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April 21, 2021

VIA ELECTRONIC MAIL

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Hon. Patrick McHenry
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U.S. House Committee on Financial Services

Re: <u>Use of Congressional Review Act to Invalidate OCC True Lender Rule That Facilitates Predatory Lending</u>

Honorable Congressional Leaders,

On behalf of the 23 undersigned State Attorneys General (the "States"), we write to express our strong and bipartisan objections to the so-called "True Lender Rule" [1] (the "Rule") finalized by the Office of the Comptroller of the Currency ("OCC") on October 30, 2020. That

[1] *See* OCC, *National Banks and Federal Savings Associations as Lenders*, 85 Fed. Reg. 68,742 (Oct. 30, 2020) (codified at 12 C.F.R. § 7.1031), *available at* https://www.govinfo.gov/content/pkg/FR-2020-10-30/pdf/2020-24134.pdf.

Rule would sanction high-cost lending schemes devised to evade state usury laws. A growing number of states continue to pass state usury interest-rate caps on high-cost small-dollar loans in an effort to protect their consumers from predatory financial products. The OCC's Rule would be exploited by lenders seeking to circumvent these state interest-rate caps and invite, indeed welcome, predatory consumer-lending partnerships between banks and lightly regulated non-depository lenders. We urge you to use the Congressional Review Act, 5 U.S.C. §§ 801-808 ("CRA"), to rescind the OCC's True Lender Rule and safeguard states' fundamental sovereign rights to protect their citizens from financial abuse.

The Rule would sanction the use of so-called "rent-a-bank" schemes in which banks, regulated by federal agencies like the OCC, enter into sham relationships with non-bank entities for the principal purpose of allowing the non-banks to evade state usury laws. To facilitate these arrangements, the Rule heedlessly licenses non-bank entities to preempt state usury laws, notwithstanding the fact that Congress delegated this privilege exclusively to banks. Such sham rent-a-bank schemes have been widely scrutinized by courts to determine whether the bank is, in fact, the "true lender" of the loans. In order to identify the true lender, courts look to the substance rather than the form of the loan, examine the relationship between the bank and the non-bank and the totality of the circumstances surrounding the transaction.

Numerous courts across the United States have held that non-banks cannot escape state usury prohibitions under the guise of rent-a-bank schemes.[2] Courts have not hesitated to apply the "true lender doctrine" when a bank is named as the nominal principal party to a loan transaction but the transaction involves a non-bank participant attempting to skirt state usury limits.[3] For example, in applying the doctrine, the West Virginia Supreme Court of Appeals, relying on a long line of federal circuit court holdings, held that the "predominant economic interest" test is the proper standard to use when determining who *is* the "true lender" and thus whether state law is preempted.[4] This test examines which party (be that the bank or non-bank

[2] See, e.g., *Cmty. State Bank v. Strong*, 651 F.3d 1241, 1260 (11th Cir. 2011) (concluding that federal banking law does not immunize a bank from state usury law "if it is not the true lender of the loan"); Think Fin., 2016 WL 183289, at *13 (same); *Spitzer v. Cnty. Bank of Rehoboth Beach*, 45 A.D.3d 1136, 1138 (3d Dep't 2007) (holding that "the true lender," rather than "the written characterization that the parties seek to give" the transaction, determines whether a bank or a non-bank would be treated as the lender); cf. *CashCall, Inc. v. Morrisey*, No. 12-1274, 2014 WL 2404300, *7, 14-15 (W. Va. 2014) (affirming judgment finding that unlicensed entity "was the de facto or true lender" and thus violated state licensing and usury laws).

[3] *See Daniel v. First Nat'l Bank of Birmingham*, 227 F.2d 353, 357 (5th Cir. 1955) (holding a National Bank was liable for usury because the transaction involved "a loan or extension of credit to which the Bank was privy throughout" even though the contract was assigned to the bank after the transaction closed); *Ubaldi v. SLM Corp*., 852 F. Supp. 2d 1190, 1203 (N.D. Cal. 2012) (denying motion to dismiss in case alleging that Sallie Mae, not a National Bank, was the true lender); *Goleta Nat'l Bank v. O'Donnell*, 239 F. Supp. 2d 745, 747, 755 (S.D. Ohio 2002) (concluding that if a non-bank was the "true lender," then it would "unquestionably [be] subject to" state usury law, even though a different entity "is clearly listed as the lender on the loan documents"); *Goleta Nat'l Bank v. Lingerfelt*, 211 F. Supp. 2d 711, 717-18 (E.D.N.C. 2002) (same); *Salazar v. Ace Cash Exp., Inc*., 188 F. Supp. 2d 1282, 1285 (D. Colo. 2002) (same); *Eul v. Transworld Sys*., No. 15 C 7755, 2017 WL 1178537, at *6 (N.D. Ill. Mar. 30, 2017) ("Because Plaintiffs allege that [a National Bank] was not the true originator of their loans, the Court is not persuaded that NBA preemption applies here.").

[4] *Cashcall* at 14-15; citing *Goleta Nat. Bank v. Lingerfelt*, 211 F.Supp.2d 711(E.D.N.C.2002); *Colorado ex rel. Salazar v. Ace Cash Exp., Inc*., 188 F.Supp.2d 1282 (D.Colo.2002); *Flowers v. EZPawn Oklahoma, Inc*., 307 F.Supp.2d 1191(N.D.Okla.2004).

entity) has the predominant economic interest in loans "made" by a bank, considering factors such as which party uses its own money to fund the transaction and who holds the ultimate financial risk.[5] The predominant economic interest test, employed by courts across the country, examines the substance, not just the form, of rent-a-bank lending agreements.[6] Moreover, scrutinizing a transaction for the "true lender" in order to determine if parties are attempting to evade state usury limitations is a modern application of the *centuries* old anti-evasion doctrine.[7] Recently, Georgia codified this test in state law to prevent rent-a-bank schemes from violating that state's usury cap.[8]

In direct contradiction to this reasoned judicial analysis, the OCC has issued a harmful Rule that establishes a simplistic standard to *redefine* the meaning of "true lender". Under the OCC's Rule, regardless of the totality of the circumstances surrounding a bank and non-bank relationship, the national bank will be viewed as the true lender "when, as of the date of origination, it (1) is named as lender in the loan agreement or (2) funds the loan." This superficial approach allows free rein for the predatory rent-a-bank lending artifice to expand into and thrive within every state regardless of state consumer protection laws.

In an attempt to halt the application of the Rule, the State Attorneys General from New York, California, Colorado, District of Columbia, Massachusetts, Minnesota, New Jersey and North Carolina[9] have filed a multistate lawsuit against the OCC for its wholesale disregard of regulatory law and administrative procedure in promulgating the Rule.[10] While that litigation remains pending, and may take years to resolve, a high cost will be borne in needless consumer

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[5] *Cashcall* at 14, footnote 19:

> Courts have also applied the "predominant economic interest" test in deciding cases on the merits. For example, in *Spitzer v. County Bank of Rehoboth Beach*, 846 N.Y.S.2d 436 (N.Y.App.Div.2007), New York's Attorney General brought an enforcement action against payday lenders who had entered into rent-a-bank arrangements. In *Spitzer*, the Attorney General alleged that the payday lenders were the true lenders and that their agreements with a rent-a-bank were a scheme to circumvent New York's usury laws. The *Spitzer* court noted that the payday lenders purchased ninety-five percent of each of the bank's loans, assumed all risks of the loans, and indemnified the bank against any loss arising from a loan transaction. The *Spitzer* court then found that a totality of the circumstances must be used to determine the identity of the "true lender," with the key factor being who had the predominant economic interest in the transactions. *Id.* at 438–39. Ultimately, the bank and the payday lender in *Spitzer* entered into a $5.2 million settlement agreement with New York's Attorney General. *See also Andrews v. Cramer*, 256 Ill.App.3d 766, 195 Ill.Dec. 825, 629 N.E.2d 133, 136 (Ill.App.1993) (quote omitted); *Ghirardo v. Antonioli*, 8 Cal.4th 791, 35 Cal.Rptr.2d 418, 883 P.2d 960, 965 (Cal.1994) (citations omitted) (stating that the trier of fact must look to the substance of the transaction, rather than its form, and must determine whether such form was a mere sham and subterfuge to cover up usurious transactions); *Williams v. Powell,* 216, 214 Ga.App. 216, 447 S.E.2d 45, 48 (Ga.App.1994) (quote omitted).

[6] Id at 15, relying on *Carper v. Kanawha Banking & Trust Co.*, 157 W.Va. 477, 207 S.E.2d 897 (478, 901) (1974).

[7] See, *De Wolf v. Johnson*, 23 U.S. 367 (1825) ("Usury is a mortal taint wherever it exists, and no subterfuge shall be permitted to conceal it from the eye of the law; this is the substance of all the cases, and they only vary as they follow the detours through which they have had to pursue the money lender."); see also *Scott v Lloyd*, 34 U.S. 418, 446-47 (1835).

[8] *See*, e.g., Ga. Code. Ann. § 16-17-2(b)(4) (creating totality of the circumstances test to determine when "a purported agent shall be considered a de facto lender" for purposes of state usury laws);

[9] California, Colorado, District of Columbia, Massachusetts, New Jersey, New York and North Carolina are also signatories to this letter.

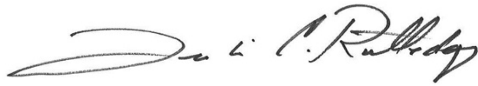
[10] See *New York v. OCC*, Case No. 1:21-Civ.-00057-SHS (S.D.N.Y.), complaint available at https://ag.ny.gov/sites/default/files/01.05.21_complaint_doc._no._1.pdf.

hardship and waste of precious time, during which predatory lenders, under cover of the OCC's Rule, will propagate their rent-a-bank schemes.

The most efficient course to prevent unrestrained abuse and avert immediate and ongoing consumer harm would be for Congress to invalidate the Rule pursuant to its remedial oversight powers under the Congressional Review Act.[11]

Americans spanning all political alignments are demanding that lenders who impose unconscionably exorbitant interest rates be subject to more, not less, regulation.[12] Currently, 45 states and the District of Columbia cap interest rates on installment loans, depending on the size, at a median rate of 38.5% for a $500, 6-month loan and 32% for a $2,000, 2-year loan.[13] During an unprecedented economic downturn, brought on and exacerbated by Covid-19, the OCC seeks to *expand* the availability of exploitative loans that trap borrowers in a never-ending cycle of debt. We urge Congress to use its powers under the Congressional Review Act to invalidate the OCC's True Lender Rule and safeguard the right of sovereign states, and the ability of an independent judiciary, to safeguard our citizens from rent-a-bank schemes designed to work end-runs around essential consumer protections.

Respectfully submitted,



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[11] 5 U.S.C. §§ 801-808.

[12] For example, when South Dakota voted on an interest rate cap in 2016, the payday loan industry spent over a million dollars lobbying against the measure, which was ultimately approved by 76% of voters in what one opponent of the cap conceded was a "landslide." *See* Bart Pfankuch, *Payday Loans Gone, But Need for Quick Cash Remains*, Capital Journal (Pierre, S.D.), Mar. 23, 2018. *See also* Megan Leonhardt, *Nebraska becomes the latest state to cap payday loan interest rates*, CNBC.com., Nov. 4 2020. Roughly 83% of Nebraska voters approved Measure 428 supporting a ballot initiative that caps rates on payday loans at 36% throughout the state. https://www.cnbc.com/2020/11/04/nebraska-becomes-the-latest-state-to-cap-payday-loan-interest-rates.html

[13] *See* National Consumer Law Center, State Rate Caps for $500 and $2,000 Loans (March 2021), http://bit.ly/state-rate-caps. These states include Nebraska, where a 36% rate cap passed by ballot measure on November 3, 2020, with 83% of the vote. Nebraska Initiated State Statute 45-901 *et seq*., 2020 Initiative 428. Montana passed its 36% consumer loan rate cap in 2010. Montana Deferred Deposit Loan Act, Mont. Code Ann. 31-1-701. Arkansas set a 17% interest rate cap in 2010, even including this rate cap in its state constitution. Ark. Const. Amend. 89 § 3. South Dakota passed a 36% interest rate cap on consumer loans, including title loans, in 2016. S.D. Codified Laws 54-4-36 *et seq*. Other states with a rate cap of 36% or lower include: Colorado, Connecticut, Illinois, Massachusetts, North Carolina, New Hampshire, New Jersey, New York, Pennsylvania, Vermont. Several other states cap the interest rate at 36% but allow a fee that can increase the APR on smaller loans: Arizona, Georgia, Maryland, Virginia and West Virginia. On Jan. 13, 2021, the Illinois General Assembly passed SB1792, the Predatory Loan Prevention Act. The legislation passed with a bipartisan vote in both chambers. This measure, signed into law on March 23, 2021, is largely mirrored on the Federal Military Lending Act, 10 U.S.C. 98, implemented by the Department of Defense, that protects active-duty military, their spouses and their dependents, with a 36 percent rate cap referred to as the Military Annual Percentage Rate. The Illinois Predatory Loan Prevention Act extends that same protection to veterans and all Illinois consumers who use financial products of under $40,000 in value, including payday and car title loans.

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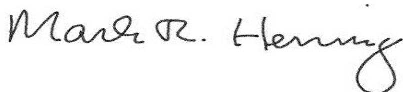

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