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Hennepin County Civil, MN

STATE OF MINNESOTA

COUNTY OF HENNEPIN

DISTRICT COURT

FOURTH JUDICIAL DISTRICT

Case Type: Other Civil
(Consumer Protection)

Court File No. 27-CV-13-12740
Hon. Kathleen D. Sheehy

State of Minnesota, by its Attorney General, Lori Swanson and its Commissioner of Commerce, Michael Rothman,

Plaintiff,

vs.

CashCall, Inc., a California corporation; WS Funding, LLC, a Delaware limited liability company, doing business in its own name and/or as a division or subsidiary of CashCall; and WS Financial, LLC, doing business in its own name and/or as an incorporated or unincorporated division or subsidiary of CashCall,

Defendants.

PLAINTIFF'S MEMORANDUM IN OPPOSITION TO DEFENDANTS' MOTION TO DISMISS

INTRODUCTION

Defendants lend to Minnesotans at usurious interest rates and charge usurious fees, thereby harming Minnesota residents. Minnesota law limits interest charged on most small loans to 21.75%, yet Defendants charge Minnesota consumers annual percentage rates of more than ***ten times*** this limit. Minnesota law also limits the fee that can be charged on most small loans to $25, yet Defendants charge a fee of up to $500.

Defendants do not deny that they are violating Minnesota's lending laws, but instead argue that they should be allowed to evade Minnesota's laws, and that the State is powerless to protect its residents. The State, however, is not constitutionally prohibited from regulating loans made to Minnesota residents, especially as Defendants direct voluminous business activity into the state. Defendants are also not shielded by "tribal immunity," as no tribe has any involvement

in the scheme and therefore no tribal interests are impacted. Finally, the State should not be prohibited from suing here based on a year-old administrative order against Western Sky (who is not a defendant here), dealing with only three loans, asserting a different legal theory, and that was ultimately dismissed without prejudice.

Defendants are not entitled to ignore the laws of the states in which they lend. Defendants, in their Motion to Dismiss, are re-arguing the same specious "rent-a-tribe" arguments that have been rejected by every court around the country to address them. The law does not require this Court to allow Defendants to gouge Minnesotans with usurious loans, and Defendants' Motion to Dismiss should therefore be denied.

FACTS

This is a civil enforcement action by the State of Minnesota, through its Attorney General and Commissioner of Commerce, against several affiliated companies that fund, service, purchase, and collect on loans to Minnesotans that accrue interest at rates far in excess of those allowed under Minnesota law. Complaint, ¶ 1. Defendants are engaged in a deceptive "rent-a-tribe" scheme where they associate with a South Dakota limited liability company, Western Sky Financial, LLC ("Western Sky",) that is supposedly owned by a member of the Cheyenne River Sioux Tribe. *Id.*, ¶¶ 1, 16-22. Defendants represent to borrowers and regulators that this association makes the loans immune to state usury and consumer protection laws by operation of tribal sovereign immunity. *Id.*, ¶¶ 40, 41, 48, 60-62, 67-68. Numerous states, as well as the federal government, have brought actions against this scheme. *Id.*, ¶¶ 24-34. Every court that has reviewed the scheme has held that sovereign immunity does not apply. *Id.*

As the State alleges, the scheme is not protected by tribal sovereign immunity because Western Sky is not owned or operated by an Indian tribe, and is not operated for the benefit of an Indian tribe. *Id.*, ¶ 23. Western Sky is organized pursuant to South Dakota law rather than tribal

law, and its sole member is an individual named Martin A. Webb. *Id.* Defendants' representations to borrowers about tribal immunity and consumers' legal rights are misleading and deceptive. *Id.*, ¶¶ 40-41. Nor does Western Sky enjoy any form of "member" immunity. *Id.*, ¶ 23.

Defendants' memorandum ignores the numerous allegations in the Complaint detailing the aspects of Defendants' lending that occur in Minnesota when they lend to Minnesotans. *Id.*, ¶¶ 21, 35, 37. For example, the State's Complaint alleges that advertisements for both CashCall and Western Sky appear on television and radio broadcast into Minnesota. Complaint, ¶ 18. The Complaint alleges that when Defendants and Western Sky lend to Minnesotans, those Minnesotans were physically in Minnesota, using telephone and computers in Minnesota when the loan transactions occurred. *Id.*, ¶¶ 35, 37. The Complaint alleges that Defendants deposit the loans directly into Minnesotans' bank accounts in Minnesota through an electronic transfer, and that Minnesotans do not travel to South Dakota to receive these loans. *Id.*, ¶ 37. The Complaint alleges that Defendants routinely call, email, and text message Minnesotans in Minnesota while originating and servicing the loans. *Id.* In addition, Defendants collect on their loans in Minnesota, including their usurious interest charges, by making numerous automatic withdrawals from each Minnesotan's bank account. *Id.* The Complaint alleges that Western Sky's website advertises the loan products Western Sky purports to offer to Minnesotans, and that the contracts between CashCall and Western Sky call for CashCall to host this website. *Id.*, ¶¶ 21, 36.

Rather than addressing these facts, Defendants assert that the loan transactions were "executed" by Western Sky in South Dakota. Def. Memo. at 8. Defendants do not cite any facts that support this assertion. For purposes of this Motion, the Court cannot rely on the self-serving affidavits introduced by Defendants in opposition to the State's Temporary Injunction Motion.

There is no support for Defendants' contention that its loans were "executed" or "consummated" on the reservation. Nonetheless, (as discussed more below) this assertion is the sole factual basis for Defendants' Dormant Commerce Clause argument, which also fails as a matter of law.

ARGUMENT

I. STANDARD OF REVIEW.

A motion to dismiss merely tests the legal sufficiency of a complaint. *Hebert v. City of Fifty Lakes*, 744 N.W.2d 226, 229 (Minn. 2008). The court must accept the facts alleged in the complaint as true and must construe all reasonable inferences in favor of the nonmoving party. *N. States Power Co. v. Franklin*, 122 N.W.2d 26, 30 (Minn. 1963). A motion to dismiss for failure to state a claim should only be granted if it appears to a certainty that no facts which could be introduced consistent with the pleading exist to support the relief demanded. *Krueger v. Zeman Constr. Co.*, 758 N.W.2d 881 (Minn. Ct. App. 2008), *aff'd*, 781 N.W.2d 858 (Minn. 2010). A motion to dismiss for failure to state a claim upon which relief can be granted will be denied "if it is possible on any evidence which might be produced, consistent with the pleader's theory, to grant the relief demanded." *Id.*

Additionally, Defendants challenge the constitutionality of Minnesota statutes, and therefore bear "the very heavy burden of demonstrating beyond a reasonable doubt that the statute is unconstitutional." *State v. Merrill,* 450 N.W.2d 318, 321 (Minn. 1990); *State v. Intl. Harvester Co.*, 63 N.W.2d 547, 552 (Minn. 1954). Defendants cannot meet their burden.

II. APPLYING MINNESOTA LAW TO THE LOANS DEFENDANTS GAVE TO MINNESOTANS DOES NOT VIOLATE THE UNITED STATES CONSTITUTION.

Defendants argue that the "Dormant Commerce Clause" of the United States Constitution prohibits the State from applying Minnesota law to the loans Defendants gave to Minnesotans.

Contrary to Defendants' arguments, courts have repeatedly and consistently held that it does not violate the federal constitution to apply state law to online lenders and other out-of-state lenders.

The "Dormant Commerce Clause" is a constitutional limit on state power inferred from the Commerce Clause of the United States Constitution, which provides that "[t]he congress shall have the power ... [t]o regulate Commerce with foreign Nations and among the several states." U.S. Const. art. I, § 8, cl. 3. The United States Supreme Court has held that this clause impliedly contains a negative command—the Dormant Commerce Clause—that forbids states from discriminating against or unduly burdening interstate commerce. *Chapman v. Comm'r of Revenue*, 651 N.W.2d 825, 831 (Minn. 2002) (citing *Quill Corp. v. North Dakota*, 504 U.S. 298, 312 (1992)).

The Dormant Commerce Clause "precludes the application of a state statute to commerce that takes place *wholly outside of the State's borders*, whether or not the commerce has effects within the State." *Healy v. Beer Inst.*, 491 U.S. 324, 335 (1989) (emphasis added).[1] As explained below, Defendants' argument that the State is attempting to apply its laws "wholly outside" Minnesota fails because Defendants' lending did not take place "wholly outside" the physical borders of Minnesota. In fact, Defendants' lending to Minnesotans took place almost entirely *within* Minnesota. Moreover, Defendants misread and misconstrue *Berman, P.C. v. City*

[1] Although neither is applicable here—or argued by the Defendants—two other categories of state laws also violate the Dormant Commerce Clause. The first is state laws that are "discriminatory" (e.g., that discriminate against out-of-state economic interests in favor of in-state economic interests; for example, by imposing a protective tariff or a customs duty on out-of-state companies that conduct business in the state). *See, e.g., West Lynn Creamery, Inc. v. Healy*, 512 U.S. 186, 193 (1994); *State v. Kolla*, 672 N.W.2d 1, 9 (Minn. Ct. App. 2003). The second is state laws that place an "undue burden" on interstate commerce. Laws will only be found unconstitutional under this "undue burden" standard when "the burden imposed on [interstate] commerce is *clearly excessive* in relation to the putative local benefits." *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970) (emphasis added).

of New York, 2012 WL 4514407 (E.D.N.Y. 2012) and the discussion of "consummation" in that decision. As a result, Defendants have failed to carry their heavy burden of showing that the application of Minnesota law to their lending to Minnesotans violates the United States Constitution.

A. The Application of State Law to Out-of-State Lenders Has Been Repeatedly Upheld.

Perhaps the most on-point authorities are two decisions from the Ramsey County District Court in a case brought by the State against an online payday lender named Integrity Advance. In that action, the defendant was represented by the attorneys that represent Defendants here (Mr. Benson and Ms. Callaway), who made the same Dormant Commerce Clause argument as here. The Ramsey County District Court denied the defendant's motion to dismiss, holding that the State had sufficiently alleged that defendant's commerce occurred at least partially in Minnesota:

> Based upon the allegations in the complaint, there are at least two actions that took place in Minnesota: 1) the loans in question occurred while the borrowers were physically in Minnesota; and 2) the subsequent withdrawal of interest charges (which by definition were usurious) from bank accounts in Minnesota also occurred in this state.

February 10, 2012 Order and Memorandum at 3 ("Order"). Bryden Aff., Ex. A. The defendant sought discretionary review at the Minnesota Court of Appeals of that Order, which the Court of Appeals denied, holding that the Ramsey County District Court's decision "does not appear to be questionable or involve an unsettled question of law." Bryden Aff., Ex. B at 2.

The parties later cross-moved for summary judgment on the Dormant Commerce Clause issue, and the court again ruled in favor of the State. Brennaman Aff., Ex. D. As before, the Ramsey County District Court held that the online lender's commerce did not occur "wholly outside" Minnesota and that, therefore, the Dormant Commerce Clause did not prohibit the application of Minnesota law to the loans defendant gave to Minnesotans. *Id.* at 10-14. The

court also noted that "consummation" is not the applicable legal standard under the Dormant Commerce Clause and, even if it was, the loan transactions were consummated when the loans were deposited into bank accounts in Minnesota. *Id.* at 10.

The Ramsey County District Court's ruling was consistent with a long line of authority rejecting similar Dormant Commerce Clause challenges, including challenges brought by other Internet lenders. For example, in *Quik Payday, Inc. v. Stork*, 549 F.3d 1302 (10th Cir. 2008), an online payday lender sued Kansas state officials who asserted that Kansas law applied to loans the lender made to Kansas residents. Quik Payday argued that Kansas' enforcement efforts violated the Dormant Commerce Clause. *Id.* at 1303-04. The Tenth Circuit, however, found that the payday loan transactions Kansas sought to regulate were "not wholly extraterritorial, and thus not problematic under the Dormant Commerce Clause." *Id.* at 1308. In so holding, the Tenth Circuit noted that aspects of loan transactions with Kansas residents are likely to occur in Kansas, and that "the transfer of loan funds to the borrower would naturally be to a bank in [the state where the borrower resides]..." making the transaction not "extraterritorial." *Id.*

The Ramsey County District Court and Tenth Circuit decisions against online lenders are merely the latest iteration of the long-standing rule that states may apply their usury and other lending regulations to out-of-state lenders without violating the Dormant Commerce Clause. The Pennsylvania Supreme Court summed up the law as follows:

> If there is anything well established in constitutional law it is that regulation of the rate of interest is a subject within the police power of the State, and this is especially true in the case of loans of comparatively small amounts, since the business of making such loans profoundly affects the social life of the community.

Equitable Credit & Discount Co. v. Geier, 342 Pa. 445, 455, 21 A.2d 53, 59 (Pa. 1941). Indeed, federal courts have recognized since the 1970s that merchants who do business in multiple states

are subject to each state's laws regarding interest rates and other credit terms. The seminal cases involve a mail-order retailer based in Chicago, Aldens, Inc., that sold merchandise across the country and offered credit to its customers. Aldens brought a trio of lawsuits against state officials who sought to apply their states' credit laws to Aldens. *See Aldens, Inc. v. Packel*, 524 F.2d 38 (3d Cir. 1975), *cert. denied*, 425 U.S. 943 (1976); *Aldens, Inc. v. LaFollette*, 552 F.2d 745 (7th Cir. 1977); *Aldens, Inc. v. Ryan*, 571 F.2d 1159 (10th Cir. 1978). Aldens' Dormant Commerce Clause challenges were unanimously rejected by all three federal circuit courts that reviewed them.

The Third Circuit acknowledged "the historical recognition that the states may, despite the burden on commerce, enact varying usury laws and varying contract laws" which apply to commercial transactions between their residents and out-of-state companies. *Packel*, 524 F.2d at 48. The Third Circuit further found that Pennsylvania was "not attempting to export its public policy on consumer credit interest rates. It merely seeks to afford uniform protection to all Pennsylvania residents with respect to such rates." *Id.*

Similarly, the Seventh Circuit rejected Aldens' challenge to a Wisconsin law that capped the rate of interest that could be charged to Wisconsin residents. Aldens had no physical presence in Wisconsin, no office, place of business or tangible property in Wisconsin, did not advertise in the Wisconsin media, and did not have a Wisconsin telephone number. *Id.* at 747. The Court noted, however, that the Wisconsin law, which placed a cap on interest rate charges, applied to interstate merchants that transact business with "Wisconsin residents while the customer is in Wisconsin." *LaFollette*, 552 F.2d at 747. It also noted "[m]ost especially in the exercise of the police power, state sovereignty is, in many areas of interstate commerce, parallel to and concurrent with that of the federal government." *Id.* (citing *Huron Portland Cement Co.*

v. City of Detroit, 362 U.S. 440, 442 (1960); *California v. Thompson*, 313 U.S. 109, 112-113 (1941)). The Seventh Circuit rejected Aldens' Dormant Commerce Clause challenge.

The Tenth Circuit also rejected Aldens' Dormant Commerce Clause challenge to the application of Oklahoma law to its business, noting that "[i]t is clear from times prior to *International Shoe* that the state can regulate the consequences of commercial transactions on its citizens which arise or are directed from outside its borders." *Ryan*, 571 F.2d at 1161 (italics added). The Tenth Circuit noted that "recent decisions on the point have discarded, for these purposes, the established doctrines of reliance on place of sale, place of delivery, the 'presence' concept, ***place of contract***, and place of performance which may be well recognized for other purposes." *Id.* (emphasis added)

The Second Circuit's holding in *SPGGC, LLC v. Blumenthal*, 505 F.3d 183 (2nd Cir. 2007) is also instructive. *SPGGC* sold gift cards over the Internet (and other channels) around the country, including to Connecticut consumers. Connecticut's gift card law prohibits inactivity fees to protect Connecticut consumers from unwittingly being deprived of the value of gift cards they purchase. *Id.* at 187. *SPGGC* sued the Connecticut Attorney General to enjoin him from applying this law to the company's sales to Connecticut consumers, arguing that doing so would run afoul of the Dormant Commerce Clause. *SPGGC* argued that applying Connecticut law to online transactions would be "extraterritorial." *Id.* at 195. The Second Circuit, however, rejected this Dormant Commerce Clause argument:

> The fact that an ordinary commercial transaction happens to occur in cyberspace does not insulate it from otherwise applicable state consumer protection laws... Based on the facts alleged, we see no risk that the Connecticut Gift Card Law will control sales of gift cards to anyone other than Connecticut consumers, whether such sales occur in person or online.

Id. at 195. In other words, so long as the Connecticut law was applied to transactions with Connecticut consumers, the Dormant Commerce Clause was not violated. The exact same reasoning applies here: Minnesota law is merely being applied to loans Defendants made to Minnesota borrowers who were physically in Minnesota when making the loan. There is nothing unconstitutional about applying Minnesota law to such transactions.

B. Defendants Misread the *Berman* Case and Misconstrue the Importance of "Consummation."

Defendants' argument that their loans were not "consummated" in Minnesota cannot be reconciled with the well-established Dormant Commerce Clause principles discussed above. As an initial matter, federal circuit courts that have addressed the issue have disavowed reliance on doctrines such as the "place of contract" or the "place of performance" when analyzing Dormant Commerce Clause issues. *Ryan*, 571 F.2d at 1161. No court has abandoned the traditional "wholly extraterritorial" test for the "consummation" test and the *Berman* case, when read properly, does not either.

Rather than addressing the facts showing how its commerce occurred at least partially, if not primarily, in Minnesota, Defendants mostly ignore the "wholly outside" standard articulated by the United States Supreme Court. Instead, Defendants try to rely on *Berman, P.C. v. City of New York*, 2012 WL 4514407 (E.D.N.Y. 2012)[2], but miss the central point of the case. Crucially, the *Berman* court does not disavow the "wholly outside" standard for Dormant Commerce Clause analysis—it embraces it. *Berman*, 2012 WL 4514407 at *17. Moreover, the *Berman* court cites favorably to and relies on *Quik Payday* and *SPGGC*, two decisions discussed

[2] Defendants also rely on *FTC v. Payday Financial, LLC*, 2013 WL 1309437 (D.S.D. 2013), but this decision does not analyze the Dormant Commerce Clause. Instead, this decision relates to whether an Indian tribal court has jurisdiction over a non-member of the tribe who entered into a contract with a member of the tribe. *Id.* at *1. Accordingly, there is no support for Defendants' novel interpretation of the Dormant Commerce Clause in this Indian Law decision.

above that plainly support the application of Minnesota law in this case. In other words, the *Berman* court recognizes that when a payday loan borrower is a resident of a state and obtains a payday loan over the Internet, the law of the state where the borrower was present can be applied without running afoul of the Dormant Commerce Clause. *Berman* at *21-*22 (discussing how *Quik Payday* was properly decided). Accordingly, the *Berman* court's reasoning cannot possibly support Defendants' position here.

What Defendants fail to appreciate is that the *Berman* court was wrestling with a very different fact pattern than the one presently before the Court. The *Berman* court was trying to determine the proper scope of the Dormant Commerce Clause where *both parties* were physically outside the state when they entered into a transaction. *See Berman* at *27 (noting that to the extent the parties were both physically outside New York, then it might raise Dormant Commerce Clause concerns to apply New York law, but holding that the party raising the Dormant Commerce Clause challenge had failed to submit sufficient evidence to support its claims).

It is for this reason that the *Berman* court notes that the *Midwest Title* case "is perhaps most similar to the case here." 2012 WL 4514407 at *20. In *Midwest Title*, residents of Indiana had physically left Indiana and traveled to Illinois. *Midwest Title Loans, Inc. v. Mills*, 593 F.3d 660, 662 (7th Cir. 2010). While in Illinois, the Indiana residents visited a storefront operated by an Illinois title lender and entered into loan transactions at that Illinois storefront. *Id.* The Indiana Consumer Credit Code purported to apply to loan transactions that occurred in other states, and Indiana alleged that the Indiana law applied the title lender's loans to Indianans who had traveled to Illinois. *Id.* The Seventh Circuit affirmed the district court's holding that this application of Indiana law to transactions in which Indiana residents traveled to Illinois ran afoul

of the Dormant Commerce Clause. *Id.* at 669. By relying on *Midwest Title* and saying it is "most similar" to the case at bar, the *Berman* court is clearly indicating that the fact pattern it is addressing is one where *both* parties to the transaction were physically in another state. Thus, when the *Berman* court discusses "consummation" wholly outside a given state, it is referring to the instance where both parties are physically present in another state. There is no other way to read *Berman* consistent with *Quik Payday*, *Midwest Title,* and all of the other cases that the *Berman* court explicitly accepts and purports to adopt.

Indeed, the district court decision in *Midwest Title*, affirmed by the Seventh Circuit and relied upon by Defendants (Def. Memo. at 10) and by the *Berman* court, draws this distinction even more clearly when it describes the line of authorities rejecting Dormant Commerce Clause challenges:

> [I]n each of these cases, the customer was located in his or her home state when he or she ordered merchandise and entered into the purchase contract. Under the *Dean Foods* analysis, such transactions could not be held to have occurred wholly outside the customer's state.

Midwest Title v. Ripley, 616 F.Supp.2d 897, 906 (S.D. Ind. 2009). This is the crucial distinction between the instant case and the Dormant Commerce Clause decisions striking down the application of state law to a given transaction. In decisions where the Dormant Commerce Clause was held to prohibit the application of state law to a given transaction, both parties were physically outside of the state during the transaction. This is true in *Midwest Title* and *Dean Foods*, both relied upon by Defendants, and *Berman* (although the *Berman* court ultimately held it did not have sufficient facts to rule one way or the other on the Dormant Commerce Clause). But where the borrower to a loan transaction is physically in Minnesota—as the State alleges the borrowers were here—there is no constitutional prohibition on applying Minnesota law to that transaction.

The Minnesota Court of Appeals has similarly recognized that where one party to a transaction is physically in Minnesota during the transaction, there is no Dormant Commerce Clause prohibition on applying Minnesota law to the transaction. In *Rio/Bill Blass v. Bredeson Assocs., Inc.*, 1998 WL 27299, No. C6-97-1386 (Minn. Ct. App., Jan. 27, 1998),[3] a Minnesota corporation sought to confirm an arbitration award against a New York corporation for unpaid commissions under the Minnesota Sales Representative Act ("MSRA"), Minn. Stat. § 325E.37. Raising arguments similar to those raised by Defendants, the defendant argued that the MSRA violated the Dormant Commerce Clause. In rejecting defendant's constitutional challenge, the court noted that the state statute "by its own terms regulates only agreements with sales representatives who are Minnesota residents, have their principal place of business in Minnesota, or whose sales territory includes part or all of the state." *Id.* In this respect, the Minnesota lending laws as applied here are indistinguishable from the statutes at issue in *Rio/Bill Blass*, and the same legal conclusion follows. Again, in this case, Minnesota is only attempting to regulate loans made to Minnesota citizens, when those citizens were physically located in the State.

Even if "consummation" was the relevant standard (which no court other than the Eastern District of New York has ever suggested—and in that case under different facts), there are no facts in the record to support Defendants' argument that the consummation of these loans occurred in South Dakota.[4] Indeed, the only courts to have reviewed Defendants' argument have

[3] In accordance with Minn. Stat. § 480A.08(3), unpublished opinions are attached as exhibits to the Affidavit of Daniel C. Bryden.

[4] Defendants assert, without citing any support, that the loan contracts here were consummated when "executed" by Western Sky, Def. Memo. at 8, but factual allegations outside the Complaint are not admissible on a motion to dismiss. *See N. States Power Co. v. Franklin*, 122 N.W.2d 26, 30 (Minn. 1963) (holding that court must accept the facts alleged in the complaint as true and must construe all reasonable inferences in favor of the nonmoving party on a motion to dismiss).
(Footnote Continued on Next Page)

determined that consummation occurs where the borrower resides, not on the reservation. Again, the Ramsey County District Court held that the loans were consummated in Minnesota, where the loan proceeds were deposited. *See* Brennaman Aff., Ex. D. Other courts have held similarly. *See Colorado v. Western Sky Fin.*, 845 F.Supp.2d 1178, 1182 (D. Colo. 2011) (ordering remand and noting that "this is not a case about commercial activity on Indian lands"); *Colorado v. Western Sky Fin., LLC et al.*, No. 11-CV-638, April 15, 2013 Order at 7-8 (holding that Western Sky's lending does not occur on the reservation); *State of West Virginia v. Payday Loan Resource Center, LLC*, Kanawha County Circuit Court, West Virginia, No. 10-MISC-372, Oct. 28, 2011 Final Order Granting State's Petition To Enforce Investigative Subpoena, Discussion ¶¶ 4-5 (holding that loan transactions between other Martin Webb lending companies and West Virginians did not occur on the reservation).[5] Thus, in addition to being legally untenable, Defendants' "consummation" argument also fails as a factual matter on this Motion to Dismiss, when the State's allegations must be taken as true, and all reasonable inferences must be made in its favor.

In short, this case is not similar to *Berman*, *Dean Foods*, and *Midwest Title*, which are the only cases Defendants can cite to, but which all involve fact patterns where *both* parties to a transaction were physically outside the state whose law is asserted to apply to the transaction.[6]

(Footnote Continued from Previous Page)

[5] This decision is attached as Exhibit U to the Bryden Affidavit submitted in support of the State's Motion for a Temporary Injunction. While facts outside the Complaint are not before the court on a motion to dismiss, the parties may submit unpublished decisions for the court's consideration.

[6] Defendants' reliance on *MorEquity, Inc. v. Naeem*, 118 F.Supp.2d 885 (N.D. Ill. 2000) is misplaced. *MorEquity* does not apply the Dormant Commerce Clause or its standards, and provides no guidance on the constitutional issue before the Court. Instead, it relates merely to a (Footnote Continued on Next Page)

C. Granting Defendants' Motion to Dismiss Would Violate Core Principles of Federalism and Prevent the State from Addressing Known Problems Within Its Borders.

States are entitled to protect their residents from abusive business practices. Every state has consumer protection statutes of one form or another, and most states have usury laws and regulate small loan lending. Our federalist system has long left these particular areas to the state police powers. Unless federal law preempts state enforcement, companies that operate nationally *already* comply with the various states' laws when they do business with the residents of any given state. Defendants actively advertised in Minnesota and chose to lend to Minnesota residents. There is nothing unfair or unforeseeable about Minnesota regulating those transactions.

III. The Present Action Is Not Barred by the Doctrine of Tribal Immunity.

The doctrine of tribal sovereign immunity protects Indian tribes from certain state laws absent a clear waiver by the tribe or congressional abrogation. *Santa Clara Pueblo v. Martinez*, 436 U.S. 49, 63-64, 98 S.Ct. 1670, 1680 (1977). This doctrine recognizes that Indian tribes are "domestic dependent nations" that exercise inherent sovereign authority over their members and tribes. *Okla. Tax Com'r v. Citizen Band Potawatomi Indian Tribe of Okla.*, 498 U.S. 505, 509, 111 S.Ct. 905, 909 (1991) (citing *Cherokee Nation v. Georgia*, 5 Pet. 1, 17, 8 L.Ed. 25 (1831)). Tribal immunity does not extend to individual tribe members. *Puyallup Tribe, Inc. v. Dep't of*

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feature of federal regulation of FDIC-insured banks (which Defendants are *not*). Under 12 U.S.C. § 1831d(a), FDIC-insured banks may charge the interest rates prevailing in their home state when the bank enters into a transaction with a party in another state. The FDIC opinion letter invents a three-part test for determining whether the state where the bank is chartered or the state where the branch office is located is the home state for any given loan from an FDIC-insured bank. This standard fails to apply well-established Dormant Commerce Clause principles, and where Defendants' loans were "made" is not the constitutional question. Accordingly, *MorEquity* is irrelevant.

Game, 433 U.S. 165, 171-72, 97 S.Ct. 2616, 2620 (1977). In *Puyallup*, the United States Supreme Court held that a state's suit to enjoin violations of state law by individual tribe members was permissible, as the doctrine of tribal immunity does not immunize individual tribe members. *Id.*; *see also Potawatomi*, 498 U.S. at 514, 111 S.Ct. at 912 (holding that "individual agents or officer of a tribe" remain liable for damages brought by a state, despite their tribe's enjoyment of sovereign immunity); *Swenson v. Nickaboine*, 793 N.W.2d 738, 744 n.1 (Minn. 2011) (recognizing that tribal immunity does not immunize individual members of a tribe).

Nor will the doctrine of tribal immunity protect a tribal business from a state's reach unless the Court finds that "the entity acts as an arm of the tribe so that its activities are properly deemed to be those of the tribe." *See Cash Advance & Preferred Cash Loans v. State*, 242 P.3d 1099, 1109 (Colo. 2010) (citing *Allen v. Gold Country Casino*, 464 F.3d 1044, 1046 (9th Cir. 2006)). Courts examine a number of facts to determine whether an entity is acting as an arm of the tribe including: (1) whether the tribe owns and operates the entity, (2) whether the entity is dependent upon tribal government approval, (3) whether the entity's benefits, both economic and otherwise, inured to the tribe in its sovereign capacity, and (4) whether the entity's immunity directly protected the tribe's treasury. *Id.*; *see also Hagen v. Sisseton-Wahpeton Cmty. Coll.*, 205 F.3d 1040, 1043 (8th Cir. 2000); *Allen*, 464 F.3d at 1046 (9th Cir. 2006). The central inquiry is whether the entity operates "not as a mere business," *Hagen*, 205 F.3d at 1043, but rather as an extension of the tribe's own economic activity, "so that its activities are properly deemed to be those of the tribe." *Allen*, 464 F.3d at 1046.

Under the facts alleged in the State's Complaint, Defendants cannot be granted dismissal based on either tribal immunity or the "arm of the tribe" doctrine. The State's Complaint specifically alleges that "Western Sky . . . is not owned or operated by an Indian tribe, is not a

tribal entity, and does not exist for the benefit of a tribe." Complaint at ¶ 23. Western Sky is owned and operated by an individual named Martin Webb, who takes the profits made by Western Sky for himself. *Id.* Defendants are California and Delaware companies that have no independent connection or affiliation with any Indian tribe. *Id.* at ¶¶ 5-7. Defendants do not appear to dispute these facts and, in any event, they must be taken as true for purposes of this Motion.

Defendants nevertheless argue that they are protected by a doctrine they describe as "tribal member immunity,"[7] but the United States Supreme Court has held that there is no such thing. *Puyallup*, 433 U.S. at 171-72 ("[W]hether or not the Tribe itself may be sued in a state court without its consent or that of Congress, a [state] suit to enjoin violations of state law by individual tribe members is permissible. The doctrine of sovereign immunity...does not immunize the individual members of the Tribe.") Defendants attempt to skirt this well-established rule, but the cases they rely on only repeat basic principles of tribal sovereign immunity. They do not create a new doctrine for "member immunity."

Both the *Williams* and *Montana* cases cited by Defendants address what effect state regulation would have on the ***sovereign interests of a tribe*** (not an individual tribe member). In *Williams*, Lee, a non-Indian, operated a general store on a reservation, selling goods to tribal members, under a license required by federal law. *Williams v. Lee*, 358 U.S. 217, 79 S.Ct 2693 (1959) (citing 25 U.S.C. § 262). Lee brought suit against the Williamses, tribal members, to collect for goods sold on the reservation on credit. *Id.* The United States Supreme Court reversed a judgment in Lee's favor, holding that Lee's action "infringed on the right of

[7] At the hearing on the State's Motion for Temporary Injunction, on August 22, 2013, Defendants' attorney asserted that "tribal member immunity" was the type of immunity being sought by Defendants.

reservation Indians to make their own laws and be ruled by them." *Id.* at 220, 271 (citing *Utah & N. Ry. Co v. Fisher*, 116 U.S. 28, 6 S.Ct. 246 (1885) (emphasis added).

The *Montana* case addressed the issue of whether a tribe had jurisdiction to prohibit nonmembers from hunting or fishing on reservation property that was no longer owned by the tribe. *Montana v. United States*, 450 U.S. 544, 101 S.Ct. 1245 (1981). The United States Supreme Court held that the tribe was not authorized to regulate such activity. *Id.* at 654, 1258. The Court noted that tribal sovereign power only extended to "***what is necessary to protect tribal self-regulation*** or to control internal relations." *Id.* (internal citations omitted) (emphasis added).

Finally, in *Pourier v. South Dakota Dept. of Rev.*, the Court's inquiry was whether the state had power to tax a member-owned corporation. 658 N.W.2d 395 (S.D. 2003). In that case, the corporation (1) was licensed to do business on the reservation, (2) exclusively sold its fuel at its retail gas station on the reservation, and (3) sold approximately 90% of its goods to reservation Indians. *Id.* at 397-398. Based on those factual circumstances, the Court held that the state did not have power to tax a corporation owned by a tribal member doing business on the reservation ***for the benefit of reservation Indians***. *Id.* at 404 (emphasis added).

The common theme running through these cases is that a state will only be prohibited from exercising jurisdiction when ***tribal sovereignty*** is threatened—not because of the interests of any particular tribal member are threatened. Far from standing for any separate principle of "tribal member immunity" the cases cited by Defendants are simply reiterations of the basic concept of tribal immunity, described above. There is nothing in the State's Complaint to support that the Cheyenne River Sioux Tribe is even remotely interested in, or involved in, Western Sky, or that this Tribe's sovereignty is threatened by regulation by the State of Western Sky's loans to Minnesotans. To the contrary, the Complaint alleges that CashCall and its

subsidiaries are the primary beneficiaries of the lending scheme, that Defendants control almost every aspect of the advertisements, origination, funding, and servicing of the loans, and that Western Sky is merely used as a "front" used by Defendants to evade state law. Complaint at ¶ 18-23. Western Sky does not operate for the benefit of the tribe. *Id.* Western Sky is a limited liability corporation created under South Dakota law, and its sole member is Mr. Webb, who retains Western Sky profits for himself. *Id.*

Other courts to have examined this exact scheme have repeatedly held that neither Western Sky nor Defendants are entitled to tribal immunity. These courts have specifically rejected the "member immunity" argument advanced by Defendants here. In *Colorado v. Western Sky Financial, LLC et al.*, the Denver County District Court ruled in favor of Colorado on its summary judgment motion, holding that Webb, as an enrolled tribal member, was not individually entitled to immunity, nor did his membership in the tribe confer such immunity upon Western Sky. No. 11-CV-638, April 15, 2013 Order; *see also Commr. v. Western Sky Fin. et al.*, No. CFR-FY2011-182, OAH No. DLR-CFR-76A-47146, May 22, 2013 Opinion and Final Order (rejecting Western Sky's sovereign immunity defense, and holding "it is undisputed that tribal sovereign immunity does not protect individual tribal members"); *Virginia v. Payday Loan Res. Center LLC*, Kanawha County Circuit Court, West Virginia, No. 10-MISC-372, Oct. 28, 2011 Final Order Granting State's Petition to Enforce Investigative Subpoena (holding that business conducted by an entity organized under South Dakota law, owned by an individual rather than a tribe, and conducted over the internet was not protected by the doctrine of tribal sovereign immunity); *Missouri v. Webb et al.*, No. 27-CV-13-12740, slip op. at *4-5 (E.D. Mo. March 27, 2012) (holding that Webb, as an enrolled member of the Tribe, was not individually

entitled to immunity, nor did his membership confer such immunity upon the Lending Companies).

Finally, even if this this Court were to find that either Mr. Webb or Western Sky was entitled to tribal immunity—which they are not—Defendants would still not be entitled to dismissal. The State's Complaint alleges that Defendants are the true, or "de facto," lender and that Western Sky is simply a "front" for Defendants' illicit "rent-a-tribe" scheme. Complaint ¶ 22. The Complaint alleges that Defendants control virtually every aspect of the lending and only associate with Western Sky in order to improperly give an air of legitimacy to its illegal lending. *Id.*, ¶¶ 18-23. These facts must be taken as true for purposes of this Motion. Defendants cannot obtain dismissal simply by pointing to the very conduct the State claims is fraudulent.

IV. THE STATE IS NOT ESTOPPED FROM BRINGING THIS ACTION.

Defendants argue that the instant action is barred by the doctrines of collateral estoppel, res judicata, and/or equitable estoppel, due to the Minnesota Department of Commerce's ("DOC's") voluntary dismissal of a prior administrative action under one statute, Minn. Stat. § 47.60, involving three consumers loans. Defendants fail to explain, however, how the agency's voluntary dismissal of that action could possibly bar the instant action, which among other things, seeks future injunctive relief, restitution for an entire class of consumers (some of whom obtained loans after the DOC voluntarily dismissed its regulatory action), and asserts violations of state statutes that were not at issue in the prior agency action. Defendants fail to establish any of the required elements for any type of estoppel, and their argument should be rejected in its entirety.

A. Defendants' Estoppel Argument Ignores the Statutory Administrative Process, which Provides that an Agency has the Final Say on ALJ Recommendations.

For their estoppel argument, Defendants focus on the Administrative Law Judge's ("ALJ's") dismissal with prejudice, but ignore the Agency's ultimate dismissal of the case ***without prejudice***. Defendants do not attempt to argue that this final Agency determination changing the ALJ's decision was contrary to the law or administrative procedure in any way. In fact, the agency's decision followed Minnesota Statutes Chapter 14.

Under the Administrative Procedure Act (APA), Chapter 14 of the Minnesota Statutes, the agency decision is the final decision on all contested case hearings, unless: 1) the agency orders that the decision of the ALJ constitutes the final decision in the case, Minn. Stat. § 14.57, subd. 1; or 2) if the agency fails to act within 90 days after the record closes, Minn. Stat. § 14.62, subd. 2a. The record closes after exceptions are filed by the parties in response to the ALJ's "report." Minn. Stat. § 14.61, subd. 2.

Here, it is uncontested that there was no ALJ "order" constituting the "final decision" in the Western Sky contested case. Therefore, the record did not close until exceptions were received. Minn. Stat. § 14.61, subd 2. As required by statute, the final decision of the agency included the reasons for modifying the ALJ's recommendation. § 14.62, subd. 1. While Defendants take issue with the delay between the ALJ's recommendation and the request for filing exceptions, there is nothing in the APA that requires a shorter timeline than was used.

Defendants argue that the agency's "agreement" to the dismissal should change the analysis. First, the record does not support that the agency agreed to dismissal "with prejudice."

Second, Defendants point to no authority to support that an agency is not entitled to make a final decision modifying the ALJ order in these circumstances.[8]

Accordingly, Defendants cannot show that the ultimate dismissal of the administrative matter ***without prejudice*** was not authorized under the APA. It is therefore the Agency's decision—not the ALJ's recommendation—that is the final decision, leaving no basis for estoppel whatsoever.

B. None of the Theories of Estoppel are Applicable in this Case.

Defendants' inaccurate portrayal of the rules of administrative procedure is not the only problem with their estoppel arguments. Defendants cannot establish the elements required for any form of estoppel because of the numerous differences between the administrative action and this case, and because there was no adjudication of any issues on the merits.

1. Collateral Estoppel Does Not Apply.

Collateral estoppel, or "issue preclusion," is an equitable doctrine. *Barth v. Stenwick*, 761 N.W.2d 502, 508 (Minn. Ct. App. 2009). Defendants have the burden of proving estoppel is available and should be applied. *Id.* Collateral estoppel is not rigidly applied even if all conditions are satisfied, nor is it applied where "its application would work an injustice on the party to be estopped." *State v. Lemmer*, 736 N.W.2d 650, 659 (Minn. 2007). Collateral estoppel occurs when:

> (1) the issue was identical to one in a prior adjudication;
> (2) there was a final judgment on the merits;
> (3) the estopped party was a party or in privity with a party to the prior adjudication; and
> (4) the estopped party was given a full and fair opportunity to be heard on the

[8] The APA specifically provides that, "Agencies may take notice of judicially cognizable facts and . . . may utilize their experience, technical competence, and specialized knowledge in the evaluation of the evidence. . . ." Minn. Stat. § 14.60, subd. 4.

adjudicated issue.

Id. (citation omitted). Because Defendants fail to establish any of these elements, collateral estoppel does not apply.

As to the first element, the issues in the two actions are completely different. The administrative action targets Western Sky, not these Defendants. It alleges claims under one statute, Minn. Stat. § 47.60, which is not at issue here. It identifies only three consumers' loans, while the current action is on behalf of all affected consumers. Even the issue of tribal sovereign immunity is different, since this suit alleges that the Defendants participated in a broad and deceptive "rent-a-tribe" scheme using Western Sky as a front.

The remainder of the elements are unsatisfied as well. For all the reasons described in section A, above, the ALJ's recommendation is not a final judgment on the merits, and there was no adjudication of any issue. In fact, the "merits" of the tribal immunity claim and the § 47.60 lending claim were not discussed by the ALJ. The agency stipulated to voluntary dismissal following deceptive representations by Western Sky about the application of the doctrine to its conduct. To establish collateral estoppel, Defendants must show, along with the other elements, that the issue of tribal immunity was "distinctly contested and directly determined" in an earlier adjudication and "necessary and essential to the resulting judgment in that action." *Hauschildt v. Beckingham*, 686 N.W.2d 829, 838-39 (Minn. 2004) (internal citations omitted); *see Roseberg v. Steen*, 363 N.W.2d 102, 105 (Minn. Ct. App. 1985) (holding that collateral estoppel only operates to matters actually litigated, determined by and essential to a previous judgment). Because the issue of tribal immunity was not adjudicated, and for the other reasons discussed above, collateral estoppel cannot now be applied.

2. Res Judicata Does Not Apply.

The elements of res judicata, or "claim preclusion" are:

(1) the cause of action or claim involved the same parties or their privies;
(2) there was a final judgment on the merits;
(3) the estopped party had a full and fair opportunity to litigate the matter, and
(4) the cause of action or claim involved the same set of factual circumstances.

See Rucker v. Schmidt, 794 N.W.2d 114, 122 (Minn. 2011). As discussed above, the ALJ decision on which Defendants rely is not a final judgment on the merits. Nor do any of the other factors of res judicata apply.

Commonality of interests alone is insufficient to establish privity. *Lemmer*, 736 N.W.2d at 660. Minnesota courts consider whether the party: (1) had a controlling participation in the first action, (2) had an active self-interest in the previous litigation, or (3) had a right to appeal from a prior judgment. *Id.* at 661 (citations omitted). Here, as a part of their defense in general, Defendants studiously maintain the fiction that CashCall is completely separate from Western Sky, is simply an assignee, and exercises no control over Western Sky. Defendants cannot simultaneously argue that CashCall had a controlling interest in the previous litigation, yet divorce themselves from Western Sky for the purpose of defending against the State's claims in this action.[9]

[9] Likewise, there is no privity between the Department of Commerce and the Attorney General's Office. *Lemmer*, 736 N.W.2d at 660 ("Collateral estoppel will not apply between the two government agencies [i]f the second action involves an agency or official whose functions and responsibilities are so distinct from those of the agency or official in the first action that applying preclusion would interfere with the proper allocation of authority between them.") The Attorney General is specifically empowered by statute to enforce Minnesota law with respect to "unlawful practices in business, commerce or trade" and to seek injunctive relief and civil penalties for the violation of such laws. Minn. Stat. § 8.31. In addition, the Attorney General has "extensive common-law powers which are inherent in [her] office" including the authority to seek restitution for Minnesotans who have been harmed by a defendant's illegal practices. *Dunn v. Schmid,* 60 N.W.2d 14, 17 n.8 (Minn. 1953); *State by Humphrey*, 490 N.W.2d at 896 n. 4. No
(Footnote Continued on Next Page)

The claims at issue in the administrative action and this lawsuit are different. First, the statutes that the State seeks to vindicate are different. The administrative action involved only a violation of Minn. Stat. § 47.60. By contrast, this lawsuit alleges violations of the Consumer Fraud Act (Complaint at ¶¶ 58-64.), Deceptive Trade Practices Act (Complaint at ¶¶ 65-72), state usury laws (Complaint at ¶¶ 54-57.), state licensing laws (Complaint at ¶¶ 50-53.), and consumer short-term lender laws (Complaint at ¶¶ 43-49.). Second, the defendants in the two lawsuits are different. The administrative action was against Western Sky, while this lawsuit is against CashCall and its affiliates. Third, the facts are different. The administrative action involved six paragraphs of factual citations involving three consumers. This lawsuit alleges a sweeping "rent-a-tribe" scheme in which defendant CashCall uses non-defendant Western Sky as a "front" to purposefully evade state interest rate caps and other consumer protection laws. Fourth, the relief sought is different. Unlike the regulatory action, this suit seeks restitution for injured borrowers, disgorgement of Defendants' ill-gotten gains by alleging unjust enrichment, and civil penalties under four statutes that were not even raised in the agency's administrative action.

Finally, it should be noted that Defendants seek dismissal of this entire lawsuit based on the agency's voluntary dismissal of the regulatory action against a different party—Western Sky—in August 2012. Even if the doctrine applied (and it does not), dismissal of the lawsuit would be improper. Among other things, this lawsuit seeks *future* injunctive relief. (Complaint at ¶¶ 49, 52-53, 57, 64, 72.) Nearly one-quarter of the states in the country—plus the federal

(Footnote Continued from Previous Page)
restitution was sought in the prior agency Statement of Charges. Because the Attorney General is a distinct constitutional officer with differing authority, functions, and responsibilities than the agency, and therefore not in privity with the agency, it would be improper to estop the Attorney General's claims under res judicata based on the agency's voluntary dismissal of a small regulatory action against a different entity involving different laws.

government—have now taken action against this "rent-a-tribe" scheme. The States seeks to do what regulators across the nation have done; namely, stop this unlawful scheme. The voluntary dismissal of a completely different regulatory action cannot and does not mean the State can never again proceed to halt *future* unlawful conduct by the parties engaged in this unlawful scheme. Furthermore, many consumers for whom the State seeks restitution in this lawsuit took out loans after August 2012, the date the agency action was dismissed. A dismissal of an administrative action would not under any circumstances operate as a bar to claims accruing after that dismissal.

3. Equitable Estoppel Does Not Apply.

Equitable estoppel is a discretionary doctrine. *Barth*, 761 N.W.2d at 508. Even where the elements are met, courts need not apply it. *Id.* The Minnesota Supreme Court has held that a person seeking equitable estoppel against the government bears a "heavy burden of proof." *City of North Oaks v. Sarpal,* 797 N.W.2d 18, 25 (Minn. 2011). For equitable estoppel to apply, Defendants must demonstrate that the State, through its language or conduct, induced Defendants to rely, *in good faith*, on its language or conduct to the Defendants' injury, detriment, or prejudice. *Ridgewood Dev. Co. v. State*, 294 N.W. 2d 288, 292 (Minn. 1980) (emphasis added). Estoppel is only available if the State's "wrongful conduct threatens to work a serious injustice and if the public's interest would not be unduly damaged by the imposition of estoppel." *Id.* at 293.

For equitable estoppel to apply against the State, Defendants must demonstrate:

(1) wrongful conduct on the part of the authorized government agent;
(2) reasonable reliance by the party seeking estoppel on the wrongful conduct;
(3) unique expenditure in reliance on the wrongful conduct; and
(4) a balance of the equities weighing in favor of estoppel.

Sarpal, 797 N.W.2d at 25. The most important element of an equitable estoppel case against the government is wrongful government conduct. *Id.* Wrongful conduct is not established by "simple inadvertence, mistake or imperfect conduct." *Id.* (citing *Bond v. Comm'r of Revenue*, 691 N.W.2d 831, 838 (Minn. 2005)). Rather, it requires a degree of malfeasance. *Id.* (citing *Kmart Corp. v. County of Stearns*, 710 N.W.2d 761, 771 (Minn. 2006)).

Here, there was no wrongful conduct, as the agency complied with the APA. The agency voluntarily dismissed its regulatory action in July 2013 following Western Sky's representations that it was subject to tribal sovereign immunity. The agnecy then undertook a more comprehensive investigation and commenced this action and made allegations similar to those by a quarter of the states in the nation and the federal government. It would be "wrongful" for Defendants to get away with their misrepresentations to the State and evade liability for their unlawful conduct.

As to the second and third elements, Minnesota law requires that Defendants not only relied, but relied in ***good faith***, on the State's action. *Ridgewood Dev. Co. v. State*, 294 N.W. 2d 288, 292 (Minn. 1980). Here, there was no good faith on the part of Western Sky or Defendants, who actively attempted to deceive both the State and the ALJ about the State's ability to regulate the loans. Defendants and Western Sky know that their tribal sovereign immunity defense has failed whenever they have attempted to raise it. Indeed, the Complaint alleges that at least nine States and the federal government have taken action against Defendants and Western Sky to stop this scheme. *See* Complaint at ¶¶ 24 - 34. Defendants' "reliance" was neither reasonable nor in good faith.

The balance of the equities favors the State. There would be no equity in rewarding Defendants' and Western Sky's deception regarding tribal immunity. There would also be no

equity in preventing the State from regulating Defendant's illegal, usurious loans that are harming Minnesotans.

CONCLUSION

For the reasons stated above, Defendants' Motion to Dismiss should be denied.

Dated: August 27, 2013

Respectfully submitted,

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MINN. STAT. § 549.211 ACKNOWLEDGMENT

The party on whose behalf the attached document is served acknowledges through its undersigned counsel that sanctions, including reasonable attorney fees and other expenses, may be awarded to the opposite party or parties pursuant to Minn. Stat. § 549.211.

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