IP 01-1336-C H/S Hudson v. Ace Cash
Judge David F. Hamilton Signed on 5/30/02

NOT INTENDED FOR PUBLICATION IN PRINT

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF INDIANA
INDIANAPOLIS DIVISION

HUDSON, VONNIE T,	)	
	)	
Plaintiff,	)	
vs.	)	
	)	
ACE CASH EXPRESS, INC,	)	
GOLETA NATIONAL BANK,	)	
NEUSTADT, DONALD H,	)	CAUSE NO. IP01-1336-C-H/G
SHIPOWITZ, JAY B,	)	
HEMMIG, RAYMOND C,	)	
ZILLIOX, KAY D,	)	
	)	
Defendants.	)	

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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF INDIANA
INDIANAPOLIS DIVISION

VONNIE T. HUDSON,	)	
	)	
Plaintiff,	)	
	)	
v.	)	CAUSE NO. IP 01-1336-C H/S
	)	
ACE CASH EXPRESS, INC.,	)	
GOLETA NATIONAL BANK,	)	
DONALD H. NEUSTADT, JAY B.	)	
SHIPOWITZ, RAYMOND C. HEMMIG,	)	
and KAY D. ZILLIOX,	)	
	)	
Defendants.	)	

ENTRY ON DEFENDANTS' MOTION TO DISMISS

Plaintiff Vonnie T. Hudson sued defendants ACE Cash Express, Inc., several of its officers, and Goleta National Bank for making a so-called "payday" loan in violation of Indiana usury law, the federal Truth in Lending Act, 15 U.S.C. § 1601 *et seq.*, and the federal Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. § 1961 *et seq.* Because Hudson asserts two claims arising under federal law, the court can also exercise supplemental jurisdiction over her state law claims. See 28 U.S.C. §§ 1331 & 1367. Pursuant to Fed. R. Civ. P. 12(b)(6), defendants have moved to dismiss all asserted claims for failure to state a claim

upon which relief can be granted. For the reasons stated below, the court grants defendants' motion to dismiss.

Dismissal Standard

For purposes of a motion to dismiss under Rule 12(b)(6), the court takes as true the plaintiff's factual allegations and draws all reasonable inferences in the plaintiff's favor. *Veazey v. Communications & Cable of Chicago, Inc.*, 194 F.3d 850, 853 (7th Cir. 1999). "Dismissal under Rule 12(b)(6) is proper only if the plaintiff could prove no set of facts in support of his claims that would entitle him to relief." *Chavez v. Illinois State Police*, 251 F.3d 612, 648 (7th Cir. 2001). However, a plaintiff who pleads additional facts may plead herself out of court by demonstrating that she has no right to recover. *Klug v. Chicago School Reform Bd. of Trustees*, 197 F.3d 853, 859 (7th Cir. 1999) (affirming dismissal of public employee's First Amendment claim based on detailed complaint); *Jefferson v. Ambroz*, 90 F.3d 1291, 1296 (7th Cir. 1996) (affirming dismissal); *Thomas v. Farley*, 31 F.3d 557, 558-59 (7th Cir. 1994) (affirming dismissal).

In this case, Hudson attached several pivotal documents to her complaint. The court may consider these documents in deciding defendants' motion to dismiss. See *International Marketing, Ltd. v. Archer-Daniels-Midland Co.*, 192 F.3d 724, 729 (7th Cir. 1999) (exhibits attached to the complaint are incorporated into

the pleading for purposes of Rule 12(b)(6) motions); Fed. R. Civ. P. 10(c) (a copy of any written instrument which is an exhibit to a pleading is a part thereof for all purposes). "A plaintiff may plead himself out of court by attaching documents to the complaint that indicate that he or she is not entitled to judgment." *In re Wade*, 969 F.2d 241, 249 (7th Cir. 1992) (affirming dismissal of complaint based on attached documents).

Further, when an exhibit to a pleading contradicts an assertion in the complaint and reveals information which prohibits recovery as a matter of law, the information provided in the exhibit can trump the assertion in the complaint. *Whirlpool Financial Corp. v. GN Holdings, Inc.*, 873 F. Supp. 111, 123 n. 18 (N.D. Ill. 1995) (dismissing action), *aff'd*, 67 F.3d 605 (7th Cir. 1995).

Defendants attached documents to their motion to dismiss. The court may consider defendants' documents for purposes of a Rule 12(b)(6) motion only if they are also considered part of the pleadings. *Wright v. Associated Ins. Cos.*, 29 F.3d 1244, 1248 (7th Cir. 1994). Such documents may be deemed part of the pleadings "if they are referred to in the plaintiff's complaint and are central to his claim." *Id.*, citing *Venture Associates v. Zenith Data Systems*, 987 F.2d 429, 431 (7th Cir. 1993); accord, *Menominee Indian Tribe v. Thompson*, 161 F.3d 449, 456

(7th Cir. 1998) (affirming dismissal based on terms of treaties referred to in complaint).

If materials outside the pleadings are attached to a motion to dismiss, the court may consider those materials only if the motion is converted into a motion for summary judgment. Fed. R. Civ. P. 12(b); *Levenstein v. Salafsky*, 164 F.3d 345, 347 (7th Cir. 1998). The plaintiff would ordinarily be entitled to conduct discovery and to offer additional evidence before the court rules on such a converted motion. *Id.*

In this case, however, the documents attached to defendants' motion to dismiss are within the pleadings. Hudson alleged in her complaint that "ACE entered into an agreement or scheme with Goleta National Bank" to avoid the interest rate restrictions imposed by Indiana law. Cplt. ¶ 14. Hudson alleged that the agreement provided for the extension of loans, "purportedly" from Goleta, to persons "visiting ACE payday loan locations in Indiana." *Id.* Hudson further alleged: "The agreement with Goleta was entered into in August 1999 and extended to Indiana about January 2001." *Id.*, ¶ 15.

The defendants' documents include a Master Loan Participation Agreement ("Master Agreement") dated August 11, 1999, and two amendments to that

agreement. The Master Agreement obliges Goleta to sell ACE a participation interest in certain loans. In turn, ACE is obliged to buy those interests. The amendments to the agreement change the percentage interest that ACE must purchase – a detail that is irrelevant for purposes of defendants' motion.

The agreement referenced in Hudson's complaint is clearly the Master Agreement attached to defendants' motion. Accordingly, the Master Agreement and its amendments are within the pleading and may properly be considered in deciding defendants' motion to dismiss.

Factual Allegations

Applying the standard for a Rule 12(b)(6) motion, the court treats the following matters as true for purposes of the motion. Plaintiff Vonnie T. Hudson, an Indiana resident, obtained a $300 loan from an Indiana ACE Cash Express store on January 18, 2001. As part of the loan application process, Hudson signed a "Disclosure Statement and Promissory Note." The note named Goleta National Bank of Goleta, California, as the lender. The note required Hudson to repay a total of $345 on or before February 1, 2001, just two weeks later. The $345 total included repayment of the $300 principal plus a $45 finance charge.

The finance charge was equal to the interest payable on the loan if it had been made at an annual rate of 391.07%.

Hudson also signed a Bank Authorization form that authorized ACE to send her loan application to Goleta National Bank in California. The form stated that Hudson understood and agreed: "The Bank loans are being offered and made, and all credit is being extended, by the Bank in California;" that "The decision about my application and any other credit decision regarding the Bank Loan will be made by the Bank in California;" and that "ACE's involvement is only to transmit or deliver information and other items from you to the Bank or from the Bank to you." Cplt. Ex. A.

The Master Agreement provides that Goleta will sell an undivided participation interest in certain "Bank Loans" to ACE. The Master Agreement does not define "Bank Loan" in great detail, but refers to sample loan documents that were attached to the agreement. Although these sample loan documents are not in the record, even construing the agreement in the light reasonably most favorable to Hudson, the court can infer that ACE agreed to purchase a participation interest in the bank loans that Goleta extends to ACE's customers.

At the time of Goleta's loan to Hudson, ACE was required to purchase an undivided 95% participation interest in these loans.[1] Additionally, Hudson alleges that ACE was solely responsible for collecting payments on her loan and for charging, collecting, and enforcing any late fees and "rollover fees" that might have been incurred. Pl. Reply Br. at 5. Additional facts are noted below, keeping in mind that all reasonable inferences are to be drawn in plaintiff's favor.

Discussion

Hudson's complaint attempts to assert claims for: (1) charging finance charges in excess of amounts permitted by Indiana usury law, (2) failing to make proper disclosures under the federal Truth In Lending Act, 15 U.S.C. § 1601 *et seq.*, and (3) participating in an enterprise to collect unlawful debts in violation of the federal Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §

[1]Hudson alleges that ACE was required to purchase a 100% participation interest in the loan. Cplt. ¶ 15. However, the Master Agreement indicates that only a 95% participation interest was actually purchased. Although the court must draw all reasonable inferences in plaintiff's favor, it is not required to accept allegations that are directly contradicted by documents incorporated by reference into plaintiff's complaint. *Whirlpool Financial Corp. v. GN Holdings, Inc.*, 873 F. Supp. at 123 n. 18, citing *Hamilton v. O'Leary*, 976 F.2d 341, 345 (7th Cir. 1992), and 5 Charles Wright & Arthur Miller, Federal Practice and Procedure: Civil 2d § 1327, at 766-67 (2d ed. 1990). Moreover, in light of *Marquette National Bank v. First of Omaha Serv. Corp.*, 439 U.S. 299 (1978) and *Krispin v. May Dep't Stores Co.*, 218 F.3d 919 (8th Cir. 2000), discussed below, the exact percentage of the participation interest sold does not affect the controlling legal issue.

1961 *et seq.* Hudson's federal claims are based on the premise that ACE is making loans at interest rates that are illegal under Indiana law.

Under the Indiana Uniform Consumer Credit Code ("IUCCC"), Ind. Code § 24-4.5-3-508(2), a supervised lender is prohibited from charging interest greater than 36% per year on "that part of the unpaid balances of the principal which is three hundred dollars or less." The Indiana Loansharking Statute, Ind. Code § 35-45-7-2, makes it a felony to extend loans at more than 72% interest per year. Under the IUCCC and the Indiana Loansharking Statute, lenders are also prohibited from imposing finance charges that, when expressed as an equivalent interest rate, violate the statutes' respective interest rate restrictions. *Livingston v. Fast Cash USA, Inc.*, 753 N.E.2d 572, 577 (Ind. 2001) (holding that loan finance charges for supervised loans are limited by the maximum 36% interest rate allowed under Ind. Code § 24-4.5-3-508(2) and the maximum 72% interest rate allowed under Ind. Code § 35-45-7-2).

Hudson paid a $45 fee to finance a two-week $300 loan from Goleta, the equivalent of paying interest at an annual rate of 391.07%. Thus, if Indiana law applied here, Hudson's loan would violate Ind. Code §§ 24-4.5-3-508(2) and 35-45-7-2. Indiana law, however, does not govern Hudson's loan.

Goleta, the lender, is a national bank. As a national bank, Goleta may charge interest on its loans at the rate permitted by the state in which it is located, California. 12 U.S.C. § 85; *Marquette National Bank v. First of Omaha Serv. Corp.*, 439 U.S. 299 (1978) (holding that § 85 of the National Bank Act, not state law, governs the rates at which national banks are permitted to charge interest); see also *Smiley v. Citibank (South Dakota) N.A.*, 517 U.S. 735 (1996) (holding that late payment fees constitute "interest" for purposes of § 85).

Article XV of the California Constitution exempts from any interest rate ceiling "loans made by . . . any bank created and operating under and pursuant to any laws of this State or of the United States of America . . . ." Thus, under the National Bank Act, there was no cap on the interest rate that Goleta could have lawfully charged Hudson.

Hudson argues that there is a genuine issue as to whether Goleta was the actual lender. Hudson contends that Goleta's role in servicing her loan was so insignificant that the court should regard ACE as the true lender – even though Goleta issued her loan. Pl. Mot. to Strike at 6. Hudson also suggests that the court should regard ACE as the true lender because defendants' lending arrangement was designed for the sole purpose of circumventing Indiana usury law. For purposes of the motion to dismiss, the court accepts Hudson's factual

premises regarding Goleta's role and defendants' purposes in making the loans. These arguments might appeal to those who believe substance should always trump form in the law, and they may provide a reasonable foundation for closer federal regulation of national banks that engage in such transactions. These arguments do not, however, offer a basis for giving Hudson any relief.

In *Marquette National Bank*, the Supreme Court held that § 85 authorizes a national bank in one state to charge its out-of-state credit card customers any interest rate allowed by its home state, even when that rate is greater than the rate permitted by the state of the bank's nonresident customers. 439 U.S. at 317-18. The Supreme Court recognized that § 85 "will significantly impair the ability of States to enact effective usury laws." *Id.* at 318. However, the Court added that "the protection of state usury laws is an issue of legislative policy, and any plea to alter § 85 to [protect state usury laws] is better addressed to the wisdom of Congress than to the judgment of this Court." *Id.* at 319. The reasoning of *Marquette National Bank* is not limited to charges labeled as "interest," but also extends to fees applied to loans, such as late payment fees, as the Supreme Court held in *Smiley v. Citibank*, 517 U.S. 735. Like the plaintiff in *Marquette National Bank*, Hudson challenges a national bank's practice of imposing finance charges allowed by its home state on its out-of-state customers whose states of residence would outlaw the charges.

The Eighth Circuit's decision in a similar case, *Krispin v. May Dep't Stores Co.*, 218 F.3d 919 (8th Cir. 2000), demonstrates that Goleta and ACE's lending arrangement is lawful under § 85 even if the purpose of the arrangement was to avoid application of state usury laws. In *Krispin*, the defendant Missouri department store issued credit cards to the plaintiffs in Missouri. The store later assigned its entire interest in the credit cards to a wholly-owned subsidiary national bank in Arizona. The store then issued a notice to plaintiffs stating that credit was being extended by the Arizona national bank. However, the store purchased the credit card receivables originated by the bank on a daily basis and collected and received cardholders' payments.

The plaintiffs sued the store, alleging that the late fees charged on their credit cards violated Missouri law. Plaintiffs argued that the National Bank Act did not apply because (a) plaintiffs entered into their credit agreements with the Missouri store, (b) the Missouri store "remained substantially involved in the collection process," and (c) the Missouri store retained a financial interest in the accounts even after assigning its interest to the Arizona national bank. *Krispin*, 218 F.3d at 923.

The Eighth Circuit held the credit agreements were bank loans governed by § 85. To determine whether § 85 governed, the Eighth Circuit stated,

> it makes sense to look to the originating entity (the bank), and not the ongoing assignee (the store), in determining whether the [National Bank Act] applies. . . . [F]or purposes of deciding the legality of the late fees charged to appellants' credit accounts, we find that the real party in interest is the bank, not the store.

Krispin, 218 F.3d at 924 (citation omitted). The Eighth Circuit looked to the bank despite the store's daily purchase of the bank's receivables, which significantly reduced the bank's financial stake and risk of loss concerning the loans.

The Eighth Circuit decided *Krispin* on a motion for summary judgment, finding there was no genuine issue of material fact regarding the defendants' roles in plaintiff's loan. In contrast, this case is before the court on a motion to dismiss. Thus, the court is concerned only with the legal, not factual, sufficiency of the complaint. *Szabo v. Bridgeport Machines, Inc.*, 249 F.3d 672, 675 (7th Cir. 2001). However, the significance of this procedural distinction is diminished, if not eliminated, by the comprehensiveness of Hudson's complaint. The factual allegations in Hudson's complaint closely parallel the Eighth Circuit's factual findings in *Krispin*. Thus, this court is faced with the same legal question as was the Eighth Circuit, despite the different procedural posture.

In contrast to the national bank in *Krispin*, which held no financial stake in the loans, Goleta retained a 5% stake in its loan to Hudson. Further, Goleta's

sale of a participation interest to ACE neither destroyed the debtor-creditor relationship between Goleta and Hudson nor created privity between ACE and Hudson. *Cottage Savings Ass'n v. Commissioner of Internal Revenue*, 499 U.S. 554, 557 n.3 (1991) ("By exchanging merely participation interests rather than the loans themselves, each party retained its relationship with the individual obligors."); *First National Bank of Louisville v. Continental Illinois Nat'l Bank and Trust Co. of Chicago*, 933 F.2d 466, 467 (7th Cir. 1991). In *First National Bank of Louisville*, the Seventh Circuit described a typical lending arrangement involving the sale of participation interests:

> [O]ne bank – the "lead bank" – first makes the loan agreement with the borrower and then makes a separate agreement – the participation agreement – with other banks, to which the lead bank sells shares in the loan . . . . The result is that only the lead bank has a direct contractual relationship with the borrower.

Id. at 467.

As a matter of law, § 85 of the National Bank Act governs the fees and interest rate that Goleta charged Hudson in this case. The record shows that Goleta actually made the loan and retained an even greater financial interest in its loan to Hudson than the national bank in *Krispin*, which the Eighth Circuit held sufficient to invoke the National Bank Act in that case.

While Hudson acknowledges the preemptive force of § 85, she contends the statute should be construed so as not to apply to national bank loans made for the purpose of evading state usury laws, or to loans in which a national bank "rents" its charter to some other entity. The position has some superficial appeal, but the court rejects it. Hudson invites the courts to draw boundaries between federal and state bank regulation depending upon the subjective purpose of those engaged in the transaction and/or the precise extent of financial risk accepted by the national bank. The court sees no basis for drawing jurisdictional boundaries in such an uncertain and unpredictable way, at least as a matter of statutory construction, although these arguments may well appeal to federal banking regulators concerned about the "rental" of national bank charters. See *Marquette National Bank*, 439 U.S. at 319 (concerns about protection of state usury laws present questions of legislative policy better addressed by Congress); see also *Cades v. H & R Block, Inc.*, 43 F.3d 869, 873-74 (4th Cir. 1994) (out-of-state bank's use of local agent to make loans did not affect preemptive force of National Banking Act); *Christiansen v. Beneficial Nat'l Bank*, 972 F. Supp. 681, 684-85 (S.D. Ga. 1997) (same, so long as local agency did not amount to branch of national bank); *Basile v. H & R Block, Inc.*, 897 F. Supp. 194, 198-99 (E.D. Pa. 1995) (same).[2]

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[2]In March 2002, the State of Indiana enacted House Enrolled Act 1075, which adds a chapter on "small loans" to the Indiana Uniform Consumer Credit (continued...)

Regarding those federal banking regulators, Hudson contends that the Comptroller of the Currency has taken the position that interstate lending arrangements similar to those of Goleta and ACE are unlawful under the National Bank Act. She cites the Comptroller's announcement on January 3, 2002 that Eagle National Bank signed a consent order agreeing to cease all payday lending activities. Pl. Mot. to Strike, Ex. A. However, the consent order states that the Comptroller opposed Eagle's payday lending activities because they were conducted in a manner that compromised the financial soundness of the bank. The Comptroller did not opine that interstate payday lending activities were unlawful as a general matter. In any event, the Comptroller's statements are a matter of federal enforcement policy, not state or federal law.

Hudson also argues that she has a viable claim against defendants based on a district court's decision to remand a similar case against ACE to state court. In *Long v. ACE Cash Express, Inc.*, Case No. 3:00-CV-1306-J-25TJC (M.D. Fla. June 18, 2001) (attached as Exhibit D to Pl. Mot. to Strike), the plaintiff sued ACE only under state law for making a loan at a usurious interest rate. Pl. Mot.

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[2](...continued)
Code as Ind. Code § 24-4.5-7-101 *et seq.* The chapter is drafted to apply to payday lending activities, and it is drafted to apply to, among others, "any person who facilitates, enables, or acts as a conduit for any lender who is or may be exempt from licensing under IC 24-4.5-3-502." Ind. Code § 24-4.5-7-102(2). The court expresses no view on issues that might arise under this new provision.

to Strike, Ex. C. Plaintiff did not sue the bank that apparently made the loan, which was also Goleta National Bank. ACE removed the case to federal court on the theory that Goleta was an indispensable party to the litigation and that once Goleta was joined, the National Bank Act would completely preempt plaintiff's claims, which arose solely under Florida law.

The district court in *Long* noted that plaintiff alleged that she entered a loan agreement with ACE, despite loan documents showing that she entered a loan agreement with Goleta. Pl. Mot. to Strike, Ex. D at 2. Judge Adams reasoned that the National Bank Act could not preempt the entire field of claims against the only defendant in the case, which was not itself a national bank. In the absence of such field preemption, there was no basis for federal jurisdiction and the case was remanded.

Similarly, Judge Daniel of the District of Colorado relied on *Long* to find that the National Bank Act did not preempt the field so as to establish federal jurisdiction over a state government's claim against ACE for making a loan in violation of state usury law. *Colorado v. ACE Cash Express, Inc.*, 188 F. Supp. 2d 1282 (D. Colo. 2002). Like the plaintiff in *Long*, the State of Colorado asserted claims against ACE only for violations of state usury law. 188 F. Supp. 2d at 1285. ACE removed the action to federal court, arguing that its agency

relationship with Goleta brought the state's claims within the National Bank Act. Applying the familiar well-pleaded complaint rule, Judge Daniel found that field preemption did not apply and that the case presented no claim arising under federal law. Accordingly, he remanded the action to state court.

The central issue in *Long* and *Colorado* was whether federal field preemption applied to a claim against a non-bank for making loans in violation of state law when the non-bank alleges in response that the loans were issued through a national bank. Both courts applied the general principles of field preemption set forth in such cases as *Caterpillar Inc. v. Williams*, 482 U.S. 386, 393-94 (1987) (claims for breach of individual employment contracts did not arise under federal law so as to support removal, though federal labor law might provide preemption defense on the merits), *Metropolitan Life Ins. Co. v. Taylor*, 481 U.S. 58, 62-63 (1987) (state law contract and tort claims were completely pre-empted by ERISA and removable to federal court), and *Franchise Tax Bd. of Cal. v. Construction Laborers Vacation Trust for Southern Cal.*, 463 U.S. 1, 24-26 (1983) (state law action to levy tax liability against trustees of employee benefit plan did not arise under federal law and was not removable, though federal law might provide preemption defense on the merits). Both the *Long* and *Colorado* cases found that the National Bank Act did not preempt the field so as to establish federal jurisdiction. But both courts took care not to address the issue

before this court, which is whether the National Bank Act provided a complete defense to the state law claims on the merits.

The pleadings – including documents referenced in the complaint – show that Goleta made the loan to Hudson and then sold a participation interest to ACE. Under 12 U.S.C. § 85, that fact is dispositive. Hudson's complaint fails to state any claim upon which relief can be granted. Accordingly, her complaint asserting claims under Indiana usury law, the federal Truth In Lending Act, and the federal Racketeer Influenced and Corrupt Organizations Act must be dismissed. As with virtually any Rule 12(b)(6) motion, however, Hudson is entitled to an opportunity to amend her complaint, consistent with Fed. R. Civ. P. 11.

Conclusion

Defendants' motion to dismiss under Fed. R. Civ. P. 12(b)(6) for failure to state a claim is granted. Plaintiff's motion to strike defendants' motion is denied. Plaintiff may file an amended complaint no later than June 25, 2002, and if she does not do so, the court will then enter a final judgment of dismissal.

So ordered.

Date: May 30, 2002

DAVID F. HAMILTON, JUDGE
United States District Court
Southern District of Indiana

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