

SPURIOUS PEDIGREE OF THE “VALID-WHEN-MADE” DOCTRINE

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ABSTRACT

The “valid-when-made” doctrine holds that if a loan was not subject to a state usury law when it was made, it can never subsequently become so upon transfer. The doctrine is supposedly a “well-established and widely accepted” common law doctrine that is a “cardinal rule” of banking law endorsed by multiple Supreme Court decisions.

This Article demonstrates the valid-when-made doctrine’s spurious historical pedigree. The doctrine is a modern invention, fabricated by attorneys for financial services trade associations in the appeals from the Second Circuit’s Madden decision. It rests solely on decontextualized and misinterpreted quotations from nineteenth century cases dealing with entirely different issues in usury law. Simply put, the valid-when-made doctrine is not valid, but made up, and its historicity cannot serve as a basis for legal interpretation.

INTRODUCTION

This short Article presents the first-ever detailed historical analysis of the “valid-when-made” doctrine. The doctrine holds that if a loan was not subject to a state usury law when it was made, it can never subsequently become so upon transfer.¹ Valid-when-made is supposedly a “well-established and widely accepted” common law doctrine that is a “cardinal rule” of banking law endorsed by multiple Supreme Court decisions.² This Article shows that the doctrine is in

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1. See *Kaur v. World Bus. Lenders, LLC*, 440 F. Supp. 3d 111, 121 (D. Mass. 2020) (explaining the supposed doctrine as “if the interest rate in the original loan agreement was non-usurious, the loan cannot become usurious upon assignment—so, the assignee lawfully may charge interest at the original rate” (quoting *In re Rent-Rite Superkegs W., Ltd. v. World Bus. Lenders, LLC* (*In re Rent-Rite Superkegs W., Ltd.*), 603 B.R. 41, 66 (Bankr. D. Colo. 2019), *rev’d in part*, 623 B.R. 335 (D. Colo. 2020))).

2. See, e.g., *Amicus Brief of the Fed. Deposit Ins. Corp. and Off. of the Comptroller of the Currency in Support of Affirmance and Appellee at 10, In re Rent-Rite Superkegs W., Ltd.*, (No.

fact a modern invention, completely lacking in historical roots. Valid-when-made is not a long-standing, cardinal rule of banking law, but a 2015 creation of financial services industry lawyers.

The doctrine's primary importance is to shield loans made by banks and subsequently transferred to nonbanks from the application of state usury laws. Whereas nonbanks are subject to state usury laws, banks are generally exempt.³ If the valid-when-made doctrine applies, a loan made by a bank remains exempt from state usury laws even when it is transferred to a nonbank.

The authenticity of the doctrine's historical pedigree matters for three reasons. First, the doctrine's supposed historicity is used to argue that it is a well-established part of the common law that itself provides a rule of decision in cases where a usury claim is raised against a nonbank buyer of a loan from a bank. Banks frequently make loans that they sell to nonbanks in three separate transactional situations: securitizations, sales of defaulted debt to debt buyers, and rent-a-bank transactions, in which a nonbank contracts with a bank to purchase high-cost loans that the bank has originated on spec for the nonbank.⁴ In these transactions, the bank may have little or no stake in the ultimate performance of the loan—and thus no concern about the increased likelihood of borrower default due to the high interest rates.⁵ In each of these situations, applying the valid-when-made doctrine would enable nonbanks—which are not subject to the same regulatory

19-cv-1552) [hereinafter “FDIC/OCC Amicus Brief”] (quoting *Nichols v. Fearson*, 32 U.S. (7 Pet.) 103, 109 (1833)). It is also worth noting that the “valid when made” doctrine is a federal common law. This would seem to create a problem for the doctrine. The Supreme Court made clear in *Erie R.R. Co. v. Tompkins*, 304 U.S. 64 (1938) that federal courts lack a judicial power to create general federal common law regarding state law claims when sitting in diversity jurisdiction. *Id.* at 78. Usury claims are state law claims, so to the extent that jurisdiction exists based on diversity, there is no basis for federal courts extending a common law rule. Jurisdiction might be federal question jurisdiction based on section 85 of the National Bank Act of 1864 (NBA), 12 U.S.C. § 85, and section 1831d of the Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDMCA), 12 U.S.C. § 1831d, but neither statute can support as broad of a doctrine as valid-when-made. Instead, any federal common law under either statute would have to be confined to the scope of the statute.

3. Adam J. Levitin, *Rent-a-Bank: Bank Partnerships and the Evasion of Usury Laws*, 71 DUKE L.J. 329, 332 (2021).

4. *See id.* at 333, 338.

5. Whether the bank has skin-in-the-game on the performance of the loan (and to what extent) is transaction specific. In rent-a-bank transactions, banks have very little skin-in-the-game. *See id.* at 372–73, 385 (giving illustrations of the extent of retained bank interest in rent-a-bank originated loans.) Securitization transactions, however, can vary substantially by asset type. *See* Adam J. Levitin, *Skin-in-the-Game: Risk Retention Lessons from Credit Card Securitization*, 81 GEO. WASH. L. REV. 813, 816, 818, 847–850 (2013) (contrasting formal contractual risk retention and implicit recourse in credit card securitizations).

oversight as banks⁶—to do indirectly that which they could not do directly: under the valid-when-made doctrine, nonbanks can purchase and collect on high-cost loans that they could not legally make themselves. The result is to enable evasion of usury laws, which provide a critical consumer protection in credit markets.

If the valid-when-made doctrine is part of the common law, it effectively enables nonbanks to evade state usury laws by purchasing loans that they cannot make themselves. If, on the other hand, the doctrine is a modern fabrication, then it is not part of the common law, and its historicity alone cannot provide a basis for shielding the nonbank loan purchaser from application of state usury laws.

Second, the doctrine's supposed historicity provides part of the legal support for a pair of rulemakings by the Office of the Comptroller of the Currency (OCC) and the Federal Deposit Insurance Corporation (FDIC) that codify the doctrine.⁷ In particular, the OCC claims that the doctrine was part of the common law as of 1864, when the National Bank Act (NBA) was enacted, and therefore was incorporated in the NBA's provision on interest rate exportation.⁸ The interest rate exportation provision allows national banks to charge the interest rate permitted in their home state irrespective of where they are lending.⁹ In other words, the interest rate exportation provision, although often referred to with the shorthand of preemption of state

6. In particular, bank regulation includes “soft” supervision and moral suasion that is generally effective at dissuading banks from offering products of which regulators disapprove, irrespective of the presence of statutory prohibitions. *See* Levitin, *supra* note 3, at 358.

7. Permissible Interest on Loans That Are Sold, Assigned, or Otherwise Transferred, 85 Fed. Reg. 33,530, 33,532 (June 2, 2020) (to be codified at 12 C.F.R. pts. 7 & 160) (codifying OCC valid-when-made rule)); Federal Interest Rate Authority, 85 Fed. Reg. 44,146, 44,149 (July 22, 2020) (to be codified at 12 C.F.R. pt. 331) (codifying FDIC valid-when-made rules).

8. Permissible Interest on Loans That Are Sold, Assigned, or Otherwise Transferred, 85 Fed. Reg. at 33,532. Congress is presumed to legislate against the backdrop of the common law. *E.g.*, *Voisine v. United States*, 136 S. Ct. 2272, 2286 (2016) (“[W]e presume that Congress legislates against the backdrop of the common law.”); *Astoria Fed. Sav. & Loan Ass’n v. Solimino*, 501 U.S. 104, 108 (1991). Accordingly, “[s]tatutes which invade the common law . . . are to be read with a presumption favoring the retention of long-established and familiar principles, except when a statutory purpose to the contrary is evident.” *Isbrandtsen Co. v. Johnson*, 343 U.S. 779, 783 (1952). In such cases, “to abrogate a common-law principle, the statute must ‘speak directly’ to the question addressed by the common law.” *United States v. Texas*, 507 U.S. 529, 534 (1993) (quoting *Mobil Oil Corp. v. Higginbotham*, 436 U.S. 618, 625 (1978)). Accordingly, the Supreme Court has instructed courts to follow “[t]he canon of construction that statutes should be interpreted consistently with the common law [to] interpret a statute that clearly covers a field formerly governed by the common law.” *Samantar v. Yousuf*, 560 U.S. 305, 320 (2010).

9. *Marquette Nat’l Bank v. First of Omaha Serv. Corp.*, 439 U.S. 299, 301 (1978). The interest rate exportation provision is often incorrectly referred to in shorthand as preemption of state usury laws, but it is in fact a choice of law provision. Levitin, *supra* note 3, at 350.

usury laws, is really a choice of law provision about which state's usury law applies to a national bank, not about whether a state usury law applies.

The FDIC more modestly argues that its rulemaking is merely consistent with the doctrine.¹⁰ However, the Federal Deposit Insurance Act's 1980 interest rate exportation provision¹¹ is read *in pari materia* with the NBA's 1864 provision.¹² Therefore, to the extent that the doctrine was not incorporated in the NBA's interest rate provision, the FDIC's rulemaking is inconsistent with historical understandings of federal interest rate authority in banking. As of the writing of this Article, litigation brought by several state attorneys general challenging the rulemakings remains pending.¹³

Third, the alleged historicity is used as support for policy arguments in favor of allowing nonbanks to shelter in the statutory usury exemptions of banks. The claim is that the doctrine is critical to ensuring the liquidity of banks and thus the safety of the banking system: the valid-when-made doctrine enables cash-strapped banks to sell their loans to all types of buyers without regard to the interest rate on the loans. Without the doctrine, banks would have a smaller market for their loans because nonbanks would not be able to purchase bank loans made at high interest rates.

If the doctrine lacks historical roots, however, it can hardly be credited with having protected bank liquidity historically. Moreover, as I observe in a companion Article, whatever the source of bank liquidity historically, in the modern world, bank liquidity does not depend on loan sales, but on access to the Federal Reserve's discount

10. Federal Interest Rate Authority, 85 Fed. Reg. at 44,149; Federal Interest Rate Authority, 84 Fed. Reg. 66,845, 66,848 (proposed Dec. 6, 2019) (to be codified at 12 CFR pt. 331). *But see* Statement by FDIC Chairman Jelena McWilliams on the Notice of Proposed Rulemaking: Federal Interest Rate Authority (Nov. 19, 2019), <https://bit.ly/3gCyeIM> [<https://perma.cc/W5P3-TN3W>] (stating that the FDIC's rule is "reaffirming and codifying in regulation the valid-when-made doctrine").

11. 12 U.S.C. § 1831d.

12. *See Greenwood Tr. Co. v. Massachusetts*, 971 F.2d 818, 827 (1st Cir. 1992); Federal Interest Rate Authority, 85 Fed. Reg. at 44,147; FDIC/OCC Amicus Brief, *supra* note 2, at 5–6.

13. Complaint at 5–6, *California v. Off. of the Comptroller of the Currency*, No. 20-cv-5200 (N.D. Cal. July 29, 2020); Complaint at 4–6, *California v. FDIC*, No. 20-cv-5860 (N.D. Cal. Aug. 20, 2020). While this Article was in late stage editing, the district court granted summary judgment for the OCC and FDIC in these cases respectively and denied it to the various state attorneys general. It is unclear if the decision will be appealed. Order Resolving Cross-Motions for Summary Judgment, *California v. Off. of the Comptroller of the Currency*, No. 20-cv-5200 (N.D. Cal. Feb. 8, 2022); Order Resolving Cross-Motions for Summary Judgment, *California v. FDIC*, No. 20-cv-5860 (N.D. Cal. Feb. 8, 2022).

window.¹⁴ Furthermore, even if loan sales were important for bank safety-and-soundness, most bank loans do not violate state usury laws, so they could be sold to all types of entities.¹⁵ And even for loans with higher interest rates, there is still a robust potential market of several thousand banks in the United States, almost all of which are exempt from state usury laws.¹⁶ In short, the valid-when-made doctrine plays no role in protecting bank liquidity, but merely invites evasion of state usury laws. The doctrine's concocted historicity is merely a device for justifying evasion of usury laws.

This Article shows that the valid-when-made doctrine did not and in fact could not have existed historically. This Article commences in Part I.A by discussing the claimed historicity of the doctrine. It then proceeds in Part I.B to show how the doctrine could not have existed prior to 1864 because the situation in which its relevance arises—differential treatment of banks and nonbanks under usury laws—did not exist until 1864.

The Article then turns in Part I.C, to the supposed historical case law support for the doctrine. It shows that there is no reported case consistent with the doctrine prior to 1979. The cases used as support for the doctrine's historical roots are actually dealing with an entirely separate issue in usury law regarding the calculation of interest rates. The valid-when-made doctrine is based on selective, decontextualized quotations from these historical cases.

Part I.D examines the handful of decisions since 1979 consistent with the valid-when-made doctrine. It emphasizes two points about these cases. First, prior to 2019, not a single case evinces any awareness of the existence of the doctrine. Indeed, there is no mention of the doctrine in a reported case until 2019. In fact, the earliest reference to the doctrine in any form is in the *amicus curiae* briefs filed in 2015 by financial services industry trade associations seeking rehearing *en banc* of the decision of the United States Court of Appeals for the Second Circuit in *Madden v. Midland Funding, LLC*.¹⁷ Second, almost all the modern consistent cases are built on a chain of authority founded on a misapplication of an older case's paraphrase of a nineteenth century Supreme Court case addressing an entirely different issue in usury law.

The one modern case not built on this faulty chain of authority is instead based on a misunderstanding of the “stand in the shoes”

14. Levitin, *supra* note 3, at 406.

15. *Id.* at 406–07.

16. *Id.* at 407.

17. *Madden v. Midland Funding, LLC*, 786 F.3d 246 (2d Cir. 2015).

principle of common law of assignments in which an assignee accedes to all of the rights of the assignor in the contract. As discussed in Part II, an assignee can only accede to assignable property rights, not to personal privileges like statutory exemptions from usury laws under the National Bank Act. Put another way, an assignee stands in an assignor's shoes, not in an assignee's feet.

The Article concludes in Part III by showing how the valid-when-made doctrine emerged from the *amicus* briefs filed by financial industry trade associations in the *Madden* litigation. In *Madden*, the Second Circuit held that a nonbank purchaser of loans from a bank could not shelter in the bank's exemption from state usury laws. The valid-when-made doctrine was never raised in either the district court or before the Second Circuit prior to an unsuccessful petition for rehearing or rehearing *en banc*. The argument then appeared again in an unsuccessful petition for *certiorari*, where it was endorsed by the Office of the Solicitor General of the United States and the Office of the Comptroller of the Currency. Once the argument was adopted by the Solicitor General's Office in Supreme Court briefing, it was taken as gospel truth by most commentators. Much of the scholarly writing about the *Madden* decision has presumed the doctrine's supposed historicity and therefore its importance for bank liquidity.¹⁸ More

18. See John Hannon, Note, *The True Lender Doctrine: Function Over Form as a Reasonable Constraint on the Exportation of Interest Rates*, 67 DUKE L.J. 1261, 1263, 1278–79 (2018) (agreeing with, and even extolling, the historicity of valid-when-made); Lenore Palladino, *Small Business Fintech Lending: The Need for Comprehensive Regulation*, 24 FORDHAM J. CORP. & FIN. L. 77, 97 n.127 (2018) (agreeing, in a footnote, with the historicity of the valid-when-made doctrine); Piotr Danisewicz & Ilaf Elard, *The Real Effects of Financial Technology: Marketplace Lending and Personal Bankruptcy* 2, 7–8 (May 15, 2021) (unpublished manuscript), <https://ssrn.com/abstract=3208908> [<https://perma.cc/7SH9-AEJL>] (accepting the historicity of the valid-when-made doctrine alongside an empirical study on the impact of the *Madden* decision credit availability and bankruptcy filings); Daniel Kaplan, Note, *Madden v. Midland Funding, LLC*, 786 F.3d 246 (2d Cir. 2015): *The Second Circuit Threatens To Disrupt Capital Markets*, 8 NEB. L. REV. BULL. 1, 5–8 (2017) (agreeing with the historicity of valid-when-made); Colleen Honigsberg, Robert J. Jackson, Jr. & Richard Squire, *How Does Legal Enforceability Affect Consumer Lending? Evidence from a Natural Experiment*, 60 J.L. & ECON. 673, 674–76 (2017) (conducting an empirical study on the impact of the *Madden* decision on credit availability); Brian Knight, *Federalism and Federalization on the Fintech Frontier*, 20 VAND. J. ENT. & TECH. L. 129, 145, 147–48 (2017) (agreeing with the historicity of the valid-when-made doctrine, describing it as “one of ‘two cardinal rules in the doctrine of usury’” (quoting *Nichols v. Fearson* 32 U.S. (7 Pet.) 103, 109 (1833))); Charles M. Horn & Melissa R. H. Hall, *The Curious Case of Madden v. Midland Funding and the Survival of the Valid-When-Made Doctrine*, 21 N.C. BANKING INST. 1, 6–7, 24 (2017) (accepting of the historicity of valid-when-made, describing it as a valid and dependable legal principle for loan origination, sales, and securitization markets); Angel Rzeslawski, Note, *The National Bank Act and the Demise of State Consumer Laws*, 68 HASTINGS L.J. 1421, 1436–37 (2017) (accepting the valid-when-made doctrine while suggesting that other circuits follow the Second Circuit's lead in *Madden*); Andrew Silvia, Note, *Madden v.*

recent scholarship about the *Madden* decision¹⁹ has been more skeptical about the doctrine's historicity based on some of my previous writings on the topic in the form of congressional testimony,²⁰ an amicus brief,²¹ and an op-ed.²² This Article presents the full story of the invention of the valid-when-made doctrine.

Midland Funding LLC: *Uprooting the National Bank Act's Power of Preemption*, 92 CHI.-KENT L. REV. 653–60 (2017) (agreeing with, and extolling, the historicity of valid-when-made as a cardinal rule of usury law); Zachary Adams Mason, Note, *Online Loans Across State Lines: Protecting Peer-to-Peer Lending Through the Exportation Doctrine*, 105 GEO. L.J. 217, 242 (2016) (accepting with the historicity of valid-when-made); Michael Marvin, Note, *Interest Exportation and Preemption: Madden's Impact on National Banks, the Secondary Credit Market, and P2P Lending*, 116 COLUM. L. REV. 1807, 1832–35 (2016) (claiming that *Madden* ignores Supreme Court precedent on valid-when-made); Kevin Petrasic, Helen Lee & Katherine Lamberth, *Solicitor General in Madden Supports, But Fails To Ensure, the Application of Federal Preemption Doctrine to the Secondary Loan Market and Fate of "Valid-When-Made" Principle*, J. TAX'N & REGUL. FIN. INSTS., May-June 2016, at 41, 42 (agreeing with the historicity of valid-when-made, describing it as "well-established"); Kirby M. Smith, *Banking on Preemption: Allowing National Bank Act Preemption for Third-Party Sales*, 83 U. CHI. L. REV. 1631, 1669–71 (2016) (accepting valid-when-made as a historical doctrine, but stating that context makes older cases merely persuasive, not binding). None of these works make any attempt to distinguish between possible sources of bank liquidity in the nineteenth century and contemporary sources of bank liquidity.

19. See Christopher K. Odet, *Securitizing Digital Debts*, 52 ARIZ. ST. L.J. 477, 532 & n.356 (2020) (agreeing with the historicity and "vital[] importan[ce]" of valid-when-made for fintech companies); Abbye Atkinson, *Rethinking Credit as Social Provision*, 71 STAN. L. REV. 1093, 1115 n.114, 1119 (2019) (taking a neutral position on the historicity of the valid-when-made doctrine while noting the detrimental effects it can have on low-income consumer loan customers); Jayne Munger, Note, *Crossing State Lines: The Trojan Horse Invasion of Rent-a-Bank and Rent-a-Tribe Schemes in Modern Usury Law*, 87 GEO. WASH. L. REV. 468, 488 & n.132 (2019) (disagreeing with the acceptance and application of the valid-when-made doctrine as expressed by *Madden*); Christopher Baiamonte, Note, *Stopping Third-Party Debt Buyers from Using National Bank Act Preemption To Dodge State Usury Laws*, 69 SYRACUSE L. REV. 127, 149–52 (2019) (questioning relevance of valid-when-made because of transactional dissimilarities and the *Erie* doctrine disavowing general federal common law).

20. *Examining Opportunities and Challenges in the Financial Technology ("Fintech") Marketplace Before the Subcomm. on Fin. Inst. & Consumer Credit of the H. Comm. on Fin. Servs.*, 115th Cong. 7–8, 10–12 (2018) (written testimony of Adam J. Levitin, Professor, Georgetown University Law Center), <https://bit.ly/38eYdBI> [<https://perma.cc/8DJ6-4SY9>].

21. Motion for Leave to File Amicus Curiae Brief of Professor Adam J. Levitin in Support of Appellant at 4–5, *Rent-Rite Superkegs W., Ltd. v. World Bus. Lenders, LLC* (*In re Rent-Rite Superkegs W., Ltd.*), 623 B.R. 335 (D. Colo. 2020), No. 1:19-cv-1552. The district court noted it was "convinced" the position advocated by this amicus brief in its Order on Bankruptcy Court's Determination but nevertheless applied the OCC's rule. *In re: Rent-Rite Superkegs W. Ltd.*, 623 B.R. at 340–41. See also *Kaur v. World Bus. Lenders, LLC*, 440 F. Supp. 3d 111, 121 (D. Mass. 2020) (citing the Levitin amicus brief submitted in *In re Rent-Rite Superkegs W., Ltd.*).

22. Adam J. Levitin, "*Madden Fix*" Bills Are a Recipe for Predatory Lending, AM. BANKER (Aug. 28, 2017, 10:24 AM), <https://bit.ly/3b7PRh2> [<https://perma.cc/4KHP-D7RR>].

I. THE SPURIOUS PEDIGREE OF “VALID-WHEN-MADE”

A. *The Purported Historicity of Valid-When-Made*

A central claim made by proponents of the “valid-when-made” doctrine is that it is a “well-established and widely accepted” common law doctrine that is a “cardinal rule” of banking law endorsed by multiple Supreme Court decisions.²³ The doctrine’s deep historical roots have been claimed by the Solicitor General’s Office,²⁴ the OCC and FDIC,²⁵ as well as law firms representing major financial institutions,²⁶ and trade associations.²⁷ The doctrine’s historical basis has been endorsed *sua sponte* by a federal bankruptcy court,²⁸ as well as accepted by much of the scholarly literature.²⁹

The doctrine’s supposed historicity, however, has never actually been probed. An examination of the cases and other sources cited as support for the doctrine shows that the valid-when-made doctrine is utterly lacking in historical roots. The doctrine was unknown to American law until the twenty-first century. The historical sources that

23. See, e.g., FDIC/OCC Amicus Brief, *supra* note 2, at 10.

24. Brief for the United States as Amicus Curiae at 4, *Midland Funding, LLC v. Madden*, 136 S. Ct. 2505 (2016) (No. 15-610) (jointly filed by the Solicitor General and the Office of the Comptroller of the Currency). The Solicitor General opposed a grant of certiorari on the grounds that the case was not a good vehicle, but still held that it was wrongly decided. *Id.* at 13, 17.

25. FDIC/OCC Amicus Brief, *supra* note 2, at 10–13; Permissible Interest on Loans That Are Sold, Assigned, or Otherwise Transferred, 85 Fed. Reg. 33,530, 33,532 (June 2, 2020) (to be codified at 12 C.F.R. pts. 7 & 160); Federal Interest Rate Authority, 85 Fed. Reg. 44,146, 44,149 (July 22, 2020) (to be codified at 12 C.F.R. pt. 331).

26. See, e.g., *OCC Proposes a Rule To Establish When a Bank Is the “True Lender” of a Loan*, SULLIVAN & CROMWELL, LLP (July 24, 2020), <https://bit.ly/3b229aG> [<https://perma.cc/9AZP-272F>] (“For centuries—predating the enactment of the NBA in 1864—caselaw and market practice had established that an interest rate valid at the origination of the loan remained valid even after the originator (whether or not a bank) sold or assigned the loan to another party (whether or not a bank).”); RANDALL D. GUYNN, JAI R. MASSARI & MARGARET E. TAHYAR, DAVIS POLK & WARDWELL, LLP, FEDERAL BANKING REGULATORS CAN AND SHOULD RESOLVE MADDEN AND TRUE LENDER DEVELOPMENTS 1 (Aug. 14, 2018), <https://bit.ly/3n7cSD6> [<https://perma.cc/A2PF-FQG2>] (“A long-settled legal principle known as the ‘valid-when-made’ doctrine has served for almost two centuries as the bedrock for bank lending.”).

27. See, e.g., Marketplace Lenders Ass’n, Comment Letter on Proposed Rule Entitled “Permissible Interest on Loans That Are Sold, Assigned, or Otherwise Transferred” (undated), <https://bit.ly/2Lfwfwu> [<https://perma.cc/BJC5-9BDY>]; Structured Fin. Ass’n & Bank Pol’y Inst., Comment Letter on Proposed Rule Entitled “Federal Interest Rate Authority,” (Feb. 4, 2020), <https://bit.ly/2XmDbed> [<https://perma.cc/KL4W-3322>] (noting “centuries-old fundamental market expectations” based on the valid-when-made doctrine).

28. *Rent-Rite Superkegs W., Ltd. v. World Bus. Lenders, LLC* (*In re Rent-Rite Superkegs W., Ltd.*), 603 B.R. 41, 66 (Bankr. D. Colo. 2019), *rev’d in part*, 623 B.R. 335 (D. Colo. 2020).

29. See *supra* note 18.

supposedly support the doctrine are in fact dealing with an entirely different transactional issue that is unfamiliar to most contemporary lawyers. This makes it easy for the doctrine's proponents to rely on decontextualized quotations from those older cases to claim a pedigree for a doctrine that fits their policy preferences, namely an aversion to usury laws as an inefficient, paternalist intervention in freedom of contract.³⁰ Few modern lawyers would readily understand the transactional situation in the historical cases and therefore understand that the quoted language is simply irrelevant to the claimed doctrine.

B. Impossibility of Valid-When-Made Before 1864

As an initial matter, the claim that valid-when-made was part of the common law background of the NBA runs into the problem that the doctrine could not possibly have existed prior to the enactment of the NBA in 1864 because there was no situation in which it could have arisen.

Valid-when-made is a doctrine that addresses an issue that arises when the choice of the applicable usury law depends on the entity type of the lender. Prior to 1864, the application of usury laws did not depend on the entity type of the lender. That distinction arose only because of the NBA itself.

To be sure, there was an *antebellum* interstate lending market, and there were differences among the rates allowed under *antebellum* state usury laws. The applicable usury law, however, did not depend on the identity of the lender. Instead, the applicable law was generally the law of the state where the contract was made (*lex loci contractus*),³¹ and the application of state usury laws did not distinguish among lender entity types. Therefore, it was not possible prior to 1864 for a loan to be non-usurious in the hands of a bank, yet be usurious in the hands of a nonbank assignee merely by virtue of an assignment. Assignment would have had no effect on the choice of law because state usury laws did not differentiate among lender entity types. Based on the *lex loci contractus* principle, the law would have subjected both the bank and

30. The valid-when-made doctrine does not challenge the validity of usury laws directly. Instead, it merely enables an indirect evasion of them, suggesting that the doctrine's proponents are ultimately instrumental, not principled, in their support of the doctrine.

31. JAMES AVERY WEBB, A TREATISE ON THE LAW OF USURY, AND INCIDENTALLY, OF INTEREST § 256 (1899). There was an exception if the contract specified that performance was to occur in another state, which case the law of the state of performance (*lex loci solutionis*) would control, subject to an anti-evasion principle. *Id.* §§ 256, 261, 265; *Miller v. Tiffany*, 68 U.S. 298, 308 (1864).

the nonbank assignee to the usury law of the state where the contract was made.

The impossibility of a valid-when-made situation prior to 1864 should alone indicate that none of the *antebellum* cases on which the doctrine supposedly rests (considered in more detail in the next section) have anything to do with the issue. The “valid-when-made” doctrine could not be background law against which the NBA was enacted because the situation that the doctrine purports to address was in fact created by the NBA.

C. *The Absence of “Valid-When-Made” in Pre-1979 Cases*

The valid-when-made doctrine is not actually mentioned as such in any reported case until 2019,³² and only starts to appear in pleadings in 2015.³³ The first case whose holding is even consistent with the doctrine only appears in 1979,³⁴ but that case qualifies the doctrine with an anti-evasion principle to prevent the doctrine from being used to allow nonbank assignees from partnering with banks to launder usurious loans.³⁵ Other cases clearly consistent with a valid-when-made doctrine can only begin to be observed in the 2000s.³⁶ In other words, cases clearly consistent with the doctrine do not emerge until twenty years after the enactment of the FDIA’s interest rate exportation provision and 140 years after the NBA’s interest rate exportation provision.

The doctrine’s proponents cite a large number of pre-1979 historical cases as supporting the doctrine, but they never actually discuss the details of the historical cases. Instead, the historical cases appear only as supporting citations for claims about the doctrine with decontextualized quotations provided in parentheses to the citations.

So what are the historical cases claimed to support the doctrine actually about? The historical cases address three distinct issue patterns, none of which have anything to do with “valid-when-made.” Instead, they are dealing with three different problems in the law of usury that relate to the question of how to calculate the interest rate on a loan, not the question of which state’s usury law applies to the loan. These problems are the discounted assignment, the payment option, and the cleansing assignment. They are addressed in turn below. These

32. See *In re Rent-Rite Superkegs W., Ltd.*, 603 B.R. at 66.

33. See *infra* Part III.

34. *Strike v. Trans-West Discount Corp.*, 155 Cal. Rptr. 132, 139 (Cal. Ct. App. 1979).

35. See *infra* Part I.D.

36. See *infra* Part I.D.

cases are dragooned into supporting “valid-when-made” and the associated deregulatory policy agenda through selective, decontextualized quotations, but when seen in context, none of the historical cases supports the claimed doctrine.

The first set of historical cases falls into a “discounted assignment” pattern.³⁷ This pattern of case deals with *two* credit transactions, not one. The issue is whether the interest from the second transaction will be attributed to the first transaction, potentially rendering the first transaction usurious. The general historical pattern involves a loan (credit transaction #1) and a discounted sale or pledge of the note from the initial loan (credit transaction #2).

The unfamiliar move to modern readers is that a discounted sale of a note with recourse transaction was historically a common type of credit transaction. Frequently, this was done through indorsement—the practice of the seller of the note signing his name on the back (*in dorso*) of the note. Indorsement would make the seller co-liable on the note in its face amount. Thus, if the seller indorsed a note from obligor due in one year with a face amount of \$120 and a 0% interest rate for \$100 (with the discount reflecting repayment risk), it is equivalent to the buyer making a \$100 loan to the seller at 20% annual simple interest. In either case, the buyer would have parted with \$100 and would have a right to collect \$120 in a year, from either the obligor or

37. One such case is *Munn v. Commission Co*, 15 Johns. 44, 55 (N.Y. Sup. Ct. 1818), where the New York Supreme Court of Judicature noted that:

The principle is too well settled to be questioned, that a bill, free from usury, in its concoction, may be sold at a discount, by allowing the purchaser to pay less for it than it would amount to at the legal rate of interest, for the time the bill has to run. The reason is obvious: as the bill was free from usury, between the immediate parties to it, no after transaction with another person can, as respects those parties, invalidate it.

Id. See also *Taylor v. Bruce*, 21 Va. 42, 90 (1820) (“[I]t is settled, that a bill or note which is free from usury, in its concoction, may be sold at an usurious discount, for that as it was free from usury between the original parties, no after transaction can, as to these parties, invalidate it”); *Tuttle v. Clark*, 4 Conn. 153, 157 (1822) (stating that because “the note was not usurious in its original concoction, or made with an usurious intent,” a discounted sale did not invalidate it); *Knights v. Putnam*, 20 Mass. 184, 185 (1825) (“[A] note, valid in its inception, may be recovered against the maker, by an indorsee, although discounted by him at a rate exceeding legal interest. It is a well established principle, that if a note or security is valid when made, no usurious transaction afterwards between the parties or privies will affect its validity.” (footnote omitted)); *Cram v. Hendricks*, 7 Wend. 569, 572 (N.Y. 1831) (“The principle is too well settled to be questioned, that a bill free from usury in its concoction may be sold at a discount; because, as it was free from usury between the original parties to it, no subsequent transaction with another person can, as it respects those parties, invalidate it.”).

the seller. Thus, when a note is sold at a discount from its face amount, the discount can be treated as imputed prepaid interest.³⁸

The issue in the discounted assignment cases is whether the interest imputed by the discounting (credit transaction #2) should be added to the interest on the face of the note (credit transaction #1) for the purpose of determining whether the note is itself usurious. Using the example above, should the obligor's obligation on the note be treated as having a 0% interest rate or a 20% interest rate for purposes of usury law? It depends on whether the note is viewed from the obligor's perspective (0% interest) or the buyer's perspective (20% interest).

Critically, this issue has nothing to do with the question of which jurisdiction's usury law applies. Instead, it is a question of how to calculate the applicable interest rate for usury purposes. The discounted assignment caselaw necessarily involves two separate credit transactions, and the question of whether the interest from the second credit transaction is to be attributed to the first transaction. In contrast, whereas the modern applications of valid-when-made, such as a sale of a defaulted loan, involve two transactions, only one is a credit transaction. In modern valid-when-made cases, the second transaction, even if discounted, is treated as a straight sale, not an implied credit transaction, so the issue of whether interest from the second transaction can be imputed to the first never arises. Instead, the valid-when-made issue is dealing with the wholly distinct question of whether a purchaser can shelter in the statutory privileges of the seller.

The two nineteenth century Supreme Court cases generally cited as the basis for the valid-when-made doctrine's historical pedigree, *Gaither v. Farmers & Mechanics Bank of Georgetown*³⁹ and *Nichols v. Fearson*,⁴⁰ both fall into the "discounted assignment" paradigm. *Gaither* involved a non-usurious note that was pledged by the payee as

38. *Nat'l Bank v. Johnson*, 104 U.S. 271, 276–77 (1881); *Evans v. Nat'l Bank of Savannah*, 251 U.S. 108, 114 (1919). Section 85 of the National Bank Act covers not only interest on loans, but also interest on discounts. 12 U.S.C. § 85; *See also* *Daniel v. First Nat'l Bank of Birmingham*, 227 F.2d 353, 355–56 (5th Cir. 1955) (addressing whether a discount was usurious), *reh'g denied with opinion*, 228 F.2d 803 (5th Cir. 1956). The idea of a discount being treated as imputed interest is still regularly applied today in the tax and bankruptcy law, where "original issue discount" on bonds is treated as imputed interest. *See, e.g.*, *Treas. Reg. § 1.61-7(c)*; *LTV Corp. v. Valley Fidelity Bank & Tr. Co. (In re Chateaugay Corp.)*, 961 F.2d 378, 380 (2d Cir. 1992); *Tex. Com. Bank v. Licht (In re Pengo Indus. Inc.)*, 962 F.2d 543, 546 (5th Cir. 1992). Under tax and bankruptcy law, secondary market discounts are not treated as imputed interest, however, only discounts at issuance.

39. *Gaither v. Farmers & Mechs. Bank of Georgetown*, 26 U.S. (1 Pet.) 37 (1828).

40. *Nichols v. Fearson*, 32 U.S. (7 Pet.) 103 (1833).

collateral for an unrelated, usurious loan.⁴¹ The Supreme Court observed that “the rule cannot be doubted, that if the note be free from usury, in its origin, no *subsequent usurious transactions respecting it*, can affect it with the taint of usury.”⁴² The key point to note here is that *Gaither* does not say “no subsequent transactions,” but no “subsequent *usurious* transactions.”

Gaither involved a situation in which there were two credit transactions—the making of a non-usurious note and the making of a usurious loan. The issue was whether the usurious interest from the second transaction could be imputed to the first transaction. In contrast, the “valid-when-made” situation deals with a *single* loan that is assigned. There is no “subsequent usurious transaction” to speak of in the “valid-when-made” context. *Gaither* did not involve an assignment and says nothing about the “valid-when-made” situation.

Nor is the valid-when-made doctrine supported by the other nineteenth century Supreme Court case, *Nichols v. Fearson*. *Nichols* involved a discounted sale of a note indorsed by the defendant.⁴³ When the defendant in *Nichols* indorsed the note, the defendant became jointly liable for the full face amount of the note, just as if it were the maker of the note.⁴⁴ The defendant then attempted to wriggle out of its obligation by raising a defense of usury on the basis that the stated interest rate on the note plus the additional implied interest rate from the discounting made the note usurious.⁴⁵ The Supreme Court held that the usurious discounting did not void the original note,⁴⁶ observing that among the “cardinal rules of the doctrine of usury . . . [is] that a contract, which, in its inception, is unaffected by usury, can never be invalidated by any *subsequent usurious transaction*.”⁴⁷

Again, the key point to note is that the Supreme Court did not use the phrase “any subsequent transaction,” but “any subsequent *usurious* transaction.” As with *Gaither*, *Nichols* involved a situation in which there were *two* credit transactions—the making of a non-usurious note and a usurious discounting (effectively a second loan). All *Nichols* holds is that the interest from the second transaction (the

41. *Gaither*, 26 U.S. at 41–42.

42. *Id.* at 43 (emphasis added).

43. *Nichols*, 32 U.S. at 105.

44. *Id.* at 107. *Cf.* U.C.C. § 3-415(a) (modern statutory analog).

45. *Nichols*, 32 U.S. at 105–06.

46. *Id.* at 110, 112.

47. *Id.* at 109 (emphasis added). *See also id.* at 106 (“[T]he rule of law is every where [sic] acknowledged, that a contract, free from usury in its inception, shall not be invalidated by any *subsequent usurious transactions upon it*.” (emphasis added)).

discounting) may not be imputed to the first transaction (the note). Modern valid-when-made cases do not involve any claim that the second transaction—the sale of the note—is in fact a credit transaction, even if the sale is made at a discount. There is no claim in modern valid-when-made cases that implicit interest in a discounted assignment of a note is imputed to the note itself. Thus, *Nichols* has nothing to do with the valid-when-made doctrine question of whether a bank can transfer its statutory interest rate exportation privilege to an assignee to allow the assignee to purchase and enforce a loan that the assignee could not legally make itself.

Nichols and *Gaither*—the Supreme Court cases that follow the “discounted assignment” pattern—are the primary historical cases cited in support of the “valid-when-made” doctrine.⁴⁸ The cases from the other two patterns play only a supporting role, consigned to string-cites and footnotes.⁴⁹ A quick review of these patterns shows why—they plainly have nothing to do with “valid-when-made” as would be obvious from any discussion of the facts of the cases.

The second set of historical cases involve a “payment option” pattern. These cases deal with the effect of the exercise of a payment option by the borrower on the calculation of the interest rate on a loan.⁵⁰ The option might be an option to pay in a different form of consideration or to pay late or to prepay. These cases do not even necessarily involve an assignment of the loan, underscoring that they are not about a valid-when-made issue whatsoever. For example, in

48. See *infra* Part I.D.

49. See *infra* notes 102–103 and accompanying text.

50. See, e.g., *Tate v. Wellings* (1790) 100 Eng. Rep. 716, 721 (opinion of Buller, J.) (discussing the effect on the usury calculation of a loan of stock that was repayable in stock or cash at the borrower’s option); *Unity Plan Fin. Co. v. Green*, 155 So. 900, 905 (La. 1934) (noting the effect on the calculation of the interest from the acceleration of a debt that the debtor had failed to repay on time); *FDIC v. Tito Castro Constr., Inc.*, 548 F. Supp. 1224, 1227 (D.P.R. 1982) (“[I]t was only as a consequence of defendant’s election to delay in repaying the principal amount of those [demand] notes that an effective rate of interest in excess of the Puerto Rico statutory ceiling may have resulted.”); *Rangen, Inc. v. Valley Trout Farms, Inc.*, 658 P.2d 955, 959 (Idaho 1983) (discussing the effect on usury calculation of a fee for late payment option); *Sw. Concrete Prods. v. Gosh Constr. Corp.*, 798 P.2d 1247, 1252 (Cal. 1990) (“[A] transaction that was not usurious at its inception cannot become usurious by virtue the debtor’s voluntary default.”); *Zang v. Schumann*, 55 N.W.2d 864, 867–69 (Wis. 1952) (stating that a borrower’s exercise of an option to pay an extra premium to be relieved from a lease was not to be considered in the calculation of the interest rate); *Saul v. Midlantic Nat’l Bank/South*, 572 A.2d 650, 658 (N.J. Super. Ct. App. Div. 1990) (discussing whether the value of a non-optional discounted stock sale accompanying the loan should be included in the interest for the loan); *Hoffman v. Key Fed. Sav. & Loan Ass’n*, 416 A.2d 1265, 1269 (Md. 1979) (discussing whether an optional prepayment should affect the calculation of the interest rate).

Hoffman v. Key Federal Saving & Loan Association,⁵¹ the Maryland Supreme Court considered whether an optional prepayment should affect the calculation of the interest rate.⁵² The court held that it did not, noting “[t]he virtually universal rule is that a contract legal at its inception will not be rendered usurious by voluntary prepayment.”⁵³ As with the “discounted assignment” pattern, the issue in these cases is about *how* to calculate the interest rate on a loan, not about what law applies to the transaction.

Finally, there is a set of cases involving a “cleansing assignment” pattern. These cases deal with the effect of a valid assignment or other subsequent valid transaction on a usurious loan. This pattern is the reverse transaction of what is at stake with valid-when-made, as the question is whether an initially invalid loan can be cured by a subsequent transaction.⁵⁴ For example, in *Coral Gables First National Bank v. Constructors of Florida, Inc.*,⁵⁵ the Florida Court of Appeals addressed whether the renewal of a usurious loan on non-usurious terms cured the initial usury violation.⁵⁶ These cleansing assignment cases deal with the reverse of the valid-when-made situation: they address a situation where a loan is initially *invalid*-when-made. As such, they tell us nothing about the existence of a valid-when-made doctrine.

The valid-when-made doctrine’s lack of historical basis may also be observed by its absence from historical treatises on banking and usury. If the “valid-when-made” doctrine were a “cardinal rule” of banking law, founded on Supreme Court opinions, one would expect it to regularly appear in nineteenth and twentieth century usury and banking law treatises. Yet the doctrine is entirely unknown to historical treatise writers. No prior reference to “valid-when-made” can be found

51. *Hoffman v. Key Fed. Sav. & Loan Ass’n*, 416 A.2d 1265 (Md. 1979).

52. *Id.* at 1267–69.

53. *Id.* at 1269.

54. *Watkins v. Taylor*, 16 Va. (2 Munf.) 424, 436, 438–40 (Va. 1811) (Coalter, J. dissenting) (effect of payment by surety on surety’s subrogation claim on usurious contract); *Highway Equip. & Supply Co. v. Jones*, 153 N.W.2d 859, 863 (Neb. 1967) (addressing whether usury in the initial transaction was purged by an assignment); *Coral Gables First Nat’l Bank v. Constructors of Fla., Inc.*, 119 So. 2d 741, 746 (Fla. Dist. Ct. App. 1960) (addressing the effect of renewal of a usurious loan on non-usurious terms); *Waggener v. Holt Chew Motor Co.*, 274 P.2d 968, 971 (Colo. 1954) (en banc) (addressing whether a lender’s acquisition of a required license after making loan at rate above that allowed for unlicensed lenders cured the usury violation).

55. *Coral Gables First Nat’l Bank v. Constructors of Fla., Inc.*, 119 So. 2d 741 (Fla. Dist. Ct. App. 1960)

56. *Id.* at 746.

in *any* nineteenth or twentieth century banking or usury treatise.⁵⁷ Instead, what is found in treatises are restatements of the discounted assignment pattern.⁵⁸

D. The Erroneous Basis of Modern “Valid-When-Made” Decisions

Although the first mention of the “valid-when-made” doctrine was only in 2015, there are a handful of earlier cases that are consistent with the proclaimed doctrine. Critically, however, these cases are all from the late twentieth century or twenty-first century, meaning that there are no cases consistent with the doctrine that pre-date the National Bank Act. The first case to fit within the “valid-when-made” doctrine is a 1979 California appellate decision, *Strike v. Trans-West Discount Corp.*,⁵⁹ involving an assignment of a loan from a bank (exempt from California usury law by the California Constitution) to a nonbank that was normally subject to California usury law.⁶⁰ The California Court of Appeals held that the transfer of the loan did not change its status vis-à-vis the usury laws, but suggested that the

57. To be sure, proponents of the doctrine cite to language from an 1838 edition of Blackstone’s COMMENTARIES ON THE LAWS OF ENGLAND for support: “[t]he usury must be part of the contract in its inception’ for a contract to be deemed usurious.” FDIC/OCC Amicus Brief, *supra* note 2, at 10 (citing 1 WILLIAM BLACKSTONE, COMMENTARIES ON THE LAWS OF ENGLAND 379 n.32 (18th London ed., W.E. Dean 1838)). But the quoted language does not appear in Blackstone’s original treatise. Instead, it is from a later annotator’s footnote. Nor does it actually provide much support the “valid-when-made” doctrine. The footnote cites two English cases. BLACKSTONE, *supra*. The first, *Lowes v. Mazzaredo* (1816) 171 Eng. Rep. 505, 505, 1 Stark. 385, 386, dealt with usurious discounting of a non-usurious bill of exchange, which was held not to affect the validity of the bill of exchange. *Mazzaredo* is squarely within the discounted assignment pattern (pattern 1). The second case, *Lowe v. Waller* (1781) 99 Eng. Rep. 470, 470–71, 2 Dougl. 736, 736–38, dealt with whether a good faith assignee of a usurious bill of exchange is subject to the defense of usury (pattern 3). This case fits neatly in the cleansing assignment pattern. Both cases are uninformative about the “valid-when-made” doctrine.

58. JOSEPH CHITTY, A PRACTICAL TREATISE ON BILLS OF EXCHANGE, CHECKS ON BANKERS, PROMISSORY NOTES, BANKERS’ CASH NOTES, AND BANK NOTES *105 (5th ed. 1821) (“In general, a *subsequent* illegal contract or consideration of any description, taking place in a second indorsement or transfer of a bill, and not in its inception, nor in a transfer through which the holder must make title, will not invalidate the same, in the hands of a bona fide holder.” (emphasis in original)). See also ROBERT BUCKLEY COMYN, A TREATISE ON THE LAW OF USURY 187 (1817) (“As a security or contract which is usurious in its inception must always retain its unsoundness; so on the other hand, where the security or contract has been originally valid, no subsequent taking of, or contract to take, illegal interest will invalidate it; although by such taking the party absolutely incur the penalty of the statute.”); JAMES AVERY WEBB, *supra* note 31, at § 306 (“A contract, free from usury at its execution, cannot be rendered invalid by any subsequent usurious agreement between the same or other persons. A subsequent agreement may be usurious in itself and thereby become either wholly or partly nugatory; but its fate cannot be visited upon the original valid contract.”).

59. *Strike v. Trans-West Disc. Corp.*, 155 Cal. Rptr. 132 (Cal. Ct. App. 1979).

60. *Id.* at 139.

outcome would be different if the loan had been intended for assignment from the outset.⁶¹ This is a sensible articulation of an anti-evasion position that ensures the liquidity of bank loans, but also prevents abuse of federal preemption through rent-a-bank arrangements and the like. The court in *Strike* expressed no awareness of a valid-when-made doctrine.

After *Strike*, only a handful of late twentieth century or twenty-first century cases are arguably consistent with the “valid-when-made” doctrine.⁶² As with *Strike*, none of these cases express any awareness of the supposedly long-standing, cardinal doctrine. And all but one of those cases are part of a chain of cases, commencing with the Fifth Circuit’s 1981 decision in *FDIC v. Lattimore Land Corporation*,⁶³ that misread the Supreme Court’s 1833 decision in *Nichols v. Fearson*.⁶⁴

Lattimore dealt with a choice of law question regarding what state’s law applied to the bank assignee of a loan made by a nonbank.⁶⁵ In other words, it was not actually dealing with a valid-when-made situation, but the inverse.⁶⁶ In *Lattimore*, however, the Fifth Circuit stated, “[t]he non-usurious character of a note should not change when the note changes hands.”⁶⁷ This proposition is given without any analysis, but is supported by a footnote that is worth examining in detail. The footnote that reads:

This Court long ago observed that: “If, in its inception, the contract which that instrument purported to evidence was unaffected by usury,

61. *Id.* The California Court of Appeals cited to *Calimpc, Inc. v. Warden*, 224 P.2d 421 (Cal. Ct. App. 1950), which noted that

If [an assignee cannot be held liable for accepting usurious interest], the statutes on usury might as well be abolished. All a lender would have to do would be to obtain a contract from a borrower providing for usurious interests . . . and then assign his contract and the contract would no longer be usurious.

Id. at 433. *See also* *Miller v. Tiffany*, 68 U.S. 298, 310 (1864) (noting that contractual choice of law provisions for usury are enforceable, but when done with intent to evade the law, law of the contract location applies).

62. *See* *Munoz v. Pipestone Fin., LLC*, 513 F. Supp. 2d 1076, 1078–79 (D. Minn. 2007); *Olvera v. Blitt & Gaines, P.C.*, 431 F.3d 285, 287–89 (7th Cir. 2005); *Phipps v. FDIC*, 417 F.3d 1006, 1013–14 (8th Cir. 2005); *Krispin v. May Dep’t Stores Co.*, 218 F.3d 919, 924 (8th Cir. 2000).

63. *FDIC v. Lattimore Land Corp.*, 656 F.2d 139 (5th Cir. Unit B Sept. 1981).

64. The exception is *Olvera v. Blitt & Gaines, P.C.*, 431 F.3d 285 (7th Cir. 2005). *See infra* Part II.

65. *Lattimore Land Corp.*, 656 F.2d at 148–49.

66. *Lattimore* also made clear that its analysis would have been different if there had been an allegation that the assignee was the true lender. *Id.* at 148 n.15 (“The present case differs from *Daniels* in that here the obligors assumed that the allegedly usurious instrument called for non-usurious interest when held by the initial obligee and the obligors have never claimed that Hamilton National Bank was the lender in fact.”).

67. *Id.* at 148–49.

it was not invalidated by a subsequent transaction.” *Huntsman v. Longwell*, 4 F.2d 105, 106 (5th Cir. 1925). This proposition was articulated by the Supreme Court as one of the “cardinal rules in the doctrine of usury.” *Nichols v. Fearson*, 32 U.S. 103, 109–11 (1833).⁶⁸

Yet we have already seen that *Nichols v. Fearson* had nothing to do with valid-when-made. The same is true of *Huntsman v. Longwell*,⁶⁹ which like *Nichols*, deals with the issue of whether interest from a second transaction can be imputed to the original transaction for purposes of calculating whether the first transaction violated the usury statute. In *Huntsman*, the borrower raised a usury defense.⁷⁰ On its face, the loan was in compliance with the usury cap.⁷¹ The day after the loan agreement was made, however, the borrower had agreed in a separate contract to assume certain debts of the lender as part of the consideration of the loan.⁷² The effect of this second, subsequent agreement, the borrower claimed, was to make the real interest rate on the loan (the first agreement) usurious.⁷³

Huntsman correctly cites to *Nichols* as supporting the idea that imputed interest from transaction #2 cannot be bundled with interest from transaction #1 to result in a combined interest rate that violates the usury cap.⁷⁴ *Huntsman* cites *Nichols* for the proposition that:

If, in its inception, the contract which that instrument purported to evidence was unaffected by usury, it was not invalidated by a subsequent transaction.⁷⁵

This paraphrasing, however, omits a critical word from *Nichols* (underlined below), which actually made a more limited claim:

[A] contract, which, in its inception, is unaffected by usury, can never be invalidated by any subsequent usurious transaction.⁷⁶

In *Huntsman* itself, that omission was of no consequence because it followed the same broad pattern as *Nichols*. The *Lattimore* court,

68. *Id.* at 149 n.17 (citation omitted).

69. *Huntsman v. Longwell*, 4 F.2d 105 (5th Cir. 1925).

70. *Id.* at 106.

71. *Id.*

72. *Id.*

73. *Id.* The issue before the court in *Huntsman* was related to the admissibility of evidence regarding the second contract. *Id.*

74. *Id.* (citing *Nichols v. Fearson*, 32 U.S. [7 Pet.] 103 (1833)).

75. *Id.* (citing *Nichols*, 32 U.S. 103).

76. *Nichols*, 32 U.S. at 109 (emphasis added).

however, failed to understand that *Huntsman* and *Nichols* stood for a very limited point.

Nearly all of the subsequent cases twenty-first century valid-when-made cases rely on *Lattimore*'s misreading as their foundational authority. For example, *Munoz v. Pipestone Financial, LLC*,⁷⁷ was a case with similar facts to *Madden*: a suit by a consumer alleging that the debt buyer that purchased his credit card debt was violating the Fair Debt Collection Practices Act by attempting to collect a usurious debt.⁷⁸ *Munoz* disposed of the issue with no analysis other than a quotation of *Phipps v. FDIC*⁷⁹ for the point that “[c]ourts must look at ‘the originating entity (the bank), and not the ongoing assignee . . . in determining whether the NBA applies.’”⁸⁰

Phipps involved a usury suit against a nonbank assignee of a national bank, but it too has no original analysis.⁸¹ Instead, the sentence in *Phipps* that *Munoz* quoted is in turn a quotation from *Krispin v. May Department Stores Co.*⁸² The facts of *Krispin* are not clearly presented in the Eighth Circuit's opinion, but become clear when read in conjunction with the District Court's opinion.⁸³ *Krispin* dealt with a situation in which a national bank originated credit card loans, but assigned the receivables on a daily basis to an affiliated department store.⁸⁴ The borrower in *Krispin* claimed that the late fees applied to its account were collected by the department store in violation of state usury laws.⁸⁵ The Eighth Circuit held that although “the NBA governs only national banks,” “the store's purchase of the bank's receivables does not diminish the fact that it is now the bank, and not the store, that issues credit, processes and services customer accounts, and sets

77. *Munoz v. Pipestone Fin., LLC*, 513 F. Supp. 2d 1076 (D. Minn. 2007).

78. *Id.* at 1078.

79. *Phipps v. FDIC*, 417 F.3d 1006 (8th Cir. 2005).

80. *Munoz*, 513 F.3d at 1079 (alteration in original) (quoting *Phipps*, 417 F.3d at 1013).

81. *Phipps*, 417 F.3d at 1009, 1013.

82. *Id.* at 1013 (quoting *Krispin v. May Dep't Stores Co.*, 218 F.3d 919, 924 (8th Cir. 2000)).

83. The credit card accounts in question had originally been opened with the nonbank department store, which subsequently assigned the accounts to its national bank affiliate, which then assigned on a daily basis any receivables that were created on the accounts to the department store. *Matheis v. May Dep't Stores Co.*, No. 4:98-cv-01722, 1999 U.S. Dist. LEXIS 21917, at *2–4 (E.D. Mo. May 21, 1999), *rev'd and remanded sub. nom* *Krispin v. May Dep't Stores Co.*, 218 F.3d 919 (8th Cir. 2000). The plaintiffs were only alleging usury violations for late fees that arose subsequent to their accounts being assigned to the national bank, *id.* at *2–3, so the fact that the accounts were originally opened with the nonbank department store had little legal bearing on the usury issue but gets elided in the Eighth Circuit's opinion. *See Krispin*, 218 F.3d at 923.

84. *Krispin*, 218 F.3d at 923.

85. *Matheis*, 1999 U.S. Dist. LEXIS 21917, at *2-3.

such terms as interest and late fees.”⁸⁶ Citing to *Lattimore*, the Eighth Circuit held that “in these circumstances . . . it makes sense to look to the originating entity (the bank), and not the ongoing assignee (the store), in determining whether the NBA applies.”⁸⁷ Based on this, the Eighth Circuit held that the “real party in interest is the bank, not the store.”⁸⁸ In other words, *Krispin* has nothing to do with valid-when-made because the ruling was not based on the effect of the assignment on the application of usury laws. It is instead a “true lender” decision regarding which party should be considered the lender for purposes of the application of usury laws. The clear implication of *Krispin* is actually contrary to valid-when-made: if the facts had indicated that nonbank department store was the real party in interest, then the store could not have sheltered in the National Bank Act.

II. THE “STAND-IN-THE-SHOES” PRINCIPLE

The only major modern “valid-when-made” case that does not stand on this misreading of *Nichols* is the 7th Circuit’s decision in *Olvera v. Blitt & Gaines, P.C.*⁸⁹ *Olvera*, however, does not actually embrace valid-when-made, but instead arrives at a similar result through a common law of assignment theory, namely that because the assignee of a contract takes all of the assignor’s rights under that contract, a nonbank assignee accedes to the bank assignor’s usury exception for a loan.⁹⁰

This argument, echoed by other valid-when-made proponents,⁹¹ reflects a fundamental misunderstanding of the common law of assignments. The common law of assignments relates solely to the assignment of rights under a contract or property rights. An assignee takes all of the rights of the assignor *under the contract*.⁹² An assignee does not, however, assume the assignor’s other rights extraneous to the contract, such as rights under licenses or from status. For example, if I sell my car, the buyer gets whatever rights are appurtenant to the car,

86. *Krispin*, 218 F.3d at 924.

87. *Id.* (citing *FDIC v. Lattimore Land Corp.*, 656 F.2d 139, 147–49 (5th Cir. Unit B Sept. 1981)).

88. *Id.*

89. *Olvera v. Blitt & Gaines, P.C.*, 431 F.3d 285 (7th Cir. 2005) (Posner, J.).

90. *Id.* at 288–89.

91. FDIC/OCC Amicus Brief, *supra* note 2, at 14–16; Federal Interest Rate Authority, 84 Fed. Reg. 66,845, 66,848 (proposed Dec. 6, 2019) (to be codified at 12 CFR pt. 331).

92. See Restatement (2d) of Contracts § 317(2) (AM. L. INST. 1981) (“A contractual right can be assigned . . .” (emphasis added)); 29 WILLISTON ON CONTRACTS § 74:10 (4th ed.) (“Generally, all contract rights may be assigned . . .” (emphasis added)).

but does not also get my driver's license or the benefits of my American Automobile Association membership, much less my parental or spousal rights. Similarly, if a credit union sells a loan, the buyer does not assume the credit union's statutory tax-exempt status.⁹³ The assignee "steps into the shoes" of the assignor. It does not step into the assignor's "feet." Thus, the common law of assignment has no bearing on regarding a transfer of federal statutory status or privileges, as those are neither contract nor property rights.

Banks' exemptions from state usury laws, whether under the NBA or FDIA, are statutory rights;⁹⁴ they are not contractual terms in a loan agreement. These exemptions are not alienable property rights. Neither are they characteristics of the loan that travels with the note; they are nowhere to be found in the loan documents. Instead, NBA and FDIA preemption is a personal and non-transferrable privilege that is part of a legal scheme that applies only to banks. Indeed, NBA and FDIA preemption does not void state usury laws—state usury laws remain valid and in effect for nonbanks, and in the case of FDIA, states even retain the right to opt-out of the provision.⁹⁵ Instead, NBA and FDIA "preemption" are not true preemption. It merely allows banks to export the usury cap of their home state into other states.

Because the exemption from state usury laws is in essence a personal privilege, not a property right, it is no more assignable than a medical license, a tax-exempt status, FDIC insurance, or Federal Reserve System discount window access. Indeed, if these privileges were freely assignable, there would be no point in having a bank licensing regime because regulators would not exercise control over who ultimately gained the privileges attached to the license. Accordingly, the common law of assignments has nothing whatsoever to do with the assignability of exemptions from usury laws.

III. THE MODERN ORIGINS OF VALID-WHEN-MADE

The valid-when-made doctrine cannot be discerned as a known doctrine until the late stages of the *Madden v. Midland Funding* litigation when the financial services trade associations began to be

93. Were it otherwise, then credit unions would be able to sell tax-exempt status to everyone merely by selling off a small piece of a loan.

94. See 12 U.S.C. §§ 85, 1831d.

95. See Depository Institutions Deregulation and Monetary Control Act of 1980, H.R. 4986, 96th CONG. § 525 (1980) (providing that the effective period for the provisions terminates when a state adopts a provision "which states explicitly and by its terms that such [s]tate does not want the amendments made by such sections to apply with respect to loans made in such [s]tate").

involved as *amici curiae*.⁹⁶ Midland Funding did not claim the existence of any such doctrine in its trial court briefing or its initial appellate briefing. Midland Funding's motion for summary judgment cited to some of the modern cases that support the doctrine, but never once named the doctrine or claimed that there was an overarching doctrine.⁹⁷ Notably, it failed to cite any nineteenth century cases or claim deep historical roots for a doctrine. It was the district court, *sua sponte*, that first raised *Nichols v. Fearson*,⁹⁸ but in its appellate brief, Midland Funding all but disowned *Nichols*, stating that *Nichols* "was not central to the [district court's] decision and does not change the analysis at all."⁹⁹

After Midland Funding lost the appeal before the Second Circuit, however, it engaged a heavy hitter appellate specialist, Kannon K. Shanmugam, from Williams & Connolly, LLP, who filed a petition for rehearing or rehearing *en banc*.¹⁰⁰ That petition is the first time the historical roots of the doctrine were claimed, and the first time it was called a "fundamental principle of usury law."¹⁰¹

The real historical claim, however, only emerged in an amicus brief filed on behalf of several financial services trade associations by Sullivan & Cromwell, LLP.¹⁰² Citing *Gaither* and *Nichols*, as well as a

96. The first reference to any sort of a valid-when-made doctrine can be found in a 2012 brief in a California rent-a-bank case involving First Bank of Delaware. Defendant First Bank of Delaware's Supplemental Brief in Opposition to Plaintiff's Motion to Compel Production of Documents at 4, *People v. Check'n Go of California, Inc.* (No. CGC-07-462779), 2012 Cal. Sup. Ct. Motions LEXIS 42469, at *7 (Cal. Super. Ct. May 11, 2012) [hereinafter Defendant First Bank of Delaware's Supplemental Brief]. First Bank of Delaware was the rent-a-bank partner of Think Finance. Levitin, *supra* note 3, at 372. But the claim in that case was only that the doctrine existed as a matter of California case law and the California constitution. Defendant First Bank of Delaware's Supplemental Brief, *supra*, at *7.

97. See generally Memorandum of Law in Support of Defendants' Motion for Summary Judgment, *Madden v. Midland Funding, LLC*, 237 F. Supp. 3d 130 (S.D.N.Y. 2017) (No. 7:11-cv-8149).

98. Hearing Transcript at 9:21-25, *Madden v. Midland Funding, LLC*, 237 F. Supp. 3d 130 (S.D.N.Y. 2017) (No. 7:11-cv-8149) (Dkt. No. 80-1). See also Petition for Writ of Certiorari at 15-16, *Midland Funding, LLC v. Madden*, 136 S. Ct. 2505 (2016) (No. 15-610), 2015 U.S. S. Ct. Briefs LEXIS 4061 at *28-30.

99. Brief for Defendants-Appellees at 16, *Madden v. Midland Funding, LLC*, 786 F.3d 246 (2d Cir. 2015) (No. 14-2131-cv).

100. Petition for Panel Rehearing and Rehearing En Banc by Defendants-Appellees, *Madden v. Midland Funding, LLC*, 86 F.3d 246 (2d Cir. 2015) (No. 14-2131-cv).

101. *Id.* at 7-9.

102. Brief of the Clearing House Ass'n, LLC, Fin. Servs. Roundtable, Consumer Bankers Ass'n, & Loan Syndications & Trading Ass'n as Amici Curiae in Support of Rehearing and Rehearing En Banc at 5-6 & n.4, *Madden v. Midland Funding, LLC*, 86 F.3d 246 (2d Cir. 2015) (No. 14-2131-cv) [hereinafter Brief of Clearing House Ass'n] (citing *Gaither v. Farmers & Mechs. Bank of Georgetown*, 26 U.S. (1 Pet.) 37, 43 (1828) and *Nichols v. Fearson*, 32 U.S. (7 Pet.) 103,

selection of early English and state court cases, none of which have anything to do with the purported doctrine,¹⁰³ the Sullivan & Cromwell brief claimed that “For Almost Two Hundred Years, It Has Been Well-Established in America That a Valid Loan Cannot Be Rendered Usurious by Selling or Assigning the Rights to the Loan to a Third Party.”¹⁰⁴ The lead author on the Sullivan & Cromwell brief was Henry Rodgin Cohen, widely recognized as the dean of the financial services bar.¹⁰⁵ The appearance of such a claim in a brief with Mr. Cohen’s name on it gave the purported historicity of the doctrine an immediate patina of legitimacy that no other attorney could have provided.

The claim of historicity was then taken up again in the unsuccessful *certiorari* petition and briefing, including in a joint brief by the United States Solicitor General’s Office and Office of the Comptroller of the Currency, echoing the Sullivan & Cromwell argument.¹⁰⁶ It is unclear how the Solicitor General’s Office and Office of the Comptroller of the Currency failed to understand the irrelevance of the historical cases to the claimed doctrine.¹⁰⁷

Once the Solicitor General’s Office endorsed the doctrine, it was taken as gospel by most commentators without any verification—for surely the august Solicitor General’s Office would never sign on to a spurious doctrine—and the argument was quickly adopted as a defense

109 (1833), as well as *Watkins v. Taylor*, 16 Va. (2 Munf.) 424, 436 (1811); *Munn v. Comm’n Co.*, 15 Johns. 44, 55 (N.Y. Sup. Ct. 1818); *Tuttle v. Clark*, 4 Conn. 153 (1822); *Tate v. Wellings* (1790) 100 Eng. Rep. 716, 721 (opinion of Buller, J.); and BLACKSTONE, *supra* note 57, at 355, 379 n.32. Similar claims, albeit in slightly weaker form, were also found in another amicus brief. Brief of the Structured Fin. Indus. Grp., Inc., and the Sec. Indus. & Fin. Mkts. Ass’n as Amici Curiae in Support of Defendants-Appellees’ Petition for Rehearing and Suggestion for Rehearing En Banc at 8–9, *Madden v. Midland Funding, LLC*, 86 F.3d 246 (2d Cir. 2015) (No. 14-2131-cv) (citing *Nichols*, 32 U.S. at 109 for one of the “cardinal rules in the doctrine of usury” (quoting *Nichols*, 32 U.S. at 109)).

103. Regarding *Watkins*, 16 Va. at 436, *see supra* text accompanying note 54. Regarding *Munn*, 15 Johns. at 55 and *Tuttle*, 4 Conn. 153, *see supra* text accompanying note 37. Regarding *Tate*, 100 Eng. Rep. at 721 (opinion of Buller, J.), *see supra* note 50. Regarding BLACKSTONE’S COMMENTARIES, *see supra* note 57.

104. Brief of Clearing House Ass’n, *supra* note 102, at 5–7.

105. *See* Alan Feuer, *Trauma Surgeon of Wall Street*, N.Y. TIMES (Nov. 13, 2009), <https://www.nytimes.com/2009/11/15/nyregion/15cohen.html> [<https://perma.cc/2S99-GJ7T>].

106. Brief for the United States as Amicus Curiae, *supra* note 24, at 4, 8.

107. It is unclear how the work on the brief was allocated between the Solicitor General’s Office and the OCC, and how much of the OCC’s contribution was prepared in coordination with financial services industry trade associations. Additionally, the misinterpretation of the nineteenth century cases might have reflected a lack of familiarity with the practice of indorsement of credit instruments, which could be a symptom of the decline in the teaching of commercial law in American law schools. *See* Larry T. Garvin, *The Strange Death of Academic Commercial Law*, 68 OHIO ST. L.J. 403, 404 (2007) (noting commercial law as a dying field in the American legal academy).

in subsequent rent-a-bank litigation.¹⁰⁸ That continues to be the situation today, with litigants—including financial industry trade associations represented by Mr. Cohen among others—citing to the Solicitor General’s endorsement of the argument as evidence of the doctrine’s legitimacy.¹⁰⁹

CONCLUSION

This Article has demonstrated the spurious nature of the valid-when-made doctrine’s pedigree. The doctrine is a modern invention, fabricated by attorneys for financial services trade associations as part of the appeals from the Second Circuit’s *Madden* decision. The doctrine rests on decontextualized and misinterpreted quotations from nineteenth century cases dealing with entirely different issues and from a time when there could not have been a valid-when-made doctrine because there was no relevant transactional application for such a doctrine. The absence of any reference to the doctrine in reported cases, treatises, scholarship, or other sources prior to 2015 reveals the truth of the valid-when-made doctrine: it is not valid, but made up, and should not be relied upon as a rule of decision in cases or as support for a policy of allowing nonbanks to shelter in banks’ exemption from usury laws.

108. See, e.g., Defendant PayDayOne, LLC’s Motion to Dismiss Plaintiff’s First Amended Complaint at 13, *Pennsylvania v. Think Fin.*, No. 2:14-cv-07139-JCJ (E.D. Pa. Aug. 28, 2015).

109. Brief of Amici Curiae Bank Pol’y Inst., the Structured Fin. Ass’n, the Am. Bankers Ass’n, the Consumer Bankers Ass’n, & the Chamber of Com. of the U.S. in Support of Defendant’s Motion for Summary Judgment and Opposition to Plaintiffs’ Motion for Summary Judgment at 5, *California v. FDIC*, No. 4:20-cv-5860 (N.D. Cal. June 16, 2021) (Dkt. No. 70).