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 a Writ of Certiorari to the Supreme Court of Appeals of West Virginia

REPLY BRIEF OF PETITIONERS

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REPLY BRIEF OF PETITIONERS

Respondent does not dispute three key points. First, in deciding whether Section 27 of the Federal Deposit Insurance Act (FDIA), 12 U.S.C. § 1831d, preempts state regulations of interest rates, courts apply irreconcilable rules to determine the critical question of the lender's identity. That is an untenable result in a field in which Congress sought to provide a predictable national regulatory regime.

Several courts deem the lender to be the entity that sets the terms of the loan and extends the credit. These courts have decided that when a bank originates the loan, federal law preempts state interest rate regulations as to the loan. These courts would have found preemption in this case because a state-chartered bank made the loans. In stark contrast, the West Virginia Supreme Court of Appeals and other courts hold that the lender is the entity that holds the "predominant economic interest" in the loan. Those courts find preemption substantially less frequently. While respondent quibbles with the depth of the split, he does not refute its existence.

Second, although this issue arises frequently as a practical matter, and has enormous significance because it is dispositive of the lawfulness of the transactions in question, the number of reported cases is small. That is so because plaintiffs and state regulators use the threat of punitive liability to cow lenders into settlement. The Court is therefore unlikely to obtain many future opportunities to review the Question Presented—and, in light of the critical importance of this issue to the daily operation of the financial services industry, it is especially important for the Court to review it at this time.

Finally, respondent does not dispute that the decision below restricts banks' ability to sell loans to non-bank servicers by stripping the loans of federal protection—and exposing them to the diverse regulatory regimes of the fifty states—upon sale. Given the size of the secondary market for loans, this restriction will inevitably impair state-chartered banks' ability to profit from lending, and thus chill lending—undermining one of the core purposes of the FDIA.

For these reasons, as well as those set forth in the petition and below, certiorari should be granted.

I. Courts Are Divided Over The Proper Test To Determine Whether Section 27 Preempts State Law Claims.

1. At the outset, respondent does not dispute that the ruling below conflicts with the bulk of federal authority. Numerous federal district courts have specifically rejected the precise rule embraced by the court below. As the petition explained (at 27-28), in *Sawyer v. Bill Me Later, Inc.*, 23 F. Supp. 3d 1359, 1367 (D. Utah 2014), the district court held that it was "required to dismiss [the state law] claims as preempted by Section 27," even if the servicer, "and not the state-chartered bank is the 'true lender.'" Similarly, in *Hudson v. Ace Cash Express, Inc.*, No. IP 01-1336-C H/S, 2002 WL 1205060, at *7 (S.D. Ind. May 30, 2002), the court found the fact that a chartered bank "made the loan" was "dispositive" of the preemption question under the substantively identical National Bank Act. These holdings are flatly

incompatible with the ruling below—and respondent does not cite or discuss either of them.

Of note—and contrary to the lower court's suggestion that a finding of preemption would undermine regulation—these district courts explained that "[f]ar from evading regulation, application of the FDIA results in extensive FDIC supervision of the loan program and examination for compliance with all applicable federal and state laws." *Sawyer*, 23 F. Supp. 3d at 1368.

These district court rulings follow inexorably from the holdings of the Fourth and the Eighth Circuits in very similar circumstances in *Discover Bank v. Vaden*, 489 F.3d 594 (4th Cir. 2007), *rev'd on other grounds* 556 U.S. 49 (2009), and *Krispin v. May Department Stores Co.*, 218 F.3d 919 (8th Cir. 2000). Respondent attempts to distinguish those cases on two grounds, arguing first that they addressed complete preemption rather than ordinary preemption, and second that the courts of appeals applied a "totality of the circumstances" approach instead of focusing only on the identity of the lender. BIO 16.

Respondent is correct that *Vaden* and *Krispin* were complete preemption cases. But that is a distinction without a difference because in each, the courts found in favor of the party asserting complete preemption, which *ipso facto* encompasses a finding that the state law is invalid under ordinary preemption principles. Put another way, there is no such thing as a state law that *is* subject to complete preemption yet remains valid because it *is not* preempted under ordinary principles.

"Ordinary" preemption encompasses express preemption, conflict preemption, and field preemption—all of which are defenses to state law claims. It arises when federal law displaces state substantive law. Complete preemption simply goes further; it not only displaces state substantive law, but also the state forum. It applies when "the pre-emptive force of [a federal statute] is so powerful as to displace entirely any state cause of action" raising similar claims. *Beneficial Nat'l Bank v. Anderson*, 539 U.S. 1, 7 (2003) (quoting *Franchise Tax Bd. of State of Cal. v. Constr. Laborers Vacation Trust for S. Cal.*, 463 U.S. 1, 23-24 (1983)). Thus, for complete preemption to attach, federal law must both displace state substantive law and also provide the exclusive cause of action. *Id*. at 9. Once that showing is made, any state law claim is properly recharacterized as a federal one, subject not only to federal substantive rules, but also to removal to federal court. *Id*.

In other words, every case finding complete preemption is necessarily a case in which the court finds ordinary preemption as well: it is impossible for a court to hold that federal law has entirely displaced any state law cause of action, but also hold that state substantive law governs the case. Consequently, when the courts in *Vaden* and *Krispin* found complete preemption of "suits brought ostensibly against non-bank entities for violations of state usury law" that are concededly indistinguishable from the suit here, BIO 16, they plainly would have found ordinary preemption of state law claims as well, had they been called to do so.[1] Indeed, on the facts of this case, those courts would have found complete preemption here.

2. Respondent argues next that "both the Fourth and Eighth Circuits conducted fact-intensive inquiries that relied on many different factors." BIO 20. What is critically important for certiorari purposes is that none of those factors can be reconciled with the "predominant economic interest" test adopted by the court below. Thus, whatever else respondent might say about the tests in the Fourth and Eighth Circuits, the existence of a circuit split is undeniable.

Respondent also mischaracterizes the Fourth and Eighth Circuits' tests. While those courts did examine all the facts of their respective cases, they took care to highlight particular facts that favor CashCall. For example, in *Vaden*, the court noted that the cardmember "agreements conclusively demonstrate

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[1] That inference is perhaps uniquely strong in this case because the Fourth and Eighth Circuits' inquiry in the complete preemption context—determining whether the bank or the non-bank entity was the "real party in interest"—is indistinguishable from the inquiry undertaken by the lower court here to determine whether the bank or the non-bank entity was the "true lender." Indeed, the lower courts in this case relied on "complete preemption" cases decided in the plaintiffs' favor to find against ordinary preemption here. *See* Pet. App. 35a-37a (citing *Goleta Nat'l Bank v. Lingerfelt*, 211 F. Supp. 2d 711 (E.D.N.C. 2002); *Colorado ex rel. Salazar v. Ace Cash Express, Inc.*, 188 F. Supp. 2d 1282 (D. Colo. 2002); *Flowers v. EZPawn Oklahoma, Inc.*, 307 F. Supp. 2d 1191 (N.D. Okla. 2004)).

that Discover Bank was the entity that extended Vaden credit and set the interest and fees of which Vaden complains," even though a non-bank entity mailed the billing notices and brought collection actions against borrowers. 489 F.3d at 602. The same is true here: First Bank & Trust (FB&T), the chartered bank, extended the credit to the borrowers and set the interest rates. CashCall performed servicing tasks after buying the loans.

Vaden did include a footnote stating without elaboration that the facts before it were distinguishable from a pair of cases rejecting claims of complete preemption in suits relating to alleged rent-a-charter schemes. *See* 489 F.3d at 603 n.9 (citing *Goleta*, 211 F. Supp. 2d at 718-19, and *Flowers*, 307 F. Supp. 2d at 1196). But the cases cited in that footnote merely refused to find complete preemption on the basis of the incomplete records before them. *See Goleta*, 211 F. Supp. 2d at 707; *Flowers*, 307 F. Supp. 2d at 1206. Neither case suggested that when, as here, a bank actually sets the terms of the loan and extends credit before selling the loan to a third party, the Fourth Circuit would hold that the bank is not the real party in interest, or the true lender.

The decision in *Krispin* is even more clearly favorable to CashCall. There, a department store issued credit cards to its customers. 218 F.3d at 921. Subsequently, the store created, as a wholly owned subsidiary, a nationally chartered bank. *Id*. at 922. It transferred the credit card business to the bank, but entered into another agreement whereby the store purchased the bank's receivables—*i.e.*, the customer's card payments. *Id*. at 922-23. Thus, the store created the card program, then placed it within its wholly owned subsidiary, and then claimed all of the beneficial economic interest from the program. Still, the court of appeals held that the bank, and not the store, was the true lender for preemption purposes. *Id*. at 924.

There is no way to reconcile that holding with the "predominant economic interest" test adopted by the court below. After all, the bank itself was wholly owned by the store, and thus the store ultimately bore all of the risk from the bank's operations and received all of the benefit. Moreover, the bank was established for the specific purpose of housing the credit card operation under the aegis of a bank—presumably to take advantage of the protection of national banking laws, which would not protect the store. Yet the Eighth Circuit found that the bank, and not the store, was the real party in interest.

Respondent finally parrots the lower courts' attempt to distinguish *Vaden* and *Krispin* by pointing out that in those cases, the banks and non-bank entities were affiliates of each other, while CashCall and FB&T are not. BIO 23. But that distinction only helps CashCall: after all, the likelihood that a bank is being used as a pawn for another business is much higher when—as in *Krispin*—the bank is a wholly owned subsidiary of the business, as opposed to here, where the bank and the non-bank entity deal with each other at arm's length.

II. This Case Is An Ideal Vehicle To Decide An Important Question Of Federal Law.

1. The Question Presented is of critical importance to state chartered banks and their partners. As *amicus* South Dakota Bankers Association explained, the "predominant economic interest" test adopted by the courts below "substantially undermines predictability and certainty in this important area of federal law." *Amicus* Br. 7. That is both because the "predominant economic interest" test is amorphous and ill-defined, and because—under any interpretation of the test—it restricts the sale of loans to third-party servicers, thus impeding lawful transactions that Congress concluded should be governed by a uniform body of federal law.

Respondent attempts to belittle the importance of this case by describing the ruling below as a fact-bound application of the predominant economic interest test. BIO 30-31. The key issue, however, is not any particular application of the test, but the propriety of the test itself. Respondent does not dispute that the question of which test applies matters enormously. Indeed, respondent himself stresses the importance of the issue, arguing that the power to export interest rates should be reserved to state-chartered banks, and that the predominant economic interest test "furthers this statutory purpose" while other rules assertedly do not. BIO 27-28.

2. As the petition explained, this case is an ideal vehicle to decide the Question Presented because the parties' rules track the positions in the circuit split, because the case was decided after a full trial on the merits, and because petitioners' position is typical of

servicers in the marketplace. Additionally, because few cases raising this issue are litigated through appeal—even though the issue arises frequently around the nation as a factual matter—this case presents a compelling occasion to decide the scope of FDIA preemption.

Neither of respondent's contrary arguments has merit. First, he argues that CashCall's preemption defense would fail under any standard. BIO 33. In support, however, respondent does not discuss the facts of this case, but instead attempts to sling mud by citing other lawsuits filed against the company. However, if this Court eschews the amorphous "predominant economic interest" test adopted below and holds instead that the true lender is the entity that originated the loans, it would decide in favor of preemption. Moreover, the fact that CashCall is a repeat player with nationwide operations establishes its familiarity with this area of the law, ensuring a thorough adversarial presentation of the issues.

Respondent also argues that because the court below addressed issues other than preemption, this case is a bad vehicle to adjudicate that question. But none of the other issues in the case cloud the preemption question, which was briefed, argued, and decided below—and which this Court will review de novo. Respondent does not seriously argue otherwise.

III. The Decision Below Is Incorrect.

Respondent devotes significant effort to defending the decision below on the merits. In light of the conflict among the courts, respondents' arguments weigh in favor of certiorari because they establish that the Question Presented is controversial and warrants this Court's attention. For example, respondent relies on the Eleventh Circuit's decision in *BankWest, Inc. v. Baker*, 411 F.3d 1289, 1304 (11th Cir. 2005), *vacated as moot*, 446 F.3d 1358 (11th Cir. 2006), a case on respondent's side of the split. *See* BIO 24; Pet. 28. Ultimately, however, respondent has the worse of the argument.

As the petition explained, Section 27 of the FDIA provides that state-chartered banks "may, notwithstanding any State constitution or statute which is hereby preempted for the purposes of this section, take, receive, reserve, and charge on any loan or discount made . . . the rate allowed by the laws of the State, territory, or district where the bank is located." 12 U.S.C. § 1831d(a). The ordinary meaning of the word "made," in the context of a loan, is "originated." Thus, the key question, under the statute's plain text, is which entity originates the loan.

Respondent argues that the emphasis on the word "made" is misplaced because "made" in the statute refers only to "discounts," and not to "loans." BIO 26. But the cases respondent cites as authority are unpersuasive for that point—indeed, they never make respondent's argument. The more natural reading of the statute is that the word "made" applies both to discounts and to loans—otherwise, only "discount" would have a verb attached to it.

Respondent argues further that even if "made" applies to loans, it does not matter because the statute protects only banks that "take, receive, reserve, and charge" interest, such that if a non-bank performs those activities, then Section 27 does no work. BIO 26-27. But that argument proves too much: it forecloses the "predominant economic interest" test adopted below because the words "take, receive, reserve, and charge" suggest direct interaction with borrowers—not an underlying economic interest.

Moreover, there is no evidence that Congress intended to restrict the scope of Section 27's preemptive effect only to loans that are originated *and* serviced by state-chartered banks, or that Congress was interested in limiting state-chartered banks' collaborations with third parties. Instead, all evidence indicates that Section 27 was enacted to facilitate interstate lending at a time when state-chartered banks faced substantial economic challenges.

Respondent erroneously argues that a narrow view of preemption is warranted because state-chartered banks occupy a special place in the economy—one subject to substantial regulation. But that is no answer, because petitioner's rule does not exempt those banks from any regulation. As the courts that have found in petitioner's favor have explained, when Section 27 preemption applies, including to "loans serviced through contracts with third parties," the loan program is "subject to federal regulation and oversight," including FDIC scrutiny. *See Sawyer*, 23 F. Supp. 3d at 1368.

In sum, the decision below is the subject of a circuit conflict, undermines Congress's objectives in enacting the FDIA, and is not faithful to the statutory text. Certiorari is warranted to address whether and when Section 27 preemption applies.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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