Much Ado About Colorado

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One of the beauties of the national banking system is that it allows state-chartered banks to offer uniform credit products across the 50 states without having to worry about state interest rate caps. This concept – rate exportation – is the basis of all bank lending in the United States. And it works well, most of the time except when, of course, it doesn’t.

The speed bump to uniform lending is, of course, each state that decides to assert itself and its state laws that call for a lower interest rate than the rate available to the bank. And no state has been a more effective speed bump over the last decade than Colorado. Colorado has emerged as a leader in the fight against bank partnership lending that exceeds the interest rates permissible under Colorado law, and most knowledgeable players in the bank partnership space are well-aware of how to operate in Colorado without getting tagged by the regulator.

Not content with chasing bank partnership programs out of the state on pain of enforcement action, the Colorado legislature recently passed a law – Colorado House Bill 1229 – that will attempt to retroactively opt the state out of the rate exportation scheme. The legislature does this, even though the opt out, which takes effect July 1, 2024, is probably not effective.

At issue is the opt out mechanism set forth in Section 525 of the Depository Institution Deregulation and monetary Control Act of 1980 (“DIDMCA”). Pursuant to Section 521 of DIDMCA (also known as Section 27 and cited as 12 U.S.C. § 1831d), an FDIC-insured state-chartered bank can contract for the interest (both the rate and interest fees) permitted by the state in which the bank is located (this will usually be where the bank is headquartered, but it could also be any state where the bank performs certain activities in a branch) and export that interest into other states plus the District of Columbia – even if those other states’ laws would not permit that interest under its state laws. To appease the “states’ rights” votes in Congress at the time, the legislation also includes Section 525, which allowed the states to opt out of Section 521. Specifically, Section 525 provided that Section 521 applied only to loans made during the period beginning on April 1, 1980, and ending on the date on which a state opts out of the particular provisions *(with no deadline date for a state to opt out).*

After Congress enacted DIDMCA, several states, including Colorado, opted out. However, most of the states subsequently repealed their opt outs, including Colorado. This should not matter, of course, because the opt out right in Section 525 did not have an express deadline for its exercise. Unfortunately for everyone, it is not clear that the opt out right still exists, because a subsequent banking law, Section 407 of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (“FIRREA”), might have repealed it. At least two cases, one of which originated in Colorado, support the conclusion that FIRREA repealed Section 525. If that is the case, there is no ability for

a state to opt out of rate exportation in 2023 (or any other year), because that right no longer exists. To make matters more confusing, the FDIC – which is the federal regulator that supervised state-chartered, FDIC-insured banks – has repeatedly stated in its proposed (and adopted) rulemakings that it takes the position that a state may still opt out of Section 525.

In some way, the confusion over whether the opt out right still exists is irrelevant – anyone participating in a bank partnership program in Colorado should take notice of what Colorado is doing, because Colorado has repeatedly demonstrated its propensity to sue entities that disobey Colorado's wishes. With this view in mind, what House Bill 1229 does is cap the alternative charges for loans not exceeding $1,000. Importantly, HB 1229 expressly does not apply to certain types of credit cards. Rather, it limits the charges available to lenders of these small dollar loans. Most importantly, the bill expressly states that for these loans, Colorado opts out of DIDMCA. And notwithstanding the question of whether this opt out is effective, banks offering these loans in Colorado would do well to pay attention to this strong statement of Colorado's public policy.