<u>WHAT IS DIDMCA AND WHAT DOES IT HAVE TO DO WITH FORECLOSURES?</u>

Congress passed the Depository Institutions Deregulation and Monetary Control Act ("DIDMCA" or the "Act") in 1980, and DIDMCA represented a significant piece of legislation aimed at deregulating and standardizing aspects of the national banking industry.

Overview of DIDMCA – Background and Purpose

Congress enacted DIDMCA to address certain issues in the banking sector, including interest rate restrictions, competitive disadvantages among diverse types of financial institutions/lenders, and the need for more uniform monetary policy control. The Act aimed to promote competition among depository institutions while enhancing the Federal Reserve's control over monetary policy. According to the Act's preamble, the Act's goal was "[t]o facilitate the implementation of monetary policy, to provide for the gradual elimination of all limitations on the rates of interest which are payable on deposits and accounts, and to authorize interest-bearing transaction accounts, and for other purposes.

Key Provisions of the Act

First, deregulation of interest rates was a significant aspect. DIDMCA phased out the interest rate ceilings on deposit accounts over six years, allowing banks to offer competitive rates. At Section 501, Congress provided that state laws and constitutional provisions limiting the rates or amounts of interest, discount points, finance charges, or other charges imposed by mortgage lenders would not be applicable to certain loans, including single family mortgages insured by FHA. Second, the Act extended Federal Reserve Membership to all depository institutions.

A third significant impact of the law was the preemption of State Usury Laws. DIDMCA allowed national banks and certain state chartered institutions to charge interest rates as high as those permissible for national banks in the state where they operate or are based. This is known as "interest rate exportation," or in other words, the ability to "export" the maximum interest rate allowed in the state where the lender is located to the state in which the borrower resides.

A major decision in the area of "exporting" terms or rates from the lender's home state is *Marquette National Bank v. First of Omaha Service Corporation*, 439 U.S. 299 (1978). In that case, the Supreme Court held that because the particular state designated on the national bank's organizational certificate was traditionally understood to be the state where the bank was "located," for purposes of Section 85 of the National Bank Act, 12 U.S.C. § 85, a national bank could not be deprived of this domicile merely because it extends credit to a resident of a different state. The Supreme Court said that since the bank "is a national bank; it is an '[instrumentality] of the Federal government, created for a public purpose, and as such necessarily subject to the paramount authority of the United States.' *Davis* v. *Elmira Savings Bank*, 161 U.S. 275, 283 (1896). The interest rate that Omaha Bank may charge in its BankAmericard program is thus governed by federal law." 439 U.S. at 541-42.

Since *Marquette* was decided, national banks have been allowed to charge interest rates authorized by the state where the national bank is located on loans to out-of-state borrowers, even though those interest rates may be prohibited by the state laws where the particular borrowers reside. This gave national banks a competitive advantage, and it is part of the reason for the enactment of DIDMCA. DIDMCA leveled the playing field by enabling FDIC-insured state-chartered banks also to export the maximum interest rate permitted by the state in which the bank was located.

So, what does this theory of exporting interest rates have to do with foreclosing a loan in default? There are three primary impacts arising today as borrowers become more creative in their defenses of foreclosures.

"Valid-When-Made"

The first implication is a doctrine known as the "valid-when-made" rule, which dates back almost two hundred years in this country. The doctrine effectively said that if the terms of the loan (including the rate of interest) were legal at the time the loan was made, the terms do not become illegal or unenforceable when the loan is sold to a different entity. This doctrine was seriously undermined in the Second Circuit's decision in *Madden v. Midland Funding, LLC*, (2d Cir. 2015), which held that a non-national bank entity, acting as a debt collector, did not benefit from the protections afforded under federal law from state-law usury claims. On a federal level, the FDIC and OCC have sought to codify the "Valid-When-Made" Rule, but it is expected that more borrowers will raise this issue in challenges to foreclosures.

Effects if a Buyer of the Loan is not Licensed in the State where the Foreclosure will be.

The second implication is a slightly different effect on the secondary market when a loan is sold or transferred. Under aspects of federal preemption, the *original* lender may not have been subject to state-law lender licensure requirements in the jurisdiction where the borrower resides. However, if the loan were sold on the secondary market to an entity that is *not* a national or state-chartered institution, questions arise as to whether this buyer of the loan would be able to maintain the benefits of the federal preemption that the originator of the loan had. If the buyer of the loan could not claim the benefits of federal preemption, and the new owner of the loan were therefor subject to the lender licensure requirements of the state where the borrower resides, borrowers can claim that the entity lacks the power to foreclose in that jurisdiction by its failure to be licensed. Such an enforcement attempt through foreclosure could lead to not only affirmative defenses to the foreclosure but also subject that new owner of the loan to counterclaims or liability under state usuary laws or UDAAP.

Interest Rate Opt-Outs

Another looming question deals with the effects of states that "opt out" of DIDMCA, thus affecting ability to enforce the terms of a loan. What is an "Interest Rate Opt-Out?" This term "interest rate opt-out" refers to a provision in DIDMCA at section 525 that afforded states the opportunity to opt out of interest rate exportation with respect to loans made in that state. Not long after enactment of DIDMCA, seven states and Puerto Rico in fact opted out of these provisions. Since that time, a number of the states opted back in (or let their opt-outs expire), but Iowa and Puerto Rico did not. However, with a renewed focus on interest rate charges and consumer protection, this issue is coming to the forefront once again. Iowa presents an interesting test concerning enforcement of interest rate terms stated in loan documents. Iowa's present-day view of "opting out" is that an out-of-state lender *cannot* export its home state's maximum interest rate into Iowa, but rather that the lender is bound by the maximum interest stated under Iowa law, because the loan should be considered "made" in Iowa. The state of Iowa has initiated enforcement actions against several out-of-state state-chartered banks, alleging violations of Iowa usury laws.

Other states are now considering "opt-out" provisions. Colorado enacted a bill opting out effective July 1, 2024. Bills are also pending in Washington, D.C., Minnesota, Nevada, and Rhode Island. If more states "opt-out," and take a similar view of interest rate exportation as in Iowa, there are inherent issues with proceeding with foreclosure. From a compliance standpoint, lenders and mortgage servicers will have to be aware of whether the interest rate being sought in any foreclosure would be permissible under that state's laws. This could become a patchwork of different maximum interest rates in a state depending on the type of loan or the type of originator.

This type of widely varying standards is exactly what DIDMCA sought to eliminate. However, as more states opt out, this certainly gives borrowers additional defenses against foreclosure and can enable UDAAP and FDCPA claims utilizing state usury laws.