No. 18-1827

In the United States Court of Appeals for the Fourth Circuit

LULA WILLIAMS, GLORIA TURNAGE, GEORGE HENGLE, DOWIN COFFY, and FELIX GILLISON, JR., on behalf of themselves and all others similarly situated,
Plaintiffs-Appellees,

v.

BIG PICTURE LOANS, LLC and ASCENSION TECHNOLOGIES, LLC,
Defendants-Appellants,

and

MATT MARTORELLO, DANIEL GRAVEL, JAMES WILLIAMS, JR., GERTRUDE MCGESHICK, SUSAN MCGESHICK, and GIIWEGIIZHIGOOKWAY MARTIN,
Defendants.

On Appeal from the United States District Court
for the Eastern District of Virginia

BRIEF OF APPELLEES

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December 20, 2018

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UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT
DISCLOSURE OF CORPORATE AFFILIATIONS AND OTHER INTERESTS

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No. 18-1518 Caption: Williams et al. v. Big Picture Loans et al.

Pursuant to FRAP 26.1 and Local Rule 26.1,

Lula Williams, Gloria Turnage, George Hengle, Dowin Coffy, and Felix Gillison Jr.
(name of party/amicus)

who is appellees, makes the following disclosure:
(appellant/appellee/petitioner/respondent/amicus/intervenor)

1. Is party/amicus a publicly held corporation or other publicly held entity? ☐ YES ☑ NO

2. Does party/amicus have any parent corporations? ☐ YES ☑ NO
If yes, identify all parent corporations, including all generations of parent corporations:

3. Is 10% or more of the stock of a party/amicus owned by a publicly held corporation or other publicly held entity? ☐ YES ☑ NO
If yes, identify all such owners:

4. Is there any other publicly held corporation or other publicly held entity that has a direct financial interest in the outcome of the litigation (Local Rule 26.1(a)(2)(B))? ☐ YES ☑ NO
If yes, identify entity and nature of interest:

5. Is party a trade association? (amici curiae do not complete this question) ☐ YES ☑ NO
If yes, identify any publicly held member whose stock or equity value could be affected substantially by the outcome of the proceeding or whose claims the trade association is pursuing in a representative capacity, or state that there is no such member:

6. Does this case arise out of a bankruptcy proceeding? ☐ YES ☑ NO
If yes, identify any trustee and the members of any creditors' committee:

Signature: s/ Matthew Wessler Date: 12/20/2018

Counsel for: Plaintiffs-Appellees

CERTIFICATE OF SERVICE

****

I certify that on December 20, 2018 the foregoing document was served on all parties or their counsel of record through the CM/ECF system if they are registered users or, if they are not, by serving a true and correct copy at the addresses listed below:

/s/ Matthew Wessler (signature) 12/20/2018 (date)

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INTRODUCTION

The plaintiffs in this case are Virginians who obtained payday loans over the Internet through an enterprise doing business as Big Picture. Although Virginia caps interest rates at 12%, these loans carried triple-digit interest rates that topped 600%—more than 50 times the legal limit. A typical $800 Big Picture loan put a borrower on the hook for about $6,200, or about eight times the principal.

This appeal concerns the defendants' effort to free themselves from any legal accountability for this unlawful lending scheme. For years, Big Picture did its lending under a different name—Red Rock Tribal Lending. That operation was the brainchild of Matt Martorello, a non-tribe member who struck a deal with the Lac Vieux Desert Band of Chippewa Indians to serve as the front for his online lending operation. Under the arrangement, the tribe would allow its name to be used to offer loans to consumers nationwide through Red Rock's website. And Martorello would handle nearly every aspect of the lending operations through his company in the Virgin Islands. In exchange, Martorello paid the tribe 2% of his revenue.

This arrangement was lucrative for Martorello. But several years in, pressure began to mount. To evade courts and regulators, the enterprise sought to cloak itself in immunity by claiming arm-of-the-tribe status—an analogue of arm-of-the-state sovereign immunity that permits an entity that functions as an arm of a tribe to share in the tribe's immunity. But both courts and regulators disagreed. The Second

Circuit rejected a tribal-immunity defense to a New York enforcement action brought against Red Rock. And, after suing a similar tribal lender, federal regulators denounced the idea that a lender's "relationship with a tribe" could free it from having to comply with state laws. *See* Press Release, *CFPB Sues CashCall for Illegal Online Loan Servicing* (Dec. 16, 2013), https://bit.ly/2UdynVA.

Martorello was worried. [redacted] To protect the business, Martorello convinced the tribe to wrap the entire lending operation in newly-created tribal entities. Through a series of complicated transactions, the tribe formally absorbed the enterprise: Red Rock became Big Picture, and Ascension, a new entity created by the tribe, purchased Martorello's lending company. On paper, the tribe now appeared to be in control.

But in practice, things stayed the same. As with Red Rock, Big Picture played almost no role in the actual lending. It employed just four tribe members in entry-level positions and installed a tribal council member as token CEO. Ascension had even less to do with the tribe. It hired no tribal employees and kept all the old operations in place. As far as the tribe was concerned, although it formally owned the companies, [redacted]

Since this corporate reshuffle, the enterprise's lending has continued apace. So too has the defendants' insistence that allowing "unhappy borrowers" to challenge the scheme would constitute "an assault" on tribal sovereignty. But arm-of-the-tribe status is reserved only for those entities whose activities are really those of the tribe—not for entities that, as the district court explicitly found here, were formed to "facilitat[e] the absorption" of a "decidedly non-tribal" and "fully-functioning" lending enterprise. JA202. In an 81-page decision, after thoroughly analyzing the record evidence and making careful factual findings, the district court concluded that the "driving force" behind Big Picture and Ascension was "to shelter outsiders from the consequences of their otherwise illegal actions." JA222.

This Court should affirm that conclusion. Extending tribal immunity on this record would offer a roadmap for payday lenders and others looking for ways to disregard federal and state laws: find a tribe, offer a sliver of revenue, and move the operations over on paper. Virtually nothing has to change: fill a few entry-level positions with tribe members, install a nominal CEO, and keep the core of the business (and profit-sharing) as-is. The tribe collects its checks, profit soars, and the chance of dodging liability in the event of any enforcement effort increases. Arm-of-the-tribe immunity is not designed to immunize this sort of arrangement. The Court should decline the defendants' invitation to do so here.

JURISDICTIONAL STATEMENT

The district court had subject-matter jurisdiction under 28 U.S.C. §§ 1331 and 1367. The district court issued an order denying the defendants' motion to dismiss on the basis of tribal sovereign immunity on June 26, 2018. JA141. The appellants timely appealed on July 19, 2018. JA145-47. This Court has jurisdiction to review this order under the collateral-order doctrine. *P.R. Aqueduct & Sewer Auth. v. Metcalf & Eddy, Inc.*, 506 U.S. 139, 141 (1993) (denial of sovereign immunity appealable under 28 U.S.C. § 1291); *Eckert Int'l v. Gov't of the Sovereign Democratic Republic of Fiji*, 32 F.3d 77, 79 (4th Cir. 1994).

STATEMENT OF THE ISSUES

1. Did the district court correctly place the burden of proof on the entity claiming arm-of-the-tribe sovereign immunity, just as this Court has placed the burden of proof on an entity claiming arm-of-the-state sovereign immunity?

2. Did the district court correctly join the majority of other courts in determining that the arm-of-the-tribe analysis requires assessing the actual relationship between the tribe and the entity rather than relying exclusively on formal documents?

3. Did the district court commit clear error in finding facts and applying the relevant factors to determine that the entities are not arms of the tribe?

STATEMENT OF THE CASE

I. The Big Picture lending scheme.

A. States have long regulated payday lenders.

In a payday loan, a consumer who can't afford to wait until payday receives a cash advance and, in exchange, the lender subtracts a larger amount from the consumer's paycheck. Typically, a consumer borrows several hundred dollars but has to repay the loan at triple-digit interest rates in installments over the course of months—a process that easily ends up quadrupling or quintupling the total dollar amount ultimately owed. *See*, *e.g.*, *Hayes v. Delbert Servs. Corp.*, 811 F.3d 666, 668-69 (4th Cir. 2016).

Although these loans are marketed as a source of short-term cash to be used in financial emergencies, they are often used to meet chronic budget shortfalls—"7 in 10 borrowers use them for regular, recurring expenses such as rent and utilities." Pew Charitable Trs., *Payday Loan Facts and the CFPB's Impact* (May 2016), https://bit.ly/2EtiWnt. But because borrowers "typically cannot repay the loan *and* cover their basic living expenses," they take out another loan, and then another. Ctr. for Responsible Lending, *Payday Loan Quick Facts: Debt Trap by Design* (July 2014), https://bit.ly/2LffVaT.

Lenders, in fact, rely on this feature. As one CEO put it, the "profitability" in payday lending is "to get that customer in" and "work to turn him into a repetitive

customer long-term." *Id.* The strategy has worked. On average, a "payday loan borrower is in debt for five months of the year, spending an average of $520 in fees to repeatedly borrow $375." Pew Charitable Trs., *Payday Loan Facts*. No surprise, then, that the Department of Defense has observed that the "debt trap is the rule not the exception." Dep't of Defense, *Report on Predatory Lending Practices Directed at Members of the Armed Forces and Their Dependents* 15 (Aug. 9, 2006).

States and federal agencies have enacted measures to curb the abuses that frequently arise in this lending context. Many states typically cap interest rates at somewhere between 7% and 36%. *See Usury Laws by State*, https://bit.ly/2LtcRrN. And five states plus the District of Columbia—home to more than 10% of Americans—prohibit the use of payday loans altogether. *Payday Lending State Statutes*, Nat'l Conference of State Legislatures (Jan. 23, 2018), https://bit.ly/2ktRfkU. These efforts reflect a core policy: that low-income borrowers in need of credit to help them through an unexpected expense or emergency should be able to access affordable alternatives without sinking into high-cost, long-term debt. *See* Ctr. for Responsible Lending, *Payday Loan Quick Facts*.

The results have been significant. "State interest rate caps have been very effective at eliminating payday loan abuses." Nathalie Martin & Joshua Schwartz, *The Alliance Between Payday Lenders and Tribes: Are both Tribal Sovereignty and Consumer Protection at Risk?*, 69 Wash. & Lee L. Rev. 751, 766 (2012). States that have imposed

reasonable interest-rate caps on small loans "saved their citizens an estimated $1.4 billion per year." Ctr. for Responsible Lending, *Springing the Debt Trap: Rate caps are only proven payday lending reform* 5 (Dec. 13, 2007). And those states that have restricted—or even eliminated—payday loans saw no demonstrable effect on the availability of short-term credit. *See, e.g.*, Ctr. for Community Capital, *North Carolina Consumers after Payday Lending: Attitudes and Experiences with Credit Options* 1 (Nov. 2007).

B. The tribal lending model reflects the newest effort to create a loophole around lending laws.

Still, some lenders continue to hunt for ways to circumvent lending laws. One strategy—popularized in the early 2000s—involved internet lenders partnering with unscrupulous nationally-chartered banks to use the national banks' "federal preemptive shelter" to shield their lending from liability. Ronald Mann, *Just Until Payday*, 54 UCLA L. Rev. 855, 873 (Apr. 2007). Once this approach—known as the "rent-a-bank" model—became public, federal regulators shut it down. *Id.*

As the "rent-a-bank" arrangement began to falter, a similar business model—tribal payday lending—began to take its place. Under this "most recent incarnation of payday lending regulation-avoidance," existing payday lenders "team with Indian tribes in order to gain the benefit of tribal sovereign immunity and avoid state usury laws, small loan regulations, and payday loan laws." Martin & Schwartz, *The Alliance Between Payday Lenders and Tribes*, at 753.

The tribal-lending market "is exploding." Jessica Silver-Greenberg, *Payday Lenders Join with Indian Tribes*, Wall Street J. (Feb. 10, 2011), https://on.wsj.com/2UGVfx2. One consultant disclosed that "more than 1,000 payday lenders have expressed interest in cloning" the tribal lending model. *Id.* The appeal from a lender's perspective is obvious. "All it takes to make a deal are a willing tribe and an eager payday lender." *Id.* As one major lender observed, tribal lending is "the new financial strategy that many are using as a loophole through the strict payday loan laws" because "[t]he revenue is quite high and promising for these tribes who often find themselves struggling." Martin & Schwartz, *The Alliance Between Payday Lenders and Tribes*, at 766. In short, internet lenders see "escaping US lending laws," as the way to "save their business." *Id.*

C. Martorello sets up a tribal lending scheme.

Several years into the tribal lending experiment, Matt Martorello, a 31-year old from Chicago, decided to get into the business. [redacted] So it was, in the spring of 2011, that an intermediary introduced Martorello to the Lac Vieux Desert Band of Chippewa Indians, a federally-recognized tribe located in Watersmeet, Michigan,

which had "decided" to try to "start tribal online lending businesses." JA262. Martorello started a new company—Bellicose Capital—to transact business with the tribe. *See* JA747; [redacted]

The parties formalized their relationship that summer. [redacted] the tribe passed a resolution creating an entity called Red Rock Tribal Lending. *See* [redacted] JA304, JA360, JA362. Although Red Rock's stated purpose was to create "a tribally-owned lending enterprise," JA360, it outsourced almost all the enterprise's operations to Martorello and his businesses. *See* JA755-57. According to the arrangement, a Bellicose subsidiary, SourcePoint, controlled the day-to-day operations of the enterprise from the Virgin Islands. Among other duties, SourcePoint:

- Screened and selected providers and lenders, JA755-56;
- Prepared standards for Red Rock to follow for operations, regulatory compliance, training, financial reporting, accounting, Red Rock's website, marketing, and consumer relations, JA756;
- Provided "pre-qualified leads" to Red Rock and generated the "credit-modeling data and risk assessment strategies" for lending decisions, *id.*;
- [redacted]

- Sold or transferred defaulted loans to third-party debt collectors, JA757.

SourcePoint's control also extended beyond even these lending responsibilities. It held "authority and responsibility" for "all communication and interaction whatsoever" between the operation and any "service provider, lender and other agents." JA751. It also controlled the selection of Red Rock's bank and had "sole signatory and transfer authority" over the account. JA758. And it held authority to "collect all gross revenues and other proceeds connected with or arising from the operation of [Red Rock.]" JA761.

Red Rock's duties, by contrast, were narrow and circumscribed. It was prohibited from engaging in any lending business anywhere without using SourcePoint to "service[]" the operation. JA752. And while Red Rock retained "[f]inal determination as to whether to lend to a consumer," JA755, it based this decision on predetermined underwriting criteria set by SourcePoint, JA756.

The unequal distribution of responsibility was intentional. As the parties' agreement expressly recognized, "the success of the business is based in large part upon the services provided . . . by [SourcePoint]." JA754. So too for the profits. Under the arrangement, Red Rock received 2% of the enterprise's gross revenue; after accounting for any outstanding obligations, SourcePoint took the rest. *Id.*; *see also* JA751, JA763.

D. Martorello and the tribe strike a new deal.

1. The lending enterprise faces mounting pressure. Less than two years after Red Rock and Martorello began offering online loans, pressure began to mount. JA163-165. In early 2013, New York regulators sent a cease-and-desist letter to the tribe for "using the Internet to offer and originate illegal payday loans to New York consumers." JA163 (quoting *Otoe-Missouria Tribe of Indians v. N.Y. State Dep't of Fin. Servs.*, 974 F. Supp. 2d 353, 356 (S.D.N.Y. 2013)).

The tribe refused to comply. It called New York's effort to enforce its laws "an affront to [the tribe's] inherent sovereignty" and sought to enjoin the state from further enforcement. *See Otoe-Missouria Tribe*, 974 F. Supp. 2d at 357. But because the tribe's lending practices targeted "New York residents who never le[ft] New York State," the court rejected the challenge. *Id.* at 360; *see Otoe-Missouria Tribe of Indians v. N.Y. State Dep't of Fin. Servs.*, 769 F.3d 105 (2d Cir. 2014) (affirming).

In the midst of this skirmish, Martorello confronted another development—the fall of the Western Sky tribal lending scheme. One of the first internet tribal lenders, Western Sky "issued payday loans to consumers across the country" from the Cheyenne River Indian Reservation in South Dakota. *Hayes*, 811 F.3d at 668. Although "keenly aware of the dubious nature of its trade," the lender claimed tribal immunity from the "host of state and federal lending laws" that it flaunted. *Id.* at 669. In late 2013, Western Sky was hit with a federal enforcement action. *See* Press Release,

CFPB Sues CashCall. As the CFPB explained, the lender's "relationship with a tribe" could not "exempt Western Sky from having to comply with state laws when it [made] loans over the Internet to consumers in various states." *Id.*

This gave Martorello pause. [redacted] Martorello also believed, given the similarities between the two operations, [redacted]

2. Martorello restructures the lending enterprise. Facing this unsettled landscape, Martorello devised a plan to restructure the lending operation by means of a deliberately obscure and interlocking set of new business structures.

Before getting to work, he first emailed the head of the tribal council, Jim Williams, that he was "working" on a "potential bigger deal" for the tribe. JA808. [redacted] Two weeks later, the parties began a restructure.

The corporate moves were complicated. As a formal matter it was the tribe that created a new lending entity—called Big Picture Loans—to centralize all of its

lending activities. JA364-66. Formed "as a wholly owned and operated instrumentality of the Tribe," Big Picture was managed by two members of the tribal council, and nominally run by one of them—Michelle Hazen—who was installed as CEO. JA365. Then, to create an extra layer of insulation from liability, the tribe created a holding company—called Tribal Economic Development Holdings, LLC or TED—that formally held Big Picture. JA372-74, JA165. Like Big Picture, TED was itself wholly owned by the tribe and managed by the same tribal council members. *Id.*; JA376.

On the servicer side, the tribe created a new company called Ascension Technologies. Documents stated that Ascension was a "wholly owned and operated tribally owned business entity" created to "engag[e] in marketing, technological and vendor services" to support Big Picture. JA380-81. Like Big Picture, Ascension was held by TED and managed by tribal council members. *Id.*; JA385. But unlike Big Picture, a non-tribe-member, Brian McFadden, was designated president. JA382.

[redacted] By creating Ascension and designating McFadden as president, the parties hoped "to enable the Tribe to more easily

purchase Bellicose"—the nerve center of the lending operation—from Martorello. JA166.

But purchasing Bellicose was no small matter—the tribe had nowhere near enough capital. *See* JA1345. Martorello came up with a workaround. He formed a new entity, called Eventide Credit Acquisitions, with the express purpose of enabling a seller-financed sale of Bellicose to the tribe. *See* JA825, JA828; [redacted] Martorello secured an 85% ownership stake in Eventide (the other 15% went to friends and family, including McFadden). JA835. Then, on paper, Martorello loaned the tribe $300 million which it used to purchase Bellicose. JA828, JA916; [redacted] No money actually changed hands. *See* JA917.

Martorello pushed the tribe to accept the deal. JA1331. [redacted] The tribe agreed and Bellicose was merged into Ascension. [redacted] JA826. Red Rock then assigned all of its loans and obligations to Big Picture and dissolved. JA441. Three weeks later, Big Picture and Ascension signed a contract that installed Ascension as the servicer of Big Picture's loans. *See* JA945-58. Ascension (now with Bellicose's resources and operations) agreed to service the loans in nearly the same way as SourcePoint did for Red Rock. *See* JA173.

The lending enterprise now consists of three main entities: TED, Big Picture, and Ascension. TED serves as a holding company for the other entities; Big Picture

assumed responsibility for the lending side of the business, originating loans and providing customer service; and Ascension formally became the loan servicer.

E. The current tribal lending enterprise.

Despite the shifting corporate facade, ample record evidence demonstrates that little about the actual lending operation changed.

1. Big Picture's structure. Big Picture is located on the tribe's reservation in Watersmeet and managed by two tribal council members, Hazen and Williams. JA850-52, JA1351. Hazen acts as CEO. *Id.* It was created, according to Hazen, to employ tribe members and "allow them to make a better life for themselves." JA1083. But of its fifteen employees, only four (other than Hazen) are tribe members,[1] and they are employed as customer service representatives (known as CSRs) who make between $11 and $14 per hour for an annual salary of between $20,800 and $22,880. JA1077. Since Big Picture began, they have received one pay raise totaling $1-$1.50 per hour. JA1078. As CEO, Hazen makes $90,000 per year, has "never tried" to pay her employees a livable wage, and raised no objection after learning that Big

[1] The district court stated that "Big Picture's employees primarily belong to the Tribe," JA211, but the record doesn't bear this out. Big Picture's CEO testified that, although the company had fifteen employees, only five, including herself, were members of the tribe. JA1084; *see also* JA1620-22. The district court was correct, however, that all fifteen employees work from the tribe's reservation. JA214.

Picture's CSRs were paid less than every Ascension employee, all of whom are non-tribe-members. JA1077, JA1079-80.

Big Picture is a limited liability corporation. *See* JA449 (stating that Big Picture's owner, TED, "shall not be obligated" by any debt, obligation, or liability "solely by reason" of owning Big Picture). And, because this structure largely insulates TED from liability, the tribe—as sole owner of TED—would also "not be directly affected by any judgment against Big Picture." JA224.

2. Big Picture's role. As with Red Rock, Big Picture employees perform highly circumscribed duties. Virtually all of the lending decisions—from whether to accept a borrower's initial loan application to estimating a borrower's interest rate—rely on proprietary underwriting software created by Bellicose. *See* JA787, JA1137. Big Picture employees make one decision in the course of originating loans—confirming that the borrower meets lending criteria that are pre-set by Ascension. JA264-65. Beyond this task, Big Picture employees play no other role in the actual lending process. They do, just as they did with Red Rock, respond to customer service emails and calls. JA1519-20. And, as before, the funds for these loans come from private investors, along with a small fraction from the tribe. JA263-64.

3. Ascension's structure. Like Big Picture, Ascension is managed by Hazen and Williams and is a limited liability corporation. JA381, JA385; JA389. But that is where the similarities end. Unlike Big Picture, although Ascension's nominal

headquarters is on the reservation, all 31 of its employees (before Hurricanes Irma and Maria displaced some) were located in Puerto Rico, the Virgin Islands, or Atlanta, Georgia. JA848, JA1081. And neither its president nor any of its employees are tribe members. JA1369, JA1541. No surprise: the company does not even bother to post Ascension job notices on the tribe's job board. JA860, JA1086. The company's co-managers claim that this is because Ascension requires employees with specialized skills that no member of the tribe possesses, JA858, JA1085-86, but the tribe has never attempted to create any training programs to qualify tribe members for these higher-paying jobs, JA884, JA1087-88.

Ascension's president, McFadden, makes almost all decisions for the company. JA460-63. Under the parties' contract, McFadden is expressly authorized to conduct a broad range of actions, including "approval of Ascension strategic direction" and, most significantly, "authority regarding all matters necessary for . . . day to day management." JA461. McFadden, though, must "report regularly" to the co-managers, who retain approval for any "obligation for Ascension over $100,000" and "any new major employee benefit plan." JA460-61. The co-managers are also responsible for appointing McFadden's successor. JA460.

4. Ascension's role. Ascension's role is identical to its predecessor SourcePoint. Ascension is charged with developing Big Picture's standards across the full range of lending operations—primarily from locations outside the reservation.

JA950. It likewise retains SourcePoint's responsibility for the full range of business operations. *Id.* And Ascension, like SourcePoint, "[c]oordinat[es] pre-qualified leads" and "provid[es] the necessary credit-modeling data and risk assessment strategies" for evaluating whether or not to extend funds to an individual borrower. JA951. Indeed, the key "duties" section of the contract is nearly identical to the same section in the Red Rock-SourcePoint agreement. *Compare* JA950-52, *with* JA755-57.

There is, in fact, no practical difference between SourcePoint and Ascension. As McFadden told Bellicose employees just before its acquisition, "all" of the current positions that would be "assigned to Ascension" would be "at the same or substantially similar rates of pay/benefits/conditions of employment." JA1090. Bellicose employees retained their "accrued and unused vacation and sick time, seniority, and personnel files" at Ascension. *Id.* And no positions were eliminated in the transition at all. *Id.* From the tribe's perspective, "everything that was being done [at SourcePoint] was just transferred over to Ascension to keep the flow going." JA862-63; *see also* JA883 ("[Bellicose] did like the—the same thing as Ascension does today.").

5. Lack of tribal management and oversight. The entities that make up the lending enterprise may be formally owned by the tribe and managed by tribal council members, but, as the record evidence reveals, the tribe exercises little actual oversight. As but one example, although Williams and Hazen formally approve

numerous documents related to the entities—including operating budgets, *see* JA1231, and employment materials, JA1233, JA1236—they do not know basic facts about the operations of either company. Consider the following:

- **The companies' data collection practices.** When asked what data Ascension collects and why, Williams explained "I'm not sure. I mean that—that's why we hired those guys, to figure out what's needed for the business. . . . I just trust that they're doing what they need to do to be successful." JA863.
- **The day-to-day work of the companies' employees.** Williams knew the majority of Big Picture's employees were CSRs, but did not know what CSR stood for. [redacted] Hazen could not say whether Ascension's employees have the same responsibilities now as they did when they were employed by Bellicose/SourcePoint. JA1076. In fact, she believed only McFadden would know this. *Id.*
- **The companies' formation and roles.** Hazen largely could not recall any of the details of Big Picture's formation. She did not know whose idea it was to form a new entity, who suggested the entity's name, or when it was chosen. JA1073-74; *see also* JA1557-58. Williams could not explain basic facts about what Big Picture does or how. JA864-65; *see also* JA1375-76

(acknowledging that he could not describe how loan decisions are made). And although Williams is a co-manager of Big Picture's subsidiaries, BPL A-1, BPL B-1, and BPL F-1, he admitted that he was "not familiar" with them and could only guess that they had "something to do with" Big Picture. JA870; *see also* JA1382.

F. The revenue structure of the tribal lending enterprise.

The distribution of revenue generated by the lending operation is governed by a Promissory Note between TED and Eventide that mirrors the prior arrangement—at the end of the day, the tribe receives 2% of the gross revenue (recently that increased to 3%) and Martorello's company Eventide pockets the remaining profit (structured as loan repayment).[2] JA754, JA829-30, JA959. Ascension, for its part, does not receive *any* share of the revenue. JA949.

II. This litigation.

A. The plaintiffs' loans.

The plaintiffs in this case are Virginians who found themselves in need of small loans to cover personal expenses and obtained payday loans from Big Picture. JA30-

[2] Once Big Picture has repaid $150 million to Eventide, the tribe's monthly distribution will jump to 6%. JA959. However, if TED defaults under the Loan Agreement, the distribution drops to zero. JA829. TED also distributes another 2% of gross revenue to the tribe to be "reinvested" in "growing the loan portfolio." JA829. Although this money is designated as a disbursal to the tribe, it must "stay in equity within [TED] . . . until the termination" of the Note's seven-year term. JA829-30.

32, JA40. They received advertisements from Big Picture that pitched the company's ability to process and fund a small personal loan very quickly and with little hassle. JA237. After just a few clicks, the borrowers were able to take out loans. *See* JA264-65.

Although the loans were advertised for small amounts, the total annual percentage rate of the loan topped 600%. JA40. That rate clearly ran afoul of Virginia law—which caps any interest rate chargeable to consumers at 12%. In total, for a true-dollar loan of $800, the defendants charged borrowers around $6,200—nearly eight times the amount borrowed. JA232.

B. The borrowers sue Martorello, Big Picture, and Ascension.

To curtail the defendants' unlawful conduct, the Virginia borrowers brought a putative class action against Martorello, Big Picture, and Ascension. JA28-59. They asserted violations of various Virginia usury laws and federal laws related to the illegal loans offered by Big Picture and its affiliated entities. *See* JA44-58 (asserting both common-law and statutory claims). After jurisdictional discovery, Big Picture and Ascension moved to dismiss on the basis of tribal sovereign immunity, arguing that they are "arms of the tribe" and therefore entitled to share the tribe's immunity. JA12.

C. The district court's decision.

In a thorough, 81-page decision, the district court rejected the defendants' attempt to invoke arm-of-the-tribe immunity to shield themselves from suit. After

carefully considering and weighing the evidence, it held that there was "no doubt" that the "driving force" behind the formation of Big Picture and Ascension was to use the tribe's immunity "to shelter outsiders from the consequences of their otherwise illegal actions." JA222. Because tribal immunity is reserved only for those entities that genuinely function "as an arm of the tribe so that [their] activities are properly deemed to be those of the tribe," it was unavailable here. JA221 (citation omitted).

The court began its analysis by explaining that a party seeking arm-of-the-tribe immunity bears the burden of proof on that issue. JA196. The defendants had argued that, because "tribal immunity is a matter of subject matter jurisdiction," it must fall to the plaintiff to prove that the defendants "are not entitled to sovereign immunity." JA194-95. The court rejected this claim. JA194. Placing the burden on the party seeking immunity accords with the settled approach taken in the analogous arm-of-the-state immunity context. JA197-98. And, as the court observed, the evidence required to answer the immunity question will usually be in the possession of the entity seeking immunity. JA196 (rejecting the invitation to treat the defendants "as immune entities without making them show it first").

On the merits, the court held that the defendants had "not met their burden of proof and, therefore, are not entitled to sovereign immunity." JA199. In reaching this conclusion, the court carefully applied the six-factor framework first announced

by the Tenth Circuit in *Breakthrough Management Group, Inc. v. Chukchansi Gold Casino & Resort*, 629 F.3d 1173 (10th Cir. 2010). *See* JA192 (describing the framework). Given the evidentiary record, the court explained, only one of the factors—method of creation—cut in favor of immunity, and only weakly. All five of the other factors weighed against conferring immunity on the defendants.

On the first *Breakthrough* factor—method of creation—the court determined that the entities were organized under tribal law, which generally supported the claim that the defendants were an arm of the tribe. JA199-200. But the weight of this factor was "limit[ed]" because "credible evidence" established that Big Picture and Ascension were only formed so that "Martorello and the Tribe" could "restructure Red Rock's lending operation in order to reduce exposure to liability." JA201.

The court found that the second *Breakthrough* factor—the purpose of the organizations—weighed substantially against immunity. Despite a stated purpose of "economic self-sufficiency," JA205, the court found that the "real purpose" of creating Big Picture and Ascension was to "help[] Martorello and Bellicose to avoid liability" for their otherwise-illegal operation "rather than to help the Tribe start a business," JA206.

The court further observed that Big Picture and Ascension "have largely failed to fulfill their stated purposes," which weighed against extending immunity. JA212. For starters, the tribe received only "a sliver of Big Picture's total earnings." JA209.

And the district found that the evidence "clearly illustrates" that Hazen, Big Picture's CEO "has profited from Big Picture's lending operation far more than any other tribal members," while Ascension's non-tribal employees "are paid handsomely compared to Big Picture's employees." JA212. These facts, the court explained, were "inconsistent with the goal of economic development." *Id.*

Turning to the third *Breakthrough* factor—structure, ownership, and management of the entities—the court noted that both entities are formally owned by TED, which in turn is owned wholly by the tribe, and both are managed by Hazen and Williams. JA213-14, JA218. But after thoroughly analyzing the entities' actual management, the court found that the tribe's oversight was largely "pro forma." JA217. Hazen and Williams have delegated virtually all their authority to McFadden, the non-tribal president of Ascension which, in turn, handles virtually all of the core lending duties. JA217-18.

The fourth *Breakthrough* factor—the tribe's intent—also weighed against immunity. As before, although formal documents superficially reflected the tribe's intention that both entities would share its immunity, the evidence established that the "driving force" behind the tribe's actions was to "shield Martorello and Bellicose from liability" rather than to serve as a true arm of the tribe. JA222.

So too for the fifth *Breakthrough* factor—the financial relationship between the entities and the tribe. The tribe would not be liable for any judgment against Big

Picture or Ascension because both companies' operating agreements included a liability limitation provision. JA224. And, given the financial arrangements, reducing Big Picture's income (via judgment) would be unlikely to have a substantial effect on the tribe. JA225.

Finally, the sixth *Breakthrough* factor—whether granting immunity would serve the policies underlying tribal sovereign immunity—also weighed against immunity. The court gave weight to the funds the tribe has received under the loan enterprise and the "variety of social services and other benefits" that have been funded through the distribution. JA227. But the court made clear that Big Picture and Ascension have "primarily enriched non-tribal entities like Eventide and, possibly, individuals like Martorello." JA228. Weighing all the factors, the court concluded that "neither entity qualifies as an arm of the Tribe." JA229.

SUMMARY OF ARGUMENT

The district court correctly concluded that Big Picture and Ascension do not act as arms of the tribe. The lending enterprise has been designed, from the start, to empower an outside entrepreneur to sell illegal loans and escape liability. Regardless of form, a company that primarily benefits outsiders and is primarily controlled by outsiders is not entitled to share a tribe's sovereign immunity.

I. As the majority of courts to consider the issue have made clear, an entity seeking arm-of-the-tribe sovereign immunity bears the burden of proving that it

qualifies as an arm of the tribe. That rule follows the approach taken in the analytically similar context of arm-of-the-state immunity. There, "the defendant bears the burden of demonstrating" its arm-of-the-state status because it is, "as a practical matter, structurally necessary to require the defendant to assert the immunity." *Hutto v. S.C. Ret. Sys.*, 773 F.3d 536, 543 (4th Cir. 2014). The same is true here. Both types of immunity are "akin to an affirmative defense"—they can be waived and courts have no independent obligation to raise the issue. *U.S. ex rel. Oberg v. Pa. Higher Educ. Assistance Agency*, 745 F.3d 131, 147 (4th Cir. 2014) (Traxler, C.J., concurring in judgment in part and dissenting in part). And both ask whether the entity is sufficiently related to the sovereign—a question for which the relevant facts will be in the possession of the party claiming immunity. The district court therefore correctly placed the burden of proof on the defendants.

II.A. The district court also correctly concluded that the test for arm-of-the-tribe immunity encompasses both formal and functional considerations. Because the inquiry is intended to determine whether an entity has a sufficiently close relationship with the tribe that the entity should be treated like the tribe itself, any test must look at the relationship between the two in practice rather than relying solely on what the parties have written down on paper. This Court has embraced just this approach in analogous arm-of-the-state cases and, given the similarities, it should do so here as well. A purely formalistic approach like the one embraced by the defendants would

fail to ensure that arm-of-the-tribe sovereign immunity is extended only to entities that, in practice, further the goals of tribal immunity, and would invite all manner of abuse.

II.B. The district court correctly analyzed and weighed the relevant factors. After carefully evaluating the record, it found that one of the factors—method of creation—cuts weakly in favor of immunity. JA200-02. But it also concluded that all five of the other factors weighed against immunity. JA206, JA220, JA222, JA226, JA229. Those conclusions are sound. Formal arrangements notwithstanding, the record easily demonstrates that "the real purpose" of creating Big Picture and Ascension was to deliver tribal immunity to outsiders and "shield" them "from liability." JA206, JA222. Coupled with the facts that (1) only a "sliver of Big Picture's total earnings" reaches the tribe, JA209, (2) the defendants' lending enterprise was "fully-functioning" and "decidedly non-tribal" before it was absorbed by the tribe and continued its operation in virtually the same way after, JA202, (3) the enterprise "primarily benefit[s] individuals and entities outside the Tribe," JA212, (4) neither the tribe nor its tribal leaders actually "control[]" Big Picture or Ascension, JA218, and (5) the tribe "would not be directly affected by any judgment against Big Picture or Ascension," JA224, the district court correctly concluded that the defendants failed to carry their burden.

STANDARD OF REVIEW

"On appeal from a motion to dismiss under Federal Rule of Civil Procedure 12(b)(1)," this Court reviews "the district court's factual findings with respect to jurisdiction for clear error and the legal conclusion that flows therefrom de novo." *Metzgar v. KBR, Inc.*, 744 F.3d 326, 333 (4th Cir. 2014). "Under the clear error standard of review," the Fourth Circuit "will not reverse a lower court's finding of fact simply because [it] would have decided the case differently." *United States v. Span*, 789 F.3d 320, 325 (4th Cir. 2015). Rather, it "will only reverse if left with the definite and firm conviction that a mistake has been committed." *United States v. Chandia*, 675 F.3d 329, 337 (4th Cir. 2012).

ARGUMENT

I. The district court correctly placed the burden on the defendants to establish an entitlement to arm-of-the-tribe sovereign immunity.

The district court held that a party seeking arm-of-the-tribe status "must show by a preponderance of the evidence" that it qualifies "as an arm of the tribe" and is therefore entitled to tribal immunity. JA197. That is correct. As most courts considering this issue have explained, the "burden of proof on the issue of immunity properly falls on the entity claiming immunity." *People ex rel. Owen v. Miami Nation Enters.*, 386 P.3d 357, 369 (Cal. 2016). The reason is straightforward: until the entity

"has proven it should be treated as an extension of the tribe, it is no more entitled to a presumption of immunity than any other party." *Id.* at 371.

The defendants begin their appeal by attacking this commonsense rule. They claim that the district court committed a "fundamental error" when it required them to prove an entitlement to immunity because, in their view, tribal immunity "is a matter of subject matter jurisdiction." Opening Br. 24 (citations omitted). This argument fails because sovereign immunity "is a jurisdictional consideration separate from subject matter jurisdiction." *In re Prairie Island Dakota Sioux*, 21 F.3d 302, 305 (8th Cir. 1994). Indeed, courts have long held that sovereign immunity is "not of the same character as subject matter jurisdiction." *Id.* at 304 (citing 13 Charles A. Wright et al., *Federal Practice and Procedure* § 3524 at 167-70 (1984 & 1993 Supp.)).

Several distinct features of sovereign immunity explain why. *First*, unlike traditional questions of subject-matter jurisdiction, sovereign immunity "can always" be affirmatively waived. *Hutto*, 773 F.3d at 543. The same is not true for traditional subject-matter jurisdiction questions—"[n]o party can waive" a defect in subject-matter jurisdiction or otherwise "consent to jurisdiction." *Wis. Dep't of Corr. v. Schacht*, 524 U.S. 381, 389 (1998). *Second*, "a court need not raise the issue [of sovereign immunity] on its own initiative." *Hutto*, 773 F.3d at 543. Instead, unless a party "raises the matter, a court can ignore it." *Schacht*, 524 U.S. at 389. That position is "inconsistent with the principle that a court must always raise on its own motion any

defect in subject matter jurisdiction." *Woods v. Rondout Valley C. Sch. Dist. Bd. of Ed.*, 466 F.3d 232, 238 (2d Cir. 2006).

These "notable deviations from core jurisdictional principles," *id.*, have led courts—including this one—to treat sovereign immunity "as akin to an affirmative defense." *Hutto*, 773 F.3d at 543. As this Court explained in *Hutto*, because a defendant "can waive its [immunity] protection," it is, "as a practical matter, structurally necessary to require the defendant to assert the immunity." *Id.* And that, in turn, means that the burden of proof falls to the entities seeking to share a sovereign's immunity. *Id.*[3]

This approach makes sense. Treating sovereign immunity like other affirmative defenses "comports with the traditional principle that a party in possession of facts tending to support its claim should be required to come forward with that information." *Woods*, 466 F.3d at 238. In the analytically equivalent arm-of-the-state cases, a governmental entity seeking to avoid suit must show that it "is, in fact, an arm of the state" and not just "a municipal corporation or other political subdivision." *Id.* at 236. And because the facts supporting an entity's claim that it "ought to be treated as an arm of the state" will "often be 'peculiarly within the

[3] Below, the district court concluded "the Fourth Circuit has not addressed which party bears the burden on the arm-of-the-state question." JA198. But *Hutto* squarely addressed it, aligning this Court with "every other court of appeals that has addressed the issue." 773 F.3d at 543.

knowledge'" of the entity asserting it, "placing the burden upon that party will encourage prompt disclosure of the facts relevant to resolving the immunity claim." *Id.* at 238-39.

The defendants offer no principled reason why arm-of-the-*tribe* immunity warrants different treatment. They assert (at 28) that "tribal and state immunities are different," but we are left to guess what those difference might be (other than that "Indian tribes were not at the Constitutional Convention") and how such differences might affect the analysis here. After all, the goals of tribal sovereign immunity are similar to those of state sovereign immunity. Just as tribal immunity serves to "protect the sovereign Tribe's treasury" and "encourag[e] tribal self-sufficiency," *Breakthrough*, 629 F.3d at 1183, arm-of-the-state immunity is informed, by analogy, to the "twin goals of the Eleventh Amendment—protection of the state's treasury and of its dignitary interests," *Fresenius Med. Care Cardiovascular Res., Inc. v. P.R. & the Caribbean Cardiovascular Ctr. Corp.*, 322 F.3d 56, 63 (1st Cir. 2003). And the defendants' case-specific justifications (at 26-27) for a different rule—*i.e.*, that they did not waive immunity and "supported" their claim with evidence—miss the point. It is the "structural[]" nature of an entity's claim that it should share in a sovereign's

immunity that justifies placing the burden on the defendant. *See Hutto*, 773 F.3d at 543.[4]

The three cases that the defendants say prove "the burden of proof should have been placed on Plaintiffs" offer no sound basis for departing from the settled rule. Opening Br. 24-25 (citing *E.F.W. v. St. Stephen's Indian High Sch.*, 264 F.3d 1297, 1302-03 (10th Cir. 2001), *Pistor v. Garcia*, 791 F.3d 1104, 1111 (9th Cir. 2015), and *Cash Advance & Preferred Cash Loans v. Colo. ex rel. Suthers*, 242 P.3d 1099, 1113 (Colo. 2010)). None addressed the analytically identical relationship between arm-of-the-state and arm-of-the-tribe immunity claims. (*Pistor* and *E.F.W.* were not even arm-of-the-tribe immunity cases). And contrary to the defendants' argument, those courts that *have* actually considered the parallels have reached the same conclusion—the "rationales for placing the initial burden of proof on state-affiliated entities" are just as "persuasive with regard to tribally affiliated entities." *Miami Nation*, 386 P.3d at 370; *see also Gristede's Foods, Inc. v. Unkechuage Nation*, 660 F. Supp. 2d 442, 465 (E.D.N.Y. 2009) (same); *City of N.Y. v. Golden Feather Smoke Shop, Inc.*, 2009 WL 705815, at *4 (E.D.N.Y. Mar. 16, 2009) (same).

[4] To the extent the defendants suggest that the nature of the dismissal vehicle matters, that is wrong as well. Regardless of whether a party raises immunity in a Rule 12(b)(1) or 12(b)(6) motion, the "structural[]" burden analysis is the same. *Hutto*, 773 F.3d at 541; *see Yousef v. Samantar*, 552 F.3d 371 (4th Cir. 2009) (reversing 12(b)(1) dismissal based on FSIA immunity).

Bottom line: the district court was right to place the burden on the defendants to establish their claim. Even so, as we now explain, this case doesn't turn on who shoulders the burden because the record overwhelmingly establishes that the defendants do not have a sufficiently close relationship with the tribe to warrant arm-of-the-tribe status.

II. The district court carefully weighed the *Breakthrough* factors and correctly decided that the defendants are not entitled to arm-of-the-tribe immunity.

In challenging the district court's denial of immunity, the defendants press two main arguments. For starters, they claim that arm-of-the-tribe immunity is not "a factual inquiry" but instead is "a legal one," focused exclusively on "the official actions" of the tribe. Opening Br. 15, 22. Falling back, they assert that, "even if" the inquiry is factual, the district court "clearly erred" in weighing the relevant factors. Opening Br. 15, 18. But the first argument is a nonstarter: arm-of-the-tribe status, like its state counterpart, turns on "both formal and functional considerations" that require a thorough factual inquiry. *Miami Nation*, 386 P.3d at 365. And the second poses a nearly insurmountable hurdle: the clear error standard. So long as the district court's "account of the evidence is plausible," affirmance is required. *In re KBR, Inc.*, 893 F.3d 241, 258-59 (4th Cir. 2018).

A. The district court was correct to consider the practical application of the factors as well as the formal structures created by the defendants.

Although the defendants acknowledge that the district court was right to apply the *Breakthrough* factors to analyze arm-of-the-tribe status, they insist (at 31-32) that it was wrong to consider, as part of the analysis, *any* facts beyond the tribal legislature's "official records." Doing so, the defendants say, opens up the possibility that "tribal governments" may not be "taken at their word" and turns what should be a purely legal inquiry into a factual one. Opening Br. 34. That is wrong. Any careful analysis of arm-of-the-tribe status requires more than just looking at actions of the tribal legislature.

The very court responsible for the *Breakthrough* factors has made this clear. In *Finn v. Great Plains Lending, LLC*, the Tenth Circuit explained that a "thorough consideration of the *Breakthrough* factors" involves a focus on the "actual workings" of the entity seeking immunity, not just the "formal arrangements as set forth in [a tribe-created payday lender's] organizational paperwork." 689 F. App'x 608, 610-611 (10th Cir. 2017). That is because any meaningful assessment of arm-of-the-tribe status requires understanding "not only the legal or organizational relationship between the tribe and the entity, but also the practical operation of the entity in relation to the tribe." *Miami Nation*, 386 P.3d at 365. Applying the *Breakthrough* factors, in other

words, undoubtedly "takes into account both formal and functional considerations." *Id.*; *see also Gibbs v. Plain Green, LLC*, 331 F. Supp. 3d 518, 531-32 (E.D. Va. 2018) (same).

This approach again sensibly tracks the type of inquiry that governs arm-of-the-state immunity claims. Arm-of-the-state status does not turn on mere formality; it requires demonstrating that "an entity is 'truly subject to sufficient state control to render [it] a part of the state.'" *Oberg*, 745 F.3d at 135. And "whether a state-created entity is so closely connected to its creating state that it should be permitted to share in the state's immunity from suit generally is a fact-intensive inquiry dependent on an understanding of the *actual* operations of the entity and the *actual* relationship between the entity and the state." *Id.* at 156-57 (Traxler, J., concurring in the judgment in part and dissenting in part). This Court has repeatedly embraced this basic point. *Hutto*, 773 F.3d at 544 (considering whether the state "is *functionally* liable, even if [it's] not legally liable"); *Oberg*, 745 F.3d at 139-40 (relying on an entity's annual reports to determine whether the entity was independent of the state); *Ristow v. S.C. Ports Auth.*, 58 F.3d 1051, 1053 (4th Cir. 1995) (looking to "the practical effect" of a judgment on the state treasury). It should do the same here.

Creating a different rule for arm-of-the-tribe immunity would unacceptably neuter the analysis. Tribal immunity is a practical doctrine "intended to promote the federal policy of tribal self-governance." *Miami Nation*, 386 P.3d at 371. But determining whether extending it to an entity associated with a tribe would "further

that federal policy," *id.*, requires more than a review of the "formal arrangements" between tribe and entity. *Finn*, 689 F. App'x at 611. A court instead must undertake an inquiry into "the extent to which the entity actually promotes tribal self-governance," the "degree to which the tribe actually, not just nominally, directs the entity's activities," and "the degree to which the entity's liability could impact the tribe's revenue." *Miami Nation*, 386 P.3d at 371. Those lines of inquiry cannot be answered by "[o]rganizational arrangements on paper"—which "do not necessarily illuminate how businesses operate in practice"—and so restricting the analysis to just those arrangements will not cut it. *Finn*, 689 F. App'x at 611. The district court's decision to look beyond the paper records should be affirmed.

B. The district court weighed the *Breakthrough* factors correctly.

The defendants' second challenge to the district court's conclusion faces an even more arduous climb. The defendants argue (at 32) that, "even if" facts outside the four corners of the official records are considered, the district court clearly erred when it weighed the factors and concluded that the record established that the entities do not qualify for arm-of-the-tribe status. But throughout fifteen pages of argument (at 32-58) on this account, the defendants do little more than pick at the margins and recycle their claim that it was wrong for the court to "go beyond" the formal documents. That comes nowhere close to establishing, as they must, that the district court's view of the record was implausible. *In re KBR*, 893 F.3d at 258-59.

The *Breakthrough* factors afford a straightforward starting point. In *Breakthrough*, after canvassing the relevant caselaw, the Tenth Circuit identified six non-exhaustive factors that "are helpful" in deciding if the relationship between tribes and entities is close enough to justify immunity:

- (1) the entities' method of creation;
- (2) their purpose;
- (3) their structure, ownership, and management, including the amount of control the tribe has over the entities;
- (4) whether the tribe intended for the entities to have tribal sovereign immunity;
- (5) the financial relationship between the tribe and the entities; and
- (6) whether the purposes of tribal sovereign immunity are served by granting immunity to the entities.

Breakthrough, 629 F.3d at 1183, 1187-88. Taken together, the Tenth Circuit observed, these factors allow courts to determine whether entities are "so closely related to the Tribe that they should share in the Tribe's sovereign immunity." *Id.* at 1195. As we explain below, the district court carefully evaluated these factors and reached a decisive conclusion: the balance weighs against conferring arm-of-the-tribe status on the defendants.

1. Method of creation. Although the first *Breakthrough* factor focuses on "the law under which the entity was formed," "[t]he circumstances under which the entity's formation occurred, including whether the tribe initiated or simply absorbed an operational commercial enterprise," are "also relevant." *Miami Nation*, 386 P.3d at 372; *see also Breakthrough*, 629 F.3d at 1191-92. The district court held that this factor "weighs in favor of immunity" because both Big Picture and Ascension were formally created pursuant to tribal resolutions under the tribal code. JA200. But the court found the weight "limit[ed]" because the entities were formed not to "start[] an independent lending operation" but instead to "facilitat[e] the absorption" of Red Rock—a "decidedly non-tribal" and "fully functioning lending enterprise." JA201-02.

This conclusion is correct. When Big Picture and Ascension were created, Martorello and the tribe were already several years into their lending arrangement with Red Rock and Bellicose. *See* JA360, JA364, JA380. Although Red Rock claimed to be "a tribally-owned lending enterprise," it outsourced almost all the actual lending to Martorello and his businesses—which ran "an operational commercial enterprise" owned by, managed by, and employing exclusively non-tribe members. *See* JA755-58. The defendants simply absorbed these two entities: (1) Big Picture assumed Red Rock's role as nominal, outward-facing lender; and (2) Ascension

swallowed SourcePoint—and its lending management, technology and expertise—nearly whole. JA264-65, JA436, JA755-58, JA862-63, JA883, JA950-52, JA1090.

In the face of this "credible" evidence, JA201, the defendants argue (at 32) only that circumstances beyond the law governing the entities' formation are irrelevant to this factor. That is wrong. As the district court explained, the circumstances outlined above concern *how* Big Picture and Ascension were created—a core question bearing on formation. *See Miami Nation*, 386 P.3d at 372. And where "close[] scrutiny" of the entities' origins reveals that the "capital and intellectual property" on which the "lending businesses were founded did not come from [the] tribe" but instead from "an outside commercial entity that continue[s] to play a significant role in the lending operations after [the Tribe] formally took ownership," this factor does not weigh "unequivocally in favor of extending tribal immunity. *Id.* at 379. That is exactly what happened here.

2. Purpose. The second *Breakthrough* factor concentrates on "both the stated purpose for which the entity was created and the degree to which the entity actually serves that purpose." JA203-04 (quoting *Miami Nation*, 386 P.3d at 372); *see also Breakthrough*, 629 F.3d at 1192-93 (assessing the allocation of the entity's revenue as part of purpose). For this factor, what really matters is the "fit between that stated purpose and its practical execution"—which "need not be exact, but the closer the fit, the more it will weigh in favor of immunity." *Miami Nation*, 386 P.3d at 372. Several

elements guide this assessment, including (1) the number of tribal jobs created, (2) the amount of revenue generated for the tribe, (3) whether the entity engages in any activities unrelated to its stated goals, and (4) whether the entity primarily enriches non-tribe members or only tribal leaders. *Id.* at 373. The district court found that the defendants had "largely failed to fulfill their stated purposes" and, therefore, that this factor "weighs against" immunity. JA212. Exactly right.

To begin, the district court acknowledged that, on the "surface," the defendants' stated purpose was to improve the tribe's "economic self-sufficiency." JA206. But that purpose conflicted with the record evidence, which revealed that the "real purpose" of creating the lending entities was not to "help the Tribe start a business" but instead to "help[] Martorello and Bellicose . . . avoid liability." JA206.

Recall that the entities were created just as pressure was mounting against similar schemes around the country. The Western Sky lending scheme had begun to crumble and [redacted] JA1323. Red Rock itself was in fact *already* caught in the crosshairs—multiple federal courts had refused to block New York's enforcement of its usury laws. *See supra* 11. [redacted]

Big Picture and Ascension were intended as a response to this existential threat. *See supra* 12-13. It is telling that Big Picture's first and only CEO—tribal council

member Hazen—could not "explain who decided to create Big Picture" and demonstrated a general "lack of knowledge" around the circumstances of the entities' formation. JA201-02.[5] From the start, these companies were Martorello's idea. Certainly, the defendants have not met their burden on appeal to show that the district court's findings on this score were "clear error." *Metzgar*, 744 F.3d at 333.

The district court also held that the defendants failed to prove that they fulfill their claimed purpose of economic self-sufficiency. JA207-12. The "fit" considerations bear this out. Consider the number of tribal jobs created. As of late 2017—two years after Big Picture and Ascension were formed and seven years into the lending enterprise—the *entire* operation had created *five* jobs for the tribe. JA1084, JA1620-22. Four were low-paying positions at Big Picture as CSRs and one was for Big Picture's CEO. JA1077-78, JA1084. Ascension, like Bellicose before it, does not employ even one member of the tribe. JA1369, JA1541. It gets worse. Ascension jobs are not advertised to tribe members, JA860, JA1086; they are not performed on the reservation—Ascension has instead opened facilities in Georgia and the Caribbean, JA1081, JA1084-86, JA1363; and they require skills that tribe members do not have,

[5] The defendants assert that the district court was wrong to impute Hazen's "lack of knowledge" to the entire tribal council, but other council members, including Williams, confirmed the point. *See supra* 20; JA1401, JA1409-13, JA1421-22. And the defendants offered no evidence to the contrary.

JA858, JA1085-86. The tribal council, moreover, has taken no steps to help tribe members acquire these skills or pursue Ascension jobs. JA884, JA1087-88.

The allocation of Big Picture's revenue further undermines the fit between stated purpose and practical execution. The record establishes that the operation primarily benefits Martorello and his businesses rather than the tribe. As the district court explained, under the entities' revenue sharing arrangement, the tribe receives only a "sliver"—2% to 3%—of Big Picture's gross revenue. JA209, JA829, JA959. And although that meant the tribe had received approximately $2 million in direct distributions by June 2017, the defendants failed to show how this money was being used—offering only "vague" and "general" statements that "shed[] no light" on how the revenue "helped fund" any services. JA208.[6] In contrast, as a result of the

[6] The defendants assert (at 39) that "the Tribe received 'nearly $5 million' (JA-172) from Big Picture, and these funds were used 'to fund various tribal governmental, educational, and social services.'" That claim explicitly misrepresents the facts and record below—even as it was presented by the defendants. The $5 million includes both direct distributions to the tribe ($2 million) and the amount reinvested and held as equity by TED ($3 million). JA171-72. But the "reinvestment" amount cannot be distributed to the tribe for any purpose until the seven-year contract term ends. JA829-30. It therefore cannot be used to "fund various" services and thus "belongs" to the tribe only on paper. Beyond that, no case supports the defendants' restrictive claim (at 40) that courts may not look past a "general fund" to determine whether the revenue went to specific tribal services. And *Breakthrough* itself contradicts the defendants' view. *See* 629 F.3d at 1192-93 (looking to specific allocations).

corporate restructuring, Martorello's company Eventide has raked in "about $20 million" from the scheme. JA210.[7]

Given this record, the defendants are left to argue (at 30) that only the dollar amount received by the tribe is relevant (and not the percentage of profit). But an absolute dollar amount in a vacuum says nothing about whether the entities are aimed at carrying out their stated purpose or are instead primarily serving a different purpose—like shielding private actors from state law. In *Breakthrough*, the court made clear that what matters is (1) the *percentage* of revenue that goes to the tribe and (2) the specific *allocation* of revenue and how it benefits the tribe. There, "[o]ne hundred percent of the Casino's revenue" went to the tribe and the record established that the specific allocation was 50% to governmental functions, 15% for economic development, 10% to a trust fund, and 25% distributed to each member of the tribe. 629 F.3d at 1192-95. Compared with the record here—3% of the revenue and no specific allocations—the differences are stark. *See Miami Nation*, 386 P.3d at 378 (explaining that it is "instructive" to compare the entities in a particular case with "entities that other courts have recognized as arms of their respective tribes"). Where

[7] The defendants (at 35) ultimately embrace the fit inquiry, but only "to ferret out sham purposes." That gives away the game: even under the defendants' test, purpose cannot be assessed solely through "official records." This unsupported "sham purposes" proposal fails anyway. An entity does not receive arm-of-the-tribe status so long as it avoids being an outright fraud. Rather, it must "actually promote[] tribal self-governance" enough to be treated as "the tribe itself." *Miami Nation*, 386 P.3d at 371.

the "vast majority of revenue from the lending businesses flow[s]" away from the tribe, the fit is weak. *Id.* at 376.

Other facts in the record, aside from the profit distribution, demonstrate that the primary purpose of the arrangement was not to benefit the tribe. The district court specifically concluded that Big Picture and Ascension "primarily benefit individuals and entities outside the Tribe" and "one tribal leader." JA212. For instance, it is undisputed that every Ascension employee (all of whom are non-tribe members) "are paid handsomely"—far more than the four tribe members who work as CSRs. JA212, JA1077-78, JA1081-82. Yet Hazen—who herself has "profited from Big Picture's lending operation far more than any other tribal members," JA212—has only raised wages for Big Picture's employees once, and by less than $2 per hour. *Supra* 15. And as compensation for exercising "pro forma" oversight over Big Picture, Hazen nets $90,000 a year—a greater annual salary than the tribe-member CSRs' salaries combined. JA1077. The defendants offer no understanding of this evidence that would cut in favor of immunity, let alone that the district court clearly erred.

What the defendants do offer is one last-ditch argument to avoid the consequences of this record. They say (at 41) that the current financial arrangement "should not cause concern" because, after seven years, the portion of Big Picture's revenue that flows to Eventide will (absent any changes) reverse course and flow to the tribe. But what matters is whether the arrangement *currently* benefits the tribe. *See,*

e.g., *Breakthrough*, 629 F.3d at 1192-93 (focusing on the current record and revenue streams); *Miami Nation*, 386 P.3d at 378 (same). A rule that would allow an entity to claim arm-of-the-tribe status *now* based on a revenue-sharing arrangement that might deliver meaningful economic benefit *years from now* would green light all manner of corporate gamesmanship. Outside entities seeking to set up a tribal scheme would need only to satisfy one requirement: structure the lion's share of outsider revenue as debt repayment rather than pure profit.

This case well illustrates the concern. TED—the tribe's holding company—did not acquire debt in the ordinary course of the lending operation; instead, it acquired debt from Eventide as "payment" for Martorello's previous company. *See supra* 14. Structuring the deal this way created a payment framework nearly identical to the preexisting one between Red Rock and Bellicose—where the tribe received 2% of gross revenue and Martorello's company pocketed the rest of the proceeds. *Supra* 10. The only difference now is that Martorello's cut is reframed as "debt" instead of "profit." Arm-of-the-tribe immunity was not designed to encourage this form of subterfuge.[8]

[8] The defendants' odd invitation (at 41-42) to import the business judgment rule into the analysis fails. No court has employed this rule when considering arm-of-the-tribe sovereign immunity because it concerns whether a court can reject—and thereby undo—decisions made by a business. *See Lubrizol Enters. v. Richmond Metal Finishers, Inc.*, 756 F.2d 1043, 1046-47 (4th Cir. 1985). The only question here is whether to extend the tribe's sovereign immunity to these for-profit corporations, thereby handing them immunity from suit.

3. Structure, ownership, and management. The third *Breakthrough* factor concerns "the entity's formal governance structure, the extent to which it is owned by the tribe, and the entity's day-to-day management." *Miami Nation*, 386 P.3d at 373. Relevant here is whether the entity has "outsource[d] management to a nontribal third party." *Id.* Evidence that the tribe "is a passive owner, neglects its governance roles, or otherwise exercises little or no control or oversight" weighs against immunity. *Id.*

As before, the district court was correct that this factor cuts strongly against immunity. Although the tribe retains "formal oversight" of Big Picture and Ascension, it is, in the district court's words, "overcome in practice." JA215-16. The handful of evidence the defendants point to as suggesting that the tribe exercises some control over the entities is dwarfed by evidence that the lending operation is actually run by private actors with little tribal involvement. For instance, although nominally owned by the tribe, Ascension is run out of offices in Georgia and the Caribbean by a non-tribal president and with no tribe-member employees. JA1081, JA1084-86, JA1363, JA1369, JA1541. And it, not Big Picture or TED, controls virtually all of the lending operations, including delivering "pre-qualified leads" to Big Picture and providing the key "credit-modeling data and risk assessment strategies" that determine whether to issue a loan. JA160. Ascension alone effectively dictates loan approval, regardless of whether Big Picture employees actually click the button to

originate the loans. Ascension is also responsible for, among other things, soliciting potential borrowers, marketing, ensuring regulatory compliance, running human resources, negotiating vendor contracts and enforcing them, overseeing the financing of the enterprise, and collecting on loans. *Supra* at 17-18.

The relationship is decidedly not, as defendants describe it (at 45-46), one in which Big Picture "relies on another entity to perform certain agreed-upon tasks." To the contrary, Big Picture relies on Ascension to perform *all* tasks necessary to operate the business except the "pro forma" actions required to originate a loan and to provide some customer service support. That means the management, control, and structure of Big Picture are of little significance relative to those same aspects of Ascension. And the tribe does not exercise meaningful control over Ascension. True, Williams and Hazen are technically co-managers of the entity. But in practice, they have delegated nearly all of their authority to McFadden, Ascension's president. It is therefore McFadden, not anyone affiliated with the Michigan-based tribe, who controls Ascension's strategic direction, its bank account, and its day-to-day management. *Supra* 17. And McFadden cannot be replaced as president without the approval of Eventide and, by extension, its owner and manager—and McFadden's longtime friend and business associate—Martorello. JA929.

This delegation of authority is not a mere formality. Hazen and Williams do not provide substantive oversight of Ascension: Both lack basic knowledge about its

operations and employees. *Supra* 19-20. This makes sense. Ascension does not employ tribe members. It does not typically operate from the tribe's reservation. And it employs skilled professionals knowledgeable about the lending business in a way the co-managers seemingly are not. *See supra* 19-20; JA1085-86. And the only thing that changed when the tribe bought Bellicose was its name. *Supra* 17-18.

But a name change is not enough to confer immunity. Where "the balance of evidence suggests that" outsiders "exercise[] a high degree of practical control" over the lending operation, a tribe is not sufficiently "enmeshed in the direction and control of the businesses." *Miami Nation*, 386 P.3d at 377. Because the tribe is at best a "passive owner" of Ascension, it should not share the tribe's broad immunity. *See id.* at 373.

Not only does the tribe fail to control Ascension, it also fails to control Big Picture. Indeed, there is good reason to doubt that Hazen and Williams exercise real oversight over the company. In particular, Williams did not know basic facts about Big Picture, including what its employees do. JA1379. Nor did he know that Big Picture has several subsidiaries, of which he is the manager, or what those subsidiaries do, [redacted]. JA870, JA1336, JA1382. This evidence points strongly in one direction: tribal leaders provide, at most, passive oversight and rubber-stamp approval of Big Picture's operation.

4. The tribe's intent. The fourth *Breakthrough* factor considers whether the tribe expressed an intent to share its sovereign immunity with the entity. *Miami Nation*, 386 P.3d at 372. The district court recognized that the tribe expressed its intent that Big Picture and Ascension share its sovereign immunity. JA220-21. But it also recognized that the context of this decision was relevant, namely that the tribe sought to grant the entities tribal sovereign immunity primarily to "shelter outsiders from the consequences of their otherwise illegal actions." JA222. Therefore, as the district court correctly concluded, this factor weighs against immunity.

The defendants argue (at 51) that this factor should be limited to "*whether* the Tribe intended to share its immunity . . . , not *why* it intended to do so." But this is little more than self-serving semantics. The tribe's "self-interested and unsupported claim" that they "intended their sovereign immunity to extend to [the lending entities] cannot, without more," support immunity. *Miami Nation*, 386 P.3d at 379 (citation omitted). The district court properly asked whether Big Picture and Ascension were created for a core purpose of tribal sovereign immunity or to help non-tribe members conduct an otherwise-illegal business. It was the latter. JA222. Given this improper purpose, it does not matter that the tribe expressed an intent to share its immunity with these outsiders because a "formal statement of immunity is not sufficient to tip the balance in favor of immunity." *Id.* The district court correctly concluded that Big Picture and Ascension were not entitled to share this immunity.

5. Financial relationship. The "starting point" of the next *Breakthrough* factor is "whether a judgment against the entity would reach the tribe's assets." *Miami Nation*, 386 P.3d at 373. If not, this weighs against immunity, *see Dixon v. Picopa Constr. Co.*, 772 P.2d 1104, 1109-1110 (Ariz. 1989), but this fact is not dispositive, *Miami Nation*, 386 P.3d at 373. The ultimate issue is whether "a significant percentage of the entity's revenue flows to the tribe, or if a judgment against the entity would significantly affect the tribal treasury." *Id.*

The district court was correct to conclude that this factor weighs against immunity. *First*, it is undisputed that the tribe will not be directly affected by any judgment against the entities. Both entities have limited liability provisions that prevent liability from passing to the tribe, *supra* 16, so right out of the gate the financial relationship is attenuated.

Second, the tribe does not receive a "significant portion" of Big Picture's revenue. Under the contract, only 3% is actually distributed to the tribe. *Supra* 20. Unlike a case in which "all of [the entity's] profits inure to the benefit of the Tribe," *Howard v. Plain Green, LLC*, 2017 WL 3669565, at *4 (E.D. Va Aug. 7, 2017), because the distribution here is both "a very small part of Big Picture's revenue" and concretely "limited," the "actual effect" on the tribe's general fund "appears to be insubstantial." JA224-25.

Third, the defendants failed to prove how the revenue flows to the tribe. They did not provide "an exact breakdown of revenue allocation to different tribal services," making it "impossible to discern how the Tribe would be affected, if at all, if a judgment harmed Big Picture's operations." JA225. That failure is significant. Where the record is "too vague and conclusory to establish that a judgment against the entities would appreciably impair tribal revenues," this factor weighs against immunity. *Miami Nation*, 386 P.3d at 378.[9]

Finally, the defendants attempt (at 52) to redefine the inquiry by claiming that "[a]ll that is necessary for this factor to weigh in favor of immunity is for the Tribe to lose revenue if a judgment is entered against the entity" fails. No court has adopted this broad interpretation, which would favor extending sovereign immunity to any entity that provides only *de minimis* payments to a tribe.

Contrary to the defendants' assertion, *Breakthrough* does not support the argument that *any* reduction in payment is enough. The tribe in *Breakthrough* received "[o]ne hundred percent of the Casino's revenue" and "up to $1,000,000 per month,"

[9] The defendants' late-breaking effort to supplement their inadequate evidentiary presentation adds nothing new. On December 12, 2018, the tribe passed a new resolution purporting to address certain business revenue it received this year. *See* Tribal Resolution T2018-086. This self-serving document (it was created by the same tribe members who manage Big Picture) offers no breakdown of how the revenue is allocated to tribal services and simply reiterates what the defendants argued to the district court below—that proceeds from Big Picture "could possibly fund more than 30% of the Tribe's budget over the next few years." JA207. But what matters is the relative, not absolute, amount of revenue the tribe receives.

and it established that it "depend[ed] heavily" on that revenue. 629 F.3d at pp. 1194-95. The tribe here, by contrast, receives only 3% of Big Picture's gross revenue and nowhere close to that million-per-month draw. Because the entities function essentially as "intermediaries to commercial enterprises that have only a minimal financial relationship" with the tribe, the defendants were unable to establish that a reduction in revenue would meaningfully affect the tribe. *Miami Nation*, 386 P.3d at 378 (noting that the "vast majority of revenue" flowed to outsiders). Indeed, given the corporate structure, any losses suffered by Big Picture would be felt primarily by the lending enterprise's primary beneficiary—Eventide—not the tribe. JA226 (concluding that reduction in revenue would "not be felt strongly by the Tribe itself").

That is all the more so when one considers that, unlike Eventide's cut, the tribe's share is 3% of Big Picture's *gross* revenue—which is calculated by the inflow of income *before* any deductions (like a judgment against Big Picture). *See* JA828-29, 959. The defendants' claim (at 52), unadorned by any record cites, that "any judgment against Big Picture would reduce the Tribe's income" is, yet again, contradicted by the record. The defendants have come nowhere close to carrying their burden here.

6. Purposes underlying tribal immunity. Finally, the last *Breakthrough* factor addresses "the policies underlying tribal sovereign immunity and its connection to tribal economic development, and whether those policies are served

by granting immunity to the economic entities." *Breakthrough*, 629 F.3d at 1187. These goals include protection of the tribe's monies, preservation of tribal cultural autonomy, preservation of tribal self-determination, and promotion of commercial dealings between tribes and non-tribe members. *Id.* Some courts analyzing arm-of-the-tribe immunity have treated this as a separate factor, *see, e.g.*, *id.* at 1195; JA226-27, while others have treated it as a principle that governs analysis of each of the other five factors, *see, e.g.*, *Miami Nation*, 386 P.3d at 371-72. The choice of approach does not affect the outcome of the analysis.

The district court correctly concluded that this factor weighed against immunity. The entities have "primarily enriched non-tribal entities"—Martorello's company Eventide and even "Martorello himself." JA212, JA228. Extending immunity to these entities would primarily continue to benefit these outsiders rather than primarily protect the tribe's coffers. It would also set a troubling precedent. Granting arm-of-the-tribe immunity on this record would deliver a blueprint to all manner of outside commercial operations of how to push joint ventures with tribes on starkly disparate financial terms. If a corporation can blanket itself in a tribe's immunity in exchange for only 2% or 3% of its revenue, what incentive would exist for corporations to ever negotiate more favorable contracts with a tribe? Even if some tribes might resist these bargain-basement offers, others might not—which is all it

would take for tribes to lose any negotiating leverage. That undermines, rather than promotes, the broad goals of tribal sovereign immunity.

Weighing the factors. Ultimately, the district court weighed the evidence and determined that five of the six factors weighed against treating Big Picture and Ascension as arms of the tribe. *Supra* 27. As the record makes clear, that conclusion is sound. But even if one might think that one or more of the factors come out differently, the bottom line conclusion does not change—Big Picture and Ascension were created to provide cover for Martorello's illegal lending scheme. Big Picture and Ascension have fulfilled this goal while, in exchange, providing a sliver of their revenue to the tribe. And the tribe, for its part, has collected its distribution checks, declining to oversee these businesses or control how they operate.

At bottom, arm-of-the-tribe immunity is not designed to shield this type of arrangement. However one threads these facts through the analysis, the conclusion is the same: Big Picture and Ascension do not operate as arms of the tribe and are not entitled to share in its immunity.

CONCLUSION

The decision of the district court should be affirmed.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

This brief complies with the type-volume limitation of Federal Rule of Appellate Procedure 32(a)(7)(B) because this brief contains 12,866 words, excluding the parts of the brief exempted by Rule 32(a)(7)(B)(iii). This brief complies with the typeface requirements of Rule 32(a)(5) and the type-style requirements of Rule 32(a)(6) because this brief has been prepared in proportionally spaced typeface using Microsoft Word 2010 in 14 point Baskerville font.

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CERTIFICATE OF SERVICE

I hereby certify that on December 20, 2018, I electronically filed the foregoing brief with the Clerk of the Court for the U.S. Court of Appeals for the Fourth Circuit by using the CM/ECF system. All participants are registered CM/ECF users, and will be served by the appellate CM/ECF system.

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