No. 14-894

In The

Supreme Court of the United States

CASHCALL, INC. and J. PAUL REDDAM,
in his capacity as President and CEO of CashCall, Inc.,

Petitioners,

v.

PATRICK MORRISEY, Attorney General,

Respondent.

On Petition For Writ Of Certiorari To The Supreme Court Of Appeals Of West Virginia

BRIEF AMICUS CURIAE ON BEHALF OF THE SOUTH DAKOTA BANKERS ASSOCIATION IN SUPPORT OF PETITIONERS

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INTEREST OF THE AMICUS CURIAE

The South Dakota Bankers Association[1] ("SDBA") is a voluntary association of banks doing business in South Dakota. It has 81 member banks located throughout South Dakota that provide financial products to customers across the United States. SDBA submits this brief amicus curiae to address the impact the "predominant economic interest" test, as applied by the Supreme Court of West Virginia in this case, will have on the lending interests of SDBA's member banks. SDBA encourages this Court to grant certiorari and reject the "predominant economic interest" test in order to provide necessary clarity to banks regarding the application of state law to interstate banking activities.

SUMMARY OF THE ARGUMENT

In order to facilitate a dual system of national banking, including active participation in interstate lending by both national and state banks, Congress enacted Section 85 of the National Bank Act and

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[1] The parties received timely notice of amicus curiae's intention to file, and the parties have consented to the filing of this brief. Their consents have been filed with the Court. No counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparations or submission of this brief. No person other than amicus curiae SDBA, its members, or its counsel made a monetary contribution to its preparation or submission.

Section 27 of the Federal Deposit Insurance Act. To promote interstate lending, these Acts prohibited states from applying state banking laws to discriminate against out-of-state lenders. The decision of the West Virginia Supreme Court frustrates the legislative intent of these laws – to foster interstate lending free of discriminatory state banking laws – by defining "lender" in such a way as to place legally-made interstate loans under the power of West Virginia's banking laws. By applying the "predominant economic interest" test, the West Virginia Supreme Court circumvented the intent of Congress, created an unpredictable lending environment, and placed a chilling effect on interstate lending activity.

ARGUMENT

Section 27 of the Federal Deposit Insurance Act states that Congress passed the Act "[t]o prevent discrimination against State-chartered insured depository institutions." 12 U.S.C. § 1831d. This purpose mirrors that reflected in Section 85 of the National Bank Act, under which Congress intended to preserve and foster a vibrant national banking system in which national banks could extend credit across state lines. To advance these goals, Congress acted to protect lending institutions from "unfriendly state legislation." *See* 12 U.S.C. § 85; *Beneficial Nat'l Bank v. Anderson*, 539 U.S. 1, 10-11, 123 S. Ct. 2058, 2064, 156 L. Ed. 2d 1, 10 (2003) (quoting *Tiffany v. National*

Bank of Missouri, 18 Wall. 409, 412, 21 L. Ed. 862 (1874). *See also Marquette Nat'l Bank v. First of Omaha Service Corp.*, 439 U.S. 299, 314, 99 S. Ct. 540, 548, 58 L. Ed. 2d 534, 546 (1978). Taken together, the protections granted by Section 27 and Section 85 foster "parity or competitive equality between national banks and State-chartered depository institutions[.]" *Greenwood Trust Co. v. Massachusetts*, 971 F.2d 818, 826 (1st Cir. 1992) (quoting legislative history).

This Court has repeatedly asserted that state law should be preempted, not only when it completely and explicitly conflicts with federal law, but also when the state law "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Capital Cities Cable, Inc. v. Crisp*, 467 U.S. 691, 698-699 (1984); *Hillsborough County, Florida v. Automated Medical Laboratories, Inc.*, 471 U.S. 707, 713 (1985); *Barnett Bank of Marion County, N.A. v. Nelson*, 517 U.S. 25, 31 (1996); *see also* FDIC Advisory Opinion 02-06 (December 19, 2002). Such an obstacle exists under the test advanced by the West Virginia Supreme Court in this case. Non-bank entities are not specifically addressed in Section 27. However, the "predominant economic interest" as applied below presents a significant obstacle to the full accomplishment of the Congressional objectives. Specifically, the test hinders the practical ability of state banks to extend credit across state lines without fear of interference by foreign-state banking laws.

The legal consequence of the "predominant economic interest" test in this case is that state law and state courts dictate the identity of the "lender" for purposes of Section 27 preemption. If the state bank maintains the "predominant economic interest" for the entire life of the loan, the foreign state is prevented from applying its laws. However, if the loan changes hands, whether through a total assignment or through any other arrangement in which the state-bank lender no longer retains the "predominant economic interest," the loan suddenly becomes usurious. *Cf. FDIC v. Lattimore Land Corp.*, 656 F.2d 139, 148-149 (5th Cir. 1981) ("The non-usurious character of a note should not change when the note changes hands."). This status change, from legal to usurious, subjects the party determined to be the "true lender" to potentially harsh penalties. *See, e.g.*, West Virginia Code § 46A-7-111 (allowing for civil penalties of up to ten times the amount of any excess charges). For bank and non-bank parties involved in the regular practice of assignment and servicing of loans, it is difficult under West Virginia's test to ascertain when a service agreement or assignment covering all or a portion of an otherwise legally-made loan will transform the loan's identity, remove important federal law protections, and subject the loan to potentially harsh penalties under state-imposed banking laws.

The uncertainty of the "predominant economic interest" test cannot be understated. Even within the appellate history of this case, the Court can observe the test exhibiting different permutations. The trial court determined that CashCall was the "true lender," and the loan arrangement was subject to West Virginia's laws, because CashCall "*bore the predominant economic risk* of the subject loans made to West Virginia customers[.]" (emphasis added). On appeal, the Supreme Court of West Virginia upheld the decision, stating that CashCall was the true lender because it "ha[d] *the predominant economic interest* in the loans made by the bank." *See* Appx. 34A. The difference between "having a predominant economic interest" and "bearing the predominant economic risk" is subtle, but potentially significant.

The term "predominant economic risk" begs the question as to what is included in a measurement of "economic risk." Arguably, this measurement could be confined to the potential losses in case of debtor default. However, could it also include other non-quantified economic risks, such as the costs associated with potential litigation, or reputational damage causing economic loss? The term "economic interest" begs similar questions. A court could consider only the proportional shares of interest payments each party is entitled to receive from the transaction. But could the court also determine economic interest by measuring entitlement to interest payments offset by the expenses and risks borne by each party? There is no clear indication of how these standards are measured. Accordingly, under the test advanced by the court below, parties entering into a loan-servicing arrangement cannot know at what point a loan servicer will suddenly become the "true lender" and thus lose the protections of federal law under Section 27.

The elusive nature of the "predominant economic interest" test is further exemplified by the cases cited by the West Virginia Supreme Court to uphold its application. Again, each of these cases presents a slightly different test. For example, in *BankWest, Inc. v. Baker*, the court upheld as the true lender the party that "maintains a predominant economic interest *in the revenues generated by the loan*[.]" 324 F. Supp. 2d 1333, 1341 (N.D. Ga. 2004), *vacated by BankWest, Inc. v. Baker*, 446 F.3d 1358 (11th Cir. 2006) (per curiam) (quoting O.C.G.A. § 16-7-6) (emphasis added). Alternatively, in *Spitzer v. County Bank of Rehoboth Beach*, the court stated that it would determine the "true lender" by looking to the totality of the circumstances surrounding the business association involved. 45 A.D.3d 1136, 1138 (N.Y. App. Div. 3d Dep't 2007). Under the totality of the circumstances, the court's determination of "who had the predominant economic interest" in the transactions was a "key factor," but not the only factor considered. *Id.*

In sum, the "predominant economic interest" test, as advanced by the Supreme Court of West Virginia, is not a clearly defined rule of law. As such, it is an inappropriate test to determine whether a loan, legally made by a state-chartered bank, should nonetheless be subjected to the potentially severe penalties of state usury laws. Banks, like any other business, operate best in a legal system that promotes certainty and predictability. This Court has on many occasions recognized the importance of this predictability and certainty. *See, e.g.*, *Hertz Corp. v. Friend*, 559 U.S. 77, 94-95, 130 S. Ct. 1181, 1193, 175 L. Ed. 2d 1029, 1043 (2010) ("Predictability is valuable to corporations making business and investment decisions."); *First Nat'l City Bank v. Banco Para El Comercio Exterior De Cuba*, 462 U.S. 611, 621, 103 S. Ct. 2591, 2597, 77 L. Ed. 2d 46, 55 (1983); *Pinter v. Dahl*, 486 U.S. 622, 652, 108 S. Ct. 2063, 2081, 100 L. Ed. 2d 658, 685 (1988). The test advanced by the West Virginia Supreme Court substantially undermines predictability and certainty in this important area of federal law.

From a practical perspective, this uncertainty has a chilling effect on interstate lending. Although applied in the usury-law context in this case, the "predominant economic interest" test defines who is a "lender," and could thus frustrate other areas of important federal banking law. Assignment and third-party servicing of loans are both regular occurrences in the banking industry. However, if parties are unable to determine with certainty whether a loan-servicer's interest in a loan will transform the loan's status from lawful to unlawful, parties are deterred from entering into these lawful business arrangements. If state banks are unable to enter into these servicing arrangements, the overall effect is that state banks are prevented from extending some loans to out-of-state customers. This frustrates the intent of Congress that West Virginia's banking laws should not deter state banks from extending loans across state lines.

SDBA encourages the Court to grant certiorari in this case to prevent the application of the undefined and unpredictable "economic interest" test. As an alternative, this Court has the opportunity to apply the more clearly defined, and straightforward "federal law test" advanced by the Petitioner. Under the "federal law test," a court focuses on which entity approved the loan, extended the credit, and disbursed the funds. If the entity that completed these tasks was a state-chartered insured depository institution, the loan would be protected from discriminatory state law intrusion, regardless of a non-bank entity taking an interest in the loan. As compared to the "economic interest" test, identifying who approved the loan, extended the credit, and disbursed the funds is a simpler, more predictable test.

The South Dakota Bankers Association believes that application of the "federal law test" will enable parties to easily determine at the onset whether a loan will be subject to certain foreign-state banking laws. This encourages lawful servicing and collection agreements and overall encourages extension of credit across state lines. As the West Virginia Supreme Court indicated, this may prevent West Virginia courts from finding a loan to be usurious, or otherwise enforcing its laws. However, "this impairment . . . has always been implicit in the structure of the National Bank Act." *Smiley v. Citibank*, 517 U.S. 735, 744, 116 S. Ct. 1730, 1735, 135 L. Ed. 2d 25, 33 (1996). West Virginia's aggressive approach to applying its banking laws to out-of-state lenders should yield to the intent of Congress to facilitate interstate lending.

SDBA respectfully submits that the "predominant economic interest" test is an inappropriate test to determine application of Section 27 protection from state usury laws. The greater certainty afforded by the "federal law" test will remove barriers from lawful business arrangements between state-chartered banks and non-bank servicing entities. SDBA believes that this will encourage and foster lending across state lines by state-chartered banks, in furtherance of the Congressional intent behind Section 27. Accordingly, SDBA respectfully requests that the Court grant certiorari in this case and take these important considerations into account when rendering its decision.

CONCLUSION

For the reasons stated above, amicus curiae requests that this Court grant the Petition for Certiorari.

Respectfully submitted,

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