No. 15-610

In the Supreme Court of the United States

MIDLAND FUNDING, LLC, AND MIDLAND CREDIT MANAGEMENT, INC., PETITIONERS

v.

SALIHA MADDEN

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

REPLY BRIEF FOR THE PETITIONERS

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In her lengthy brief in opposition, respondent does not seriously dispute two central propositions. *First*, the Second Circuit's decision upends the long-settled understanding that the applicability of National Bank Act preemption turns on the identity of a loan's originator. *Second*, in light of the practical consequences of the Second Circuit's holding for the Nation's credit markets, this case presents one of the most significant legal issues currently facing the financial-services industry.

In the face of those propositions, respondent attempts to downplay the circuit conflict on, and the importance of, the question presented. Respondent also invents a host of illusory vehicle problems in an effort to avoid further review. That effort, however, smacks of desperation—and no wonder, because respondent knows full well that, if this Court were to grant review, the Second Circuit's reasoning cannot easily be defended. As the participation of all of the Nation's leading banking organizations as amici demonstrates, this case presents a question that is critical to the functioning of the national banking system, and the Second Circuit's decision creates a conflict on that question. This case is a straightforward and compelling candidate for certiorari.

1. a. Respondent first contends that there is no circuit conflict on the question presented because "no circuit has ever extended [National Bank Act] preemption to third-party debt collectors." Br. in Opp. 10. Respondent is simply playing word games. The specific identity of the assignee—whether a debt collector, a store, or some *tertium quid*—is irrelevant to the analyses of the courts of appeals to have considered whether the act of assignment can subject a loan to previously inapplicable usury laws. Until the Second Circuit's decision in this case, the courts of appeals had consistently held that the answer to that question is no, because the availability of National Bank Act preemption turns on the identity of the loan's *originator*. For that reason, there can be no doubt that those courts "would decide th[is] case differently" if presented with the same facts. Stephen M. Shapiro et al., *Supreme Court Practice* § 6.31(a), at 479 (10th ed. 2013).

As to the Eighth Circuit: respondent, like the Second Circuit, seeks to distinguish *Krispin* v. *May Department Stores Co.*, 218 F.3d 919 (2000), based on the relationship

between the bank and the store that was the assignee in that case. See Br. in Opp. 12. But while the Eighth Circuit observed that the bank that originated the loans was the "real party in interest," its holding that the claims against the assignee were preempted turned on the fact that the originating entity was a national bank. See *Krispin*, 218 F.3d at 924. Lest there be any doubt, the Eighth Circuit itself subsequently read *Krispin* in exactly that manner. See *Phipps* v. *FDIC*, 417 F.3d 1006, 1013 (2005).[1]

As to the Fifth Circuit: respondent seeks to explain *FDIC* v. *Lattimore Land Corp.*, 656 F.2d 139 (Unit B Sept. 1981), as a case in which that court merely applied "normal choice of law rules" in determining that Georgia law applied. Br. in Opp. 13 (internal quotation marks and citation omitted). For present purposes, however, the critical point is that the Fifth Circuit looked to the originator of the debt (a non-national-bank entity), not the assignee, in determining the applicable law—and it reached that conclusion by applying the "valid-when-made" principle. See 656 F.2d at 146-150. The Fifth Circuit held that the law applicable to the originator continues to govern the loan once the loan is assigned—and, in that respect, its reasoning compels preemption on the facts presented here.

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[1] Respondent contends that, in *Phipps*, the Eighth Circuit "had no opportunity to consider whether fees charged by the non-bank entity were also subject to preemption." Br. in Opp. 13. Not so. In addition to challenging fees initially charged by the national bank, the plaintiffs in *Phipps* alleged that the assignee impermissibly charged illegal fees and interest. See First Amend. Compl. ¶ 49, Dkt. 7, *Phipps* v. *Guaranty National Bank of Tallahassee*, No. 03-420 (W.D. Mo. May 15, 2003). The Eighth Circuit affirmed the dismissal of that claim. See *Phipps*, 417 F.3d at 1014.

b. Respondent next suggests that the circuit conflict may not survive the passage of the Dodd-Frank Act. See Br. in Opp. 15. But in the Dodd-Frank Act, Congress reaffirmed the principles applicable here. As noted in the petition for certiorari (at 5), Congress expressly preserved the preemptive scope of Section 85 of the National Bank Act. See 12 U.S.C. 25b(f). It necessarily follows, therefore, that the circuit decisions discussed above remain good law after the Dodd-Frank Act—and respondent does not assert otherwise. Further, as also noted in the petition (at 6), Congress expressly codified the *Barnett Bank* test for preemption of state laws that "significantly interfere[]" with a national bank's exercise of its powers, an additional and distinct source of preemption in this case. 12 U.S.C. 25b(b)(1)(B).[2]

2. a. On the importance of the question presented, respondent contends that this case involves "idiosyncratic facts," repeatedly suggesting that the Second Circuit's decision does not have any impact on cases involving different fact patterns. Br. in Opp. 1, 16, 18-21, 23-24. As a preliminary matter, that contention is belied by the fact that all of the Nation's leading banking organizations have filed amicus briefs supporting petitioner—presumably reflecting their judgment that the Second Circuit's decision has ramifications well beyond the specific facts of this case.

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[2] The provisions of the Dodd-Frank Act regarding preemption determinations by the Office of the Comptroller of the Currency (OCC), and preemption of claims against subsidiaries and affiliates, are inapplicable here. This case concerns a preemption determination "made by a court," which is a statutory alternative to a case-specific determination "by regulation or order of the [OCC]." 12 U.S.C. 25b(b)(1)(B). And this case simply does not involve a "subsidiary or affiliate" of a national bank. 12 U.S.C. 25b(e).

More broadly, while respondent suggests the result "might" be different in a case involving a different type of assignee or a different type of debt, see Br. in Opp. 16, 19, she cites nothing in the Second Circuit's reasoning to support that speculation. To the contrary, the Second Circuit unambiguously held that the National Bank Act does not continue to have preemptive effect after a national bank has sold or otherwise assigned a loan to "non-national bank entities that are not acting on behalf of a national bank." Pet. App. 11a. Respondent thus gets it exactly backwards: it is the Second Circuit that has "adopt[ed] a broad preemption rule with far-reaching and unintended consequences." Br. in Opp. 27.

For that reason, respondent's repeated efforts to emphasize various aspects of the facts of this case are misplaced. For example, respondent harps on the fact that one of the petitioners is a debt purchaser. See, *e.g.*, Br. in Opp. i, 1, 5, 10, 27.[3] Notably, this Court has never suggested that debt purchasers are treated differently for purposes of National Bank Act preemption. Indeed, in one of the Court's seminal National Bank Act cases, the defendant that benefited from preemption was an entity that, *inter alia*, "accept[ed] assignments of delinquent accounts" from the national bank and "collect[ed] interest" on those accounts. *Marquette National Bank of Minneapolis* v. *First of Omaha Service Corp.*, 439 U.S. 299, 305 & n.10 (1978). The Office of the Comptroller of the Currency (OCC) has specifically recognized

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[3] In a cynical exercise in mudslinging, respondent cites a consent order reached between petitioners and the Consumer Financial Protection Bureau. *See* Br. in Opp. 5 n.3. That order, however, does not involve allegedly usurious practices and has no relation whatsoever to this case. See Consent Order, *In re Encore Capital Group, Inc.*, No. 2015-CFPB-22 (Sept. 9, 2015).

that "banks can benefit from debt-sale arrangements." OCC, Bulletin No. 2014-37, *Risk Management Guidance* (Aug. 4, 2014). Rendering sales to debt purchasers uneconomic or too risky would significantly interfere with the powers of national banks. See *Olvera* v. *Blitt & Gaines, P.C.*, 431 F.3d 285, 288 (7th Cir. 2005). Yet that is precisely what the Second Circuit's broad rule accomplishes, by exposing debt purchasers to civil and even criminal liability simply for seeking repayment at a previously agreed-upon rate.

Respondents' efforts to minimize the practical impact of the Second Circuit's rule are likewise unavailing. For example, respondent asserts that assignees can "collect the full balances on [the] loans as of the date of assignment" and are simply barred from "continu[ing] [to] collect[] usurious interest going forward." Br. in Opp. 18. But even if respondent were correct, the impact of the Second Circuit's rule would still be severe: a loan's income stream, and thus its value, would decrease upon assignment. As noted in the petition (at 22-23), an assignee would be responsible for complying with the numerous state laws that could conceivably apply, undermining the uniformity the National Bank Act aims to promote and increasing the risk of any assignment. All of those effects would damage a national bank's ability to engage in the assignment and would discourage the bank from engaging in lending in the first place.[4]

[4] Respondent contends that the Second Circuit's decision has no effect on the fast-growing online marketplace lending industry. Br. in Opp. 23. But the Second Circuit drew no distinction between lending on the general credit market and online marketplace lending, and analysts have accordingly concluded that the decision below "cast a shadow over the [marketplace loans] industry." Sasha Padbidri, *US, European P2P Markets to Take Bigger Strides in 2016*,

b. As noted in the petition (at 21-23), numerous commentators have recognized the broad implications of the Second Circuit's decision in this case. Respondent seeks to downplay the decision's significance by citing other commentators. See Br. in Opp. 16-17. Of course, the very fact that so much attention has been lavished on the Second Circuit's decision is a telling sign that it is "controversial enough" to warrant review. *Id.* at 15. And even the commentators respondent cites acknowledge the conventional wisdom that "the holding in [this case], if it stands, will jeopardize the secondary market for consumer loans." Richard Kelly, *Are Usury Laws Making a Comeback? Examining* Madden v. Midland Funding, NewOak Capital LLC (June 23, 2015) <tinyurl.com/newoakarticle>.

Since the petition was filed, moreover, the chorus of commentators recognizing the implications of the decision below has only grown larger. One commentator suggested that, in light of the circuit conflict, it could be "very challenging for banks to do securitizations." See *Midland Seeks Supreme Court Review in High-Stakes Loan Case*, 12 Westlaw Journal Bankruptcy, no. 17, Dec. 17, 2015, at 22 (internal quotation marks omitted). In listing this case as "[o]ne of the biggest banking cases of 2016," a reporter noted the "chilling effect" of the decision below "throughout the financial services world," explaining that "[c]onsumers seeking to file a suit * * * could find a way to link their cases to Vermont, Connect-

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GlobalCapital (Jan. 4, 2016) <tinyurl.com/padbidriarticle>. In fact, concerns about the outcome of this case have caused at least one operator of an online lending marketplace to make changes to its business model. See, *e.g.*, Peter Rudegeair & Telis Demos, *LendingClub to Change Its Fee Model*, Wall St. J., Feb. 26, 2016 <tinyurl.com/wsjlendingclub>.

icut or, more likely, New York." Evan Weinberger, *Banking Cases to Watch in 2016*, Law360 (Dec. 24, 2015) <tinyurl.com/law360article>. And the authors of a leading treatise on banking law warned that the decision below "rais[es] doubt about the enforceability of [a national bank's] loan contracts and decreas[es] the marketability and value of every loan in its portfolio." 3 Barkley Clark & Barbara Clark, *The Law of Bank Deposits, Collections and Credit Cards* § 15.19 (rev. ed. forthcoming 2016). We could go on and on, but suffice it to say that few cases that come to the Court this Term will have received as much attention as this one before the petition for certiorari is even acted upon.

3. Respondent makes two primary arguments as to why this case is a poor vehicle to resolve the circuit conflict. See Br. in Opp. 23-28. Both arguments lack merit.

a. Respondent contends that petitioners have waived certain aspects of the argument that the National Bank Act continues to have preemptive effect after a national bank assigns a loan to another entity. See Br. in Opp. 25-26. But petitioners have consistently made that argument in the lower courts, invoking *Krispin* and *Phipps*. See Pet. C.A. Br. 3-4, 10-17; Pet. D. Ct. Mot. for Summ. J. 3-4, 7-8. As to the "valid-when-made" principle incorporated in Section 85, petitioners relied on that principle in both courts below, arguing that "the non-usurious character of a note should not change when the note changes hands." Pet. C.A. Br. 16 (internal quotation marks and citation omitted); Pet. D. Ct. Mot. for Summ. J. 8 (internal quotation marks and citation omitted). And as to the *Barnett Bank* test, the Second Circuit specifically passed upon the applicability of that test, repeatedly invoking the "significant interference" standard and citing *Barnett Bank* in its analysis. See Pet. App. 2a, 6a, 8a-9a, 11a, 13a-14a. All of that is more than

sufficient to preserve the preemption argument for this Court's review. See, *e.g.*, *Lebron* v. *National Railroad Passenger Corp.*, 513 U.S. 374, 379 (1995) (noting that this Court will consider an issue as long as it has been either pressed *or* passed upon below).

b. Respondent further contends that the Court should deny review simply because the preemption question was raised on a motion for summary judgment—and, for that reason, this case "is in an interlocutory posture." Br. in Opp. 24. But preemption questions are often resolved on dispositive motions, and this Court routinely grants certiorari on preemption questions in this very posture. See, *e.g.*, *Oneok, Inc.* v. *Learjet, Inc.*, 135 S. Ct. 1591, 1598-1599 (2015); *Northwest, Inc.* v. *Ginsberg*, 134 S. Ct. 1422, 1427-1428 (2014); *Dan's City Used Cars, Inc.* v. *Pelkey*, 133 S. Ct. 1769, 1777-1778 (2013). And the district court has signaled its willingness to stay any further proceedings once this Court grants review. See D. Ct. Status Hearing Tr. 5 (Oct. 13, 2015).

4. Perhaps recognizing that this case is a compelling candidate for certiorari, respondent previews her argument on the merits. See Br. in Opp. 28-35. Just two points warrant responses here.

a. Respondent correctly notes that Section 85 protects national banks themselves. See Br. in Opp. 29. But it does so by giving full effect to the core enumerated power of national banks to set interest rates at the level allowed by their home States. Respondent seeks to avoid preemption under Section 85 by arguing that Section 85 somehow does not carry with it the "valid-when-made" principle: that is, the principle that "a contract, which, in its inception, is unaffected by usury, can never be invalidated by any subsequent usurious transaction." *Nichols* v. *Fearson*, 32 U.S. (7 Pet.) 103, 109 (1833). While respondent attempts to limit *Nichols* to its facts,

this Court presented the "valid-when-made" principle in *Nichols* as a "cardinal rule[]" without in any way limiting it to the context of notes sold at a discount. *Ibid.* And while respondent derides the reliance on *Nichols* as a claim to "osmosis," see Br. in Opp. 30, it is a fundamental principle of statutory interpretation that, when Congress legislates against the backdrop of a well-established common-law principle, it does so "with an expectation that the principle will apply." *Astoria Federal Savings & Loan Association* v. *Solimino*, 501 U.S. 104, 108 (1991). That principle applies with full force to Section 85, which this Court has recognized must be read in light of the "common commercial transactions" Congress expected banks to undertake. *Marquette National Bank*, 439 U.S. at 318.[5]

b. Finally, as to the *Barnett Bank* test, respondent argues that petitioners cannot prevail under that test because they did not present specific evidence proving that "subjecting [petitioners] to state regulation in this case would impede a national bank from issuing credit cards or selling debt on the secondary market." Br. in Opp. 34-35. But that is not required to establish "significant interference" with the exercise of a national bank's powers, nor was any supposed failure to do so the basis for the Second Circuit's holding. In fact, the Second Circuit acknowledged that "it is possible that usury laws might decrease the amount a national bank could charge

[5] This Court's decision in *National Bank* v. *Johnson*, 104 U.S. 271 (1881), does not alter the foregoing analysis. There, the Court did not hold that a subsequent transaction can make a previously valid contract usurious; instead, it simply recognized that the National Bank Act trumps state law as to the permissible interest rate both when setting the original loan and when discounting a previously created loan. *Id.* at 277-278.

for its consumer debt," but dismissed that interference as legally insignificant. Pet. App. 11a. That was incorrect. As discussed above and in the petition, the state regulation permitted by the Second Circuit would gravely interfere with the ability of national banks to sell their loans and to rely on counterparties for functions such as debt collection and securitization. The resulting interference is plainly sufficient under the *Barnett Bank* test for preemption, to the extent that state regulation is not specifically preempted under Section 85.

* * * * *

In sum, this case is a clear-cut candidate for certiorari in light of the circuit conflict, the exceptional importance of the question presented, and the obvious flaws in the Second Circuit's reasoning. The petition for a writ of certiorari should therefore be granted.

In petitioners' view, it is unnecessary, and would merely introduce delay, for this Court to call for the views of the Solicitor General—especially because the OCC, the relevant government agency, has already expressed its views in multiple contexts on the propriety of imposing liability on assignees. See, *e.g.*, Pet. 19-20, 22-24. In the event the Court has any doubt about granting certiorari, however, it would be appropriate to call for the Solicitor General's views.

Respectfully submitted.

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