allow an assignee of a bank loan to charge any rate the bank could charge. The court found that the “plain language [of the Federal Deposit Insurance Act] does not apply to non-banks, therefore federal preemption does not apply.” The court made the same observation about the National Bank Act. “The court made clear that federal banking laws don’t apply to nonbanks, and for the same reason, the OCC and FDIC have no authority to preempt state interest rate limits that apply to nonbanks,” **Saunders explained.**

But the OCC and FDIC have stated that their rules do not address the situation where a nonbank is the “true lender.” The D.C. Attorney General’s case alleges that Elevate, not the two banks it uses, is the ‘true lender’ and thus state interest rates apply. The Colorado court did not yet address whether Marlette or the bank is the true lender.

Instead, the court held that even if the bank is the true lender, once a loan is assigned to a nonbank lender, new charges must follow state law. In *Madden v. Midland Funding*, the Second Circuit Court of Appeals held that debt buyers that purchase charged-off credit card debt are subject to New York usury laws when they add new interest even though the credit card banks themselves are not limited by those laws. “The Colorado court correctly rejected the specious claim that centuries of law under a so-called ‘valid-when-made’ theory prevent challenges under longstanding usury laws to usurious interest charged by nonbank lenders that purchase loans assigned by banks,” **Saunders said.** An NCLC issue brief explains the *Madden* and true lender doctrines.

“Online lenders claim that they are ‘fintechs,’ but whatever the label, they are not banks, and technology and ‘innovation’ do not give them the right to charge high interest rates that are illegal under state law,” **Saunders noted.** “Interest rate limits are the simplest and most effective protection against predatory lending, and states can and should defend their rate limits and stand up to rent-a-bank schemes.”

*Fact sheet updated in March 2021

Additional NCLC Resources

Predatory Rent-a-Bank Loan Watch List by State

Press release: Advocates Condemn Rent-a-Bank Rule that Encourages Predatory High-Cost Loans; Call on Congress to Pass Federal 36% Interest Rate Cap Limit, May 29, 2020

Brief: FDIC/OCC Proposal Would Encourage Rent-a-Bank Predatory Lending, December 2019

Fact Sheet: Stop Payday Lenders Rent-a-Bank Schemes, November 2019

Op-Ed: Rent-a-bank schemes trample voters’ and states’ rights by Lauren Saunders, Feb. 8, 2018