

California Federal District Court Adopts Predominant Economic Interest Test in True Lender Case

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On August 31, 2016, in *Consumer Financial Protection Bureau v. CashCall, Inc.*, the U.S. District Court for the Central District of California adopted the "predominant economic interest" test for determining "the true lender" in a case involving a tribal model of installment lending. Participants in the bank partnership space should also pay attention to the decision, as use of this particular test makes it more likely that a court will strike down a bank partnership. The relevant language from the opinion follows:

In identifying the true or de facto lender, courts generally consider the totality of the circumstances and apply a "predominant economic interest," which examines which party or entity has the predominant economic interest in the transaction. See *CashCall, Inc. v. Morrissey*, 2014 WL 2404300, at *14 (W.D. Va. May 30, 2014) (affirming the lower court's application of the "predominant economic interest" test to determine the true lender, which examines which party has the predominant economic interest in the loans); *People ex rel. Spitzer v. Cty. Bank of Rehoboth Beach, Del.*, 846 N.Y.S.2d 436, 439 (N.Y. App. Div. 2007) ("Thus, an examination of the totality of the circumstances surrounding this type of business association must be used to determine who is the 'true lender,' with the key factor being 'who had the predominant economic interest' in the transactions."); cf. Ga. Code Ann. § 16-17-2(b)(4) ("A purported agent shall be considered a de facto lender if the entire circumstances of the transaction show that the purported agent holds, acquires, or maintains a predominant economic interest in the revenues generated by the loan.") The key and most determinative factor is whether Western Sky placed its own money at risk at any time during the transactions, or whether the entire monetary burden and risk of the loan program was borne by CashCall. See, e.g., *Eastern*, 381 F.3d at 957 ("[T]he touchstone for decision here is whether licensed or unlicensed parties were placing their own money at risk at any time during the transactions."); *Morrissey*, 2014 WL 2404300 at *7 (in reaching its conclusion that CashCall was the true or de facto lender, the lower court found that "numerous provisions of CashCall's agreements with FB & T placed the entire monetary burden and risk of the loan program on CashCall, and not on FB & T."). Indeed, as the Ninth Circuit stated in *Eastern*, "a lender is one who puts money at risk." *Eastern*, 381 F.3d at 957.

Based on the totality of the circumstances, the Court concludes that CashCall, not

Western Sky, was the true lender. CashCall, and not Western Sky, placed its money at risk. It is undisputed that CashCall deposited enough money into a reserve account to fund two days of loans, calculated on the previous month's daily average and that Western Sky used this money to fund consumer loans. It is also undisputed CashCall purchased all of Western Sky's loans, and in fact paid Western Sky more for each loan than the amount actually financed by Western Sky.

Moreover, CashCall guaranteed Western Sky a minimum payment of \$100,000 per month, as well as a \$10,000 monthly administrative fee. Although CashCall waited a minimum of three days after the funding of each loan before purchasing it, it is undisputed that CashCall purchased each and every loan before any payments on the loan had been made. CashCall assumed all economic risks and benefits of the loans immediately upon assignment. CashCall bore the risk of default as well as the regulatory risk. Indeed, CashCall agreed to "fully indemnify Western Sky Financial for all costs arising or resulting from any and all civil, criminal or administrative claims or actions, including but not limited to fines, costs, assessments and/or penalties . . . [and] all reasonable attorneys fees and legal costs associated with a defense of such claim or action."

Accordingly, the Court concludes that the entire monetary burden and risk of the loan program was placed on CashCall, such that CashCall, and not Western Sky, had the predominant economic interest in the loans and was the "true lender" and real party in interest. The Court will now apply the principles set forth in Restatement § 187(2), in light of the Court's determination of the real parties in interest to the loan agreement, *i.e.*, CashCall and the borrower.

The court cites the *CashCall, Inc. v. Morrissey* case as a "Western District of West Virginia" federal case. It is actually a West Virginia Supreme Court case.

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