IN THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

No. 12-2617

DEBORAH JACKSON, *et al.*
Plaintiffs-Appellants,

v.

PAYDAY FINANCIAL LLC, *et al.*,
Defendants-Appellees.

On Appeal from the United States District Court
for the Northern District of Illinois
No. 1:11-cv-09288

BRIEF FOR THE FEDERAL TRADE COMMISSION AS AMICUS CURIAE

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The Federal Trade Commission ("FTC" or "Commission") submits this brief in response to the Court's invitation of May 10, 2013. In it, we seek to assist the Court in understanding the grounds for the FTC's law enforcement action against payday lenders who are also defendants in this case, and we suggest ways in which the arguments that the FTC is making in that action may inform the Court's analysis in this case.

The FTC is the federal agency with principal responsibility for the protection of consumers from unfair and deceptive trade practices. The Commission enforces Section 5 of the Federal Trade Commission Act ("FTC Act"), 15 U.S.C. § 45,[1] which prohibits unfair or deceptive acts or practices as to most entities engaged in commercial activities, including nonbank financial companies. The Commission also enforces a variety of other statutes and regulations that address specific consumer credit practices.[2] The Commission has filed numerous law enforcement actions

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[1] Section 5 of the FTC Act prohibits, *inter alia*, "unfair or deceptive acts or practices in or affecting commerce." 15 U.S.C § 45(a).

[2] *See*, *e.g.*, the Truth in Lending Act, 15 U.S.C. §§ 1601-1666j (requiring disclosures and establishing other requirements in connection with

against payday lenders for practices that violate these laws and harm consumers.

STATEMENT

As the Court is aware, the Commission has sued these same defendants in parallel litigation under the FTC Act. As discussed below, the claims in that pending litigation are relevant to (while distinct from) the arbitrability issues presented in this appeal, and we thus describe them in some detail. We begin by summarizing the procedural posture of the FTC's suit.

In September 2011, the Commission filed a lawsuit in federal district court in South Dakota against Payday Financial LLC, its owner and operator, Martin A. Webb, and other related businesses to stop certain of their lending and collection practices, which target financially-distressed consumers seeking short-term, high-interest payday loans. As initially filed, the Commission's complaint focused on

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consumer credit transactions); the Fair Debt Collection Practices Act. 15 U.S.C. §§ 1692-1692o (prohibiting abusive, deceptive, and unfair debt collection practices by third-party debt collectors); the Credit Practices Rule, 16 C.F.R. § 444 (among other things, prohibiting creditors from using certain contract provisions deemed to be unfair to consumers).

garnishment and other collection practices. The complaint alleged that the defendants engaged in unfair and deceptive practices in violation of Section 5 of the FTC Act by (1) misrepresenting to employers that they are legally authorized to garnish borrowers' wages, without first obtaining a court order; (2) falsely representing to employers that they have notified borrowers about the pending garnishment and have given them an opportunity to dispute the debt; and (3) disclosing the existence and the amounts of borrowers' supposed debts to employers and co-workers. The complaint also alleged that the defendants violated the FTC's Credit Practices Rule, 16 C.F.R. § 444, by requiring borrowers to consent, as a term of the loan contracts, to have wages taken directly out of their paychecks in the event of a default; and violated the Electronic Funds Transfer Act, 15 U.S.C. §§ 1693-1693r, and its implementing Regulation E, 12 C.F.R. § 205.10, by requiring borrowers to authorize electronic payments from their bank accounts as a condition of obtaining payday loans. *See* FTC Complaint (Doc. 1 in Case No. 3:11-cv-03017-RAL (D.S.D.)).

In March 2012, the Commission filed an amended complaint, which added claims more directly relevant to the issues before this

Court. Following the filing of the initial complaint, the Commission learned that the defendants have been invoking forum selection clauses in their loan contracts to file collection actions against borrowers in the Cheyenne River Sioux Tribal Court ("Tribal Court") on the Cheyenne River Sioux Reservation ("Reservation") in South Dakota. The amended complaint alleges that, in their loan contracts, the defendants have violated the FTC Act's prohibition on deceptive practices by misrepresenting that the Tribal Court can legitimately adjudicate such suits and issue valid judgments. The amended complaint also alleges that the defendants' practice of suing borrowers in a distant court that lacks jurisdiction is an unfair practice prohibited by Section 5 of the FTC Act. *See* FTC Amended Complaint at 20-21(Doc. 44 in Case No. 3:11-cv-03017-RAL (D.S.D.)).

The defendants moved for partial summary judgment on whether the Tribal Court has subject matter jurisdiction over their collection actions against borrowers. Significantly, the defendants do not lend either to tribe members or to residents of South Dakota, and thus all borrowers are non-members of the tribe and reside outside of South Dakota. The defendants nonetheless argued that jurisdiction exists

because, under *Montana v. United States*, 450 U.S. 544, 565 (1981), the tribe has the authority to regulate "the activities of nonmembers who enter consensual relationships with the tribe or its members, through commercial dealing [or] contracts." The district court denied the defendants' motion because (1) the record did not establish that the defendants are "members" of the Cheyenne River Sioux Tribe ("Tribe"); and (2) inconsistent language in the loan contracts specifying both exclusive tribal court jurisdiction and exclusive alternative dispute resolution created ambiguity regarding what borrowers had consented to. *See FTC v. Payday Fin., LLC*, No. 3:11-cv-03017-RAL, 2013 WL 1309437 (D.S.D. March 28, 2013). The Commission also moved for summary judgment, including on the claims relevant here. The district court has not yet decided that motion.

This appeal involves a question not presented in the FTC's case: whether, pursuant to an arbitration provision in the loan contract, the defendants can require that borrowers' claims against them be resolved by arbitration on the Reservation conducted by representatives of the Tribe (hereinafter, "tribal arbitration"). The court below granted the defendants' motion to dismiss this putative class action by Illinois

consumers, ruling that the plaintiffs had not identified any basis for invalidating the contract's forum selection clause specifying tribal arbitration of disputes. *See* Memorandum Opinion of July 9, 2012 ("Mem. Op.") (Doc. 65 in the case below).

After briefing and oral argument by the parties, this Court invited amicus submissions by the Commission and the State of Illinois, expressing a particular interest in prospective amicus's view on the validity of the arbitration clause in the defendants' loan contracts. Shortly thereafter, the Court remanded to the district court for findings of fact on two questions: (1) whether the applicable tribal law is readily available to the public and, if so, under what conditions; and (2) whether the arbitrator or method of arbitration required under the contract is actually available. The Court's remand order stated that if the FTC and Illinois filed amicus briefs, they could later submit a letter or memorandum stating their position on the district court's findings, once issued. The FTC and the State of Illinois asked instead to defer the filing of an amicus brief until after the district court issued its findings, and the Court granted these motions.

On August 29, 2013, the district court transmitted its findings of fact to this Court. The district court answered the first question in the affirmative, finding that the law of the Tribe "can be acquired by reasonable means," although the plaintiffs were able to secure a copy only after numerous failed attempts and at a greater cost than the cost to the defendants. District Court's Response to Court of Appeals Remand for Findings of Fact at 2 ("Dist. Ct. Findings") (Doc. 95 in the case below). But the district court answered the second question, regarding the availability of tribal arbitration, with "a resounding no." *Id.* at 6. Based on its review of the sole tribal arbitration of a borrower's claim and recent findings of a New Hampshire Banking Department investigation, the court found that there is no "methodized" tribal arbitration process, and the defendants' "promise of a meaningful and fairly conducted arbitration is a sham and an illusion." *Id.* at 4, 6.

DISCUSSION

Although the FTC's challenge to defendants' practices in connection with their lawsuits against borrowers in Tribal Court does not pose the precise question presented by this case, the issues presented in the two cases are related. In particular, the aspects of the

defendants' conduct that the FTC challenges as unfair and deceptive under the FTC Act are relevant to whether the arbitration provision in the defendants' loan contracts is unconscionable and, thus, unenforceable. In Sections I and II below, we explain the basis for the FTC's claims of deception and unfairness in the parallel litigation. We then turn in Section III to how those claims bear on the unconscionability issue presented in this case.

I. In Its Separate Litigation, the FTC Maintains that the Defendants Falsely Represent to Consumers that the Tribal Court Has Jurisdiction to Adjudicate the Defendants' Collection Actions.

In its enforcement action, the FTC contends that the defendants' representations in their loan contracts—that they can sue consumers in Tribal Court and thereby obtain valid orders to garnish consumers' wages—are false. Among other things, the contracts purport to be "subject solely to the exclusive laws and jurisdiction of the Cheyenne River Sioux Tribe"; require borrowers' "consent to the sole subject matter and personal jurisdiction of the Cheyenne River Sioux Tribal Court"; and state that "the sole jurisdiction of the Cheyenne River Sioux Tribal Court" will apply to "this Agreement and the potential garnishment of wages." *See* FTC Amended Complaint at 14; Appellants'

Opening Brief at 9. The defendants' loan contracts also state that the "transaction involve[es] the Indian Commerce Clause of the Constitution of the United States of America"; that the loan contract "is governed by the Indian Commerce Clause of the United States of America and the laws of the Cheyenne River Sioux Tribe"; and that the lender is "organized under and authorized by the laws of Cheyenne River Sioux Tribe and Indian Commerce Clause."[3] [Cite.]

Invoking these contract provisions, the defendants have filed at least 1,123 collection actions in Tribal Court against borrowers who have purportedly defaulted. The defendants have obtained sixty-one default judgments; only two consumers have appeared to defend the lawsuits.[4]

In the FTC Act litigation, the Commission maintains that the defendants have misled consumers about their legal rights, and have

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[3] There is some variation in the wording of the defendants' loan contracts, but they all contain similar language invoking the Indian Commerce Clause and the authority of the Tribal Court.

[4] *See* Payday Financial's Responses to Plaintiff's Second Interrogatories at 3-4, attached as Ex. 11-F to Declaration of Victoria M.L. Budich in Support of Plaintiff's Motion for Summary Judgment (Doc. 99-2 in Case No. 3:11-cv-03017-RAL (D.S.D.)).

thus engaged in deceptive practices, by misrepresenting that the Tribal Court has jurisdiction over their collection lawsuits. While tribes have authority over their own members, "exercise of tribal power beyond what is necessary to protect tribal self-government or to control internal relations is inconsistent with the dependent status of the tribes, and so cannot survive without express congressional delegation." *Montana,* 450 U.S. at 564 (citations omitted). Generally, therefore, "the inherent sovereign powers of an Indian tribe do not extend to the activities of nonmembers of the tribe," *id.* at 565, and "efforts by a tribe to regulate nonmembers . . . are 'presumptively invalid.'" *Plains Commerce Bank v. Long Family Land & Cattle Co.*, 554 U.S. 316, 330 (2008) (quoting *Atkinson Trading Co. v. Shirley*, 532 U.S. 645, 659 (2001)).

This rule applies equally to a tribe's adjudicatory authority. *See Strate v. A-1 Contractors,* 520 U.S. 438, 453 (1997) ("[a]s to nonmembers, . . . a tribe's adjudicative jurisdiction does not exceed its legislative jurisdiction"). Indeed, the Supreme Court has demonstrated its concern that tribal courts not require "defendants who are not tribal members" to "defend [themselves against ordinary claims] in an unfamiliar court." *Id.* at 441-42, 459; *see also Smith v. Salish Kootenai*

College, 434 F.3d 1127, 1132 (9th Cir. 2006) (*en banc*) ("where the nonmembers are *defendants*, the Court has thus far held that the tribes lack jurisdiction, irrespective of whether the claims arose on Indian lands") (emphasis in original).

The Supreme Court has recognized two limited exceptions to this general rule,[5] the first of which the defendants argue applies here: "[a] tribe may regulate . . . the activities of nonmembers who enter into consensual relationships with the tribe or its members, through commercial dealings, contracts, leases, or other arrangements." *Montana*, 450 U.S. at 565.[6] As the Supreme Court has explained, "*Montana* and its progeny permit tribal regulation of *nonmember conduct inside the reservation* that *implicates the tribe's sovereign interests*." *Plains Commerce Bank v. Long Family Land & Cattle Co.*,

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[5] "These exceptions are 'limited' ones, and cannot be construed in a manner that would 'swallow the rule.'" *Plains Commerce Bank v. Long Family Land & Cattle Co.*, 554 U.S. 316, 330 (2008) (quoting *Atkinson Trading*, 532 U.S. at 647, 655).

[6] The second exception applies to "the conduct of non-Indians on fee lands within [the] reservation when that conduct threatens or has some direct effect on the political integrity, the economic security, or the health or welfare of the tribe." *Montana*, 450 U.S. at 565-66. Defendants have made no argument that the second exception applies in either this or the FTC's case.

554 U.S. 316, 332 (2008) (emphasis added); *see id.* ("*Montana* expressly limits its first exception to the 'activities of nonmembers,' . . . allowing these to be regulated to the extent necessary 'to protect tribal self-government [and] to control internal relations'").

In the parallel litigation, the FTC contends that the loan transactions at issue here meet none of these conditions for the exercise of tribal authority over nonmembers. The defendants cannot overcome these deficiencies and create subject matter jurisdiction merely by having consumers sign contracts consenting to jurisdiction by the tribal court. *See Stock West, Inc. v. Confederated Tribes of the Colville Reservation*, 873 F.2d 1221, 1228-29 (9th Cir. 1989) ("a party cannot waive by consent or contract a court's lack of *subject matter* jurisdiction," and "even if the consent of [the party] was adequate to confer personal jurisdiction onto the tribal court, the question of whether the tribal court has subject matter jurisdiction over the case would still not be resolved") (emphasis in original).

Under *Montana*'s consensual commercial relationship exception, the relationship must be between the nonmember and "the tribe or its members." *Montana*, 450 U.S. at 565. But the lending companies here

are not tribal entities: "the Tribe maintains no role or relationship in the ownership or operation" of them. Mem. Op. at 2; s*ee FTC v. Payday Fin.*, 2013 WL 1309437 at *12 ("the settled facts establish that each lending company is a limited liability company organized under South Dakota law and thus apparently not 'organized under . . . the laws of the Cheyenne River Sioux Tribe' as the contracts purport");[7] *id.* at *8 (though the lending companies are owned by a tribe member, they are "a distinct entity from their owner Webb"); *Colorado v. Western Sky Fin., LLC,* No. 11-638, slip op. at 11 (Colo. Dist. Ct. Denver Cty. Apr. 17, 2012) (*Western Sky II*) (Western Sky Financial is "a non-tribal corporation").[8]

As the Ninth Circuit, sitting *en banc*, explained in *Smith v. Salish Kootenai College*, "not every enterprise that is owned or staffed by

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[7] The district court in the FTC's case questioned the significance of a business license conferred by the Tribe on the lending companies. *FTC v. Payday Fin.*, 2013 WL 1309437 at *8. But the defendants later conceded that these business licenses "do not endow them with tribal membership." Defendants' Response to the FTC's Notice of Supplemental Authority at 1 (Doc. 122 in Case 3:11-cv-03017-RAL (D.S.D.)).

[8] The court's decision in *Western Sky II* is attached as Ex. 1 to the FTC's Opposition to Defendants' Motion for Partial Summary Judgment (Doc. 58-1 in Case 3:11-cv-03017-RAL (D.S.D.)).

members of a tribe may be considered a tribal entity for purposes of jurisdiction." 434 F.3d at 1133. Instead, the identification of an organization as "tribal" (or not) turns on factors such as whether it was "created and controlled by" the tribe, whether the tribe selects the organization's management, and whether the organization "act[s] as more than a mere business" (*e.g.*, where it is "designed to further the economic interests of the tribe" or "to manage [its] energy resources"). *Id.* at 1133-34 (citing analogous cases from other circuits). Applying these factors, the court in *Smith* held that a community college on the reservation was a "tribe member" because, among other things, it was created by the tribe, was incorporated under tribal law as a "tribal corporation," and the tribe continued to exercise control over its operations, including through the tribal council's power to appoint and remove board members. *Id.* at 1134. None of these indicia of tribe "membership" exists as to the lending companies in this case. *See also Christian Children's Fund, Inc. v. Crow Creek Sioux Tribal Court*, 103 F. Supp. 2d 1161, 1162, 1166 (D.S.D. 2000) (finding that a reservation-based South Dakota non-profit corporation serving the Indian

community was not a tribal entity where the tribe did not organize or incorporate it and did not manage or direct its activities).

Furthermore, *Montana* requires nonmember conduct "inside the reservation." *Plains Commerce Bank*, 554 U.S. at 332; *see id*. at 334 ("our *Montana* cases have always concerned nonmember conduct on the land"). Here, however, the defendants market payday loans exclusively to consumers outside of the Reservation (indeed, outside of South Dakota entirely). And borrowers' activities in applying for, executing, and repaying their payday loans take place entirely off the Reservation. Other courts have found that this amounts to off-reservation commercial activity:

> [D]efendants were operating via the Internet. . . . The borrowers do not go to the reservation in South Dakota to apply for, negotiate or enter into loans. They apply for loans in Colorado by accessing defendants' website. They repay the loans and pay the financing charges from Colorado; Western Sky is authorized to withdraw the funds electronically from their bank accounts. . . . [T]his is not a case about commercial activity on Indian lands.

Colorado v. Western Sky Fin., LLC, 845 F. Supp. 2d 1178 (D. Colo. 2011) (*Western Sky I*) (remanding case to state court for lack of a federal

question); *Western Sky II, supra*, slip op. at 11 (the defendants' payday lending activities "implicate neither tribes nor on-reservation activity"); *Suthers v. Cash Advance*, 205 P.3d 389, 400-01 (Colo. App. 2008) (holding that a payday lending business that engaged in transactions over the Internet with consumers located off the reservation constituted off-reservation activity), *aff'd*, 242 P.3d 1099 (Colo. 2010).[9]

As noted above, the court in the FTC's case denied summary judgment for the defendants on the issue of tribal court jurisdiction. Although the court did not view borrowers' lack of physical presence on the Reservation to be dispositive,[10] it found other problems with

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[9] *Cf. Missouri ex rel. Nixon v. Coeur D'Alene Tribe,* 164 F.3d 1102, 1109 n.5 (8th Cir. 1999) (citing *AT&T Corp. v. Coeur D'Alene Tribe,* 45 F.Supp.2d 995, 999-1000 (D. Idaho 1998), *rev'd on other grounds,* 295 F.3d 899 (9th Cir. 2002)) ("[the] Tribe's lottery is not on Indian lands when the wager is placed by telephone from off the reservation").

[10] The court was concerned that "treating the nonmember's physical presence as determinative ignores the realities of our modern world that a defendant, through the internet or phone, can conduct business on the reservation and can affect the Tribe and its members without physically entering the reservation." *FTC v. Payday Fin.*, 2013 WL 1309437 at *11. The court indicated that the jurisdictional analysis should take into account borrowers' conduct "directed toward the Reservation," including receiving funds from a reservation-based business; and the place of contract formation (where the last act necessary to complete the contract occurs), which it noted "appears to be" the Reservation because that is where the lending companies make

defendants' claim that borrowers had consented to Tribal Court jurisdiction by entering into these loan agreements. The court pointed to the defendants' false claims about the applicability of the "Indian Commerce Clause,"[11] which in actuality "is a grant of Constitutional authority to Congress, and not to any private entity or tribe." *FTC v. Payday Fin.*, 2013 WL 1309437, at *12. The court also noted that, contrary to what the typical loan contract purports, the lending companies are not "organized under . . . the laws of the Cheyenne River Sioux Tribe," but instead are South Dakota companies. *Id.* at *8, *12. Additionally, borrowers were likely confused by "inconsistencies in the language of the lending agreement . . . specifying both exclusive tribal court jurisdiction and exclusive dispute resolution through separate arbitration without reconciling those provisions." *Id.* at *14.

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the decision to approve the loan. *Id.* at *10. Contrary to what the court surmised, however, the last act of contract formation is the borrower's execution of the loan agreement—which takes place *after* the defendants notify the borrower that her loan application has been approved, and *off* the Reservation.

[11] U.S. Const. art. I, § 8, cl. 3 ("The Congress shall have the Power To . . . regulate Commerce . . . with the Indian Tribes.")

In short, the FTC maintains, there is no basis for the defendants' claims that the Tribal Court has authority over nonmember borrowers of these payday loans. Borrowers have not entered into agreements with tribal entities, they have not engaged in conduct inside the Reservation, and their supposed consent to Tribal Court jurisdiction is undermined by defendants' deceptive and confusing contract language.

II. In Its Separate Litigation, the FTC Also Maintains that the Defendants' Conduct in Suing Consumers in a Tribal Court that Lacks Jurisdiction Is a Prohibited Unfair Practice.

In the parallel litigation, the FTC also alleges that the defendants' practice of subjecting consumers—through the purported authority of the contract provisions discussed above—to lawsuits in a Tribal Court that lacks jurisdiction is an unfair practice under the FTC Act: it "causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers themselves and not outweighed by countervailing benefits to consumers or to competition." 15 U.S.C. § 45(n); *see FTC v. Accusearch, Inc.*, 570 F.3d 1187, 1193 (10th Cir. 2009); *Orkin Exterminating Co., Inc. v. FTC*, 849 F.2d 1354, 1364-65 (11th Cir. 1988). This standard recognizes that well-informed consumers generally are capable of making choices for themselves. However, practices may

be unfair if they unreasonably create or take advantage of an obstacle to consumers' ability to make informed choices, and if they cause, or are likely to cause, consumer injury.[12] That is the precisely the case here, as the FTC has argued in its separate litigation.

The defendants' practice of filing, or threatening to file, collection actions in a Tribal Court that lacks jurisdiction causes substantial injury to consumers.[13] The Tribal Court is necessarily a distant one for these consumers, who (given their precarious financial circumstances)

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[12] The Commission has long taken this approach to unfairness under Section 5. *See* Letter from the FTC to Hon. Wendell Ford and Hon. John Danforth, Committee on Commerce, Science and Transportation, United States Senate, Commission Statement of Policy on the Scope of Consumer Unfairness Jurisdiction (December 17, 1980), reprinted in *In re Int'l Harvester Co.*, 104 F.T.C. 949, 1070, 1073 (1984) ("Unfairness Policy Statement"). Subsequently, Congress codified this standard by adding subsection 5(n), 15 U.S.C. § 45(n).

[13] Injury is sufficiently substantial if it causes a small harm to a large class of people, *FTC v. J.K. Publ'ns*, 99 F. Supp. 2d 1176, 1201 (C.D. Cal. 2000), or severe harm to a limited number of people. *In re Int'l Harvester*, 104 F.T.C. at 1064. Injury also may include non-monetary or indirect monetary harm. *FTC v. Neovi, Inc.,* 604 F.3d 1150 (9th Cir. 2010) (defendants harmed consumers by creating a software program that allowed others to write fraudulent checks); *Accusearch, Inc.*, 570 F.3d at 1193 (substantial injury element met by subversion of consumer privacy).

are unlikely to have the means to appear and defend themselves.[14] Not only is this forum geographically distant, but consumers may also have difficulty obtaining the Tribal Court's substantive or procedural laws.[15] Perhaps most importantly, the defendants' practice of subjecting consumers to collection actions in this remote and unfamiliar court

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[14] The defendants assert that borrowers can appear telephonically. But, even assuming that the rules of the Tribal Court allow this (and assuming further that such mode of participation would suffice to protect borrowers' interests), there is no mention of telephonic participation in the summons served upon borrowers notifying them of the defendants' suit and ordering them to appear at a hearing in Tribal Court.

[15] Following plaintiffs' claims that they had difficulty finding copies of the relevant tribal law, this Court remanded for the limited purpose of resolving this factual issue and one other. On remand, the court below found that tribal law "can be acquired by reasonable means," because both plaintiffs and defendant were ultimately able to obtain copies of the Tribal Code. District Court's Response to Court of Appeals Remand for Findings of Fact at 2 (Doc. 95). The court noted, however, that the plaintiffs were able to secure a copy of the Tribal Code only after numerous failed attempts and at a greater cost than the cost to the defendants. These findings do not address whether the Tribal Court's procedural rules, presumably governing the collection lawsuits initiated there by the defendants, are readily available to consumers. Furthermore, the district court's conclusion about the availability of applicable tribal law is not undisputed. Another district court examining the sole arbitration occurring under the terms the defendants' loan contracts recently found that the Tribe's "consumer dispute rules" referenced in the defendants' loan contracts do not exist. *Inetianbor v. CashCall, Inc.*, __ F. *S*upp. 2d ___, 2013 WL 4494125, at *5-6 (S.D. Fla. Aug. 19, 2013).

likely pressures many consumers into abandoning defenses or counterclaims they could have asserted in a more accessible court of competent jurisdiction. That may help explain why, of the 1,123 consumers sued by the defendants in Tribal Court, only two have appeared to defend the lawsuit. *See Am. Fin. Servs. Ass'n v. FTC*, 767 F.2d 957, 973-75 (D.C. Cir. 1985) (upholding FTC's determination that provisions in consumer credit contracts authorizing deduction of debtor's wages and giving creditor security interest in debtor's household goods are unfair; creditors' use of such provisions substantially harmed consumers, *inter alia*, by pressuring consumers to "forego assertion of valid defenses, set-offs or counterclaims"). Similarly, even before the defendants file a collection suit, the threat of such a lawsuit in the Tribal Court may pressure consumers into settling debts that they could otherwise have disputed.

Consumers also cannot reasonably avoid the injuries that arise from defendants' practice of filing, or threatening to file, collection actions in Tribal Court.[16] The defendants employ boilerplate contract

[16] An injury is "reasonably avoidable" only if consumers "have reason to anticipate the impending harm and the means to avoid it." *Orkin*, 849

provisions that consumers are powerless to modify if they wish to obtain a needed loan. Borrowers do not even see the contract's forum selection and choice of law provisions until late in the loan process,[17] and, even assuming they notice these provisions, are unlikely to understand them, a problem exacerbated by the confusing wording of these contracts. *See FTC v. Payday Fin., LLC*, 2013 WL 1309437, at *14 (describing the contracts' inconsistent and confusing language). And if consumers do not perceive a harm embedded in obscure contractual language, they cannot be said to have a reasonable opportunity to avoid that harm. *See Am. Fin. Servs. Ass'n*, 767 F.2d at 976-77 (injury not reasonably

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F.2d at 1365-66. "[W]hether some consequence is 'reasonably avoidable' depends not just on whether [consumers] know the physical steps to take in order to prevent it, but also whether they understand the necessity of actually taking those steps." *In re Int'l Harvester Co.*, 104 F.T.C. at 1066. "The focus is on 'whether consumers had a free and informed choice that would have enabled them to avoid the unfair practice'." *J.K. Publ'ns*, 99 F. Supp. 2d at 1201; *Orkin*, 849 F. 2d at 1365.

[17] After consumers submit loan applications to the defendants, containing their social security numbers, bank account numbers, and other personal information, the defendants send to approved consumers a loan agreement. By this point, consumers will have supplied the defendants with highly sensitive personal and financial data and would understandably be wary of starting the process anew with another lender.

avoidable, given consumers' "lack of understanding of contractual terms" and inability to bargain over boilerplate contract provisions, and because "default is ordinarily the product of forces beyond a debtor's control").

The defendants' practice of subjecting consumers to collection actions in a distant court that lacks jurisdiction also satisfies the last element of unfairness: it produces no countervailing benefits for consumers or competition. *See J.K. Publ'ns*, 99 F. Supp. 2d at 1201 (third prong of unfairness test is met "when a practice produces clear adverse consequences for consumers that are not accompanied by an increase in services or benefits to consumers or by benefits to competition"). In the FTC's litigation, the defendants have not identified any such benefits that might justify this practice notwithstanding the adverse consequences for consumers. Indeed, there is no legitimate benefit to suing consumers in a court that lacks jurisdiction.

III. The Defendants' Practice of Requiring Tribal Arbitration of Disputes Also May Be Deemed Unfair and Unconscionable.

Under the Federal Arbitration Act ("FAA"), arbitration agreements "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. This provision "permits agreements to arbitrate to be invalidated by generally applicable contract defenses, such as fraud, duress, or unconscionability," provided those defenses do not "apply only to arbitration or . . . derive their meaning from the fact that an agreement to arbitrate is at issue." *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 1746 (2011) (internal quotation marks omitted).

Whether the defendants can require arbitration of claims initiated by consumers is not directly at issue in the FTC's case. But unfairness under the FTC Act resembles the "generally applicable contract defense" (*id.*) of unconscionability. Accordingly, the factors that make it unfair for the defendants to induce consumers into tribal court to defend collection actions are also relevant to whether the arbitration

clause in the loan contracts requiring tribal arbitration of consumer claims is unconscionable.[18]

Unconscionability may be procedural or substantive:

> Procedural unconscionability consists of some impropriety during the process of forming the contract depriving a party of meaningful choice. * * * Factors to be considered in determining whether an agreement is procedurally unconscionable include whether each party had the opportunity to understand the terms of the contract, whether important terms were hidden in a maze of fine print, and all of the circumstances surrounding the formation of the contract. * * * Substantive unconscionability concerns the actual terms of the contract and examines the relative fairness of the obligations assumed, asking whether the terms are so one-sided as to oppress or unfairly surprise an innocent party.

Phoenix Ins. Co. v. Rosen, 242 Ill.2d 48, 60, 949 N.E.2d 639, 647 (2011) (internal quotation marks and citations omitted).[19] Here, several factors

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[18] The key issues at play here, regarding the burdens consumers would face in dealing with a distant tribal forum, arguably apply regardless of whether the forum is the Tribal Court or tribal arbitration. To the extent that plaintiffs' unconscionability arguments rely on such considerations—as opposed to problems with the arbitral forum as such—those arguments do not "derive their meaning from the fact that an agreement to arbitrate is at issue," *Concepcion*, 131 S. Ct. at 1746, and therefore are not precluded by the FAA.

[19] Illinois law, which these Illinois-based plaintiffs invoke, is consistent

in combination may well support a conclusion that the arbitration provisions in the defendants' loan contracts are both procedurally and substantively unconscionable.

As already discussed, several features of these contractual relationships impede consumers' ability to exercise any meaningful choice in agreeing to the forum selection and choice-of-law provisions in the defendants' loan contracts—suggesting procedural unconscionability. To begin with, financially-distressed consumers of these payday loans have no ability to modify the defendants' boilerplate contract provisions and still obtain a needed loan. *See Williams v. Illinois State Scholarship Comm'n*, 139 Ill.2d 24, 72, 563 N.E.2d 465,

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with general principles of unconscionability. *See* UNIFORM COMMERCIAL CODE § 2-302 cmt. 1 (2003) ("The basic test is whether, in the light of the general commercial background and the commercial needs of the particular trade or case, the clauses involved are so one-sided as to be unconscionable under the circumstances existing at the time of the making of the contract. . . . The principle is one of the prevention of oppression and unfair surprise. . . ."); RESTATEMENT (SECOND) OF CONTRACTS § 208 cmt. a (1981) ("[r]elevant factors include weaknesses in the contracting process like those involved in more specific rules as to contractual capacity, fraud, and other invalidating causes"). The defendants' loan contracts specify application of tribal law, but tribal law is inappropriately invoked here for the reasons discussed in Section I above, and in any event the parties have not articulated what tribal law might be on this issue.

487 (1990) ("A contractual clause that is part of a 'boilerplate' agreement . . . has its significance greatly reduced because of the inequality in the parties' bargaining power."). Consumers do not receive the contract language until after they apply for the loans and learn that their loans have been approved.[20] The inconsistent language in the loan contracts, specifying both exclusive Tribal Court jurisdiction and exclusive tribal arbitration without reconciling those provisions, also makes it difficult for borrowers to understand exactly what form of dispute resolution they are agreeing to. *See supra* p. 17. Moreover, the defendants' incorrect representations in their loan contracts regarding the breadth of Tribal Court jurisdiction, combined with their invocation of an irrelevant provision of the Constitution (*see supra* pp. 8-9, 17), may induce consumers to believe, mistakenly, that they have no choice but to accede to resolution of their disputes on the Reservation. *See ChampionsWorld LLC v. U.S. Soccer Federation, Inc.*, 726 F. Supp. 2d 961, 974 (N.D. Ill. 2010) (holding that contracting party's alleged misrepresentations supported plaintiff's allegation of procedural

[20] *See supra* note 17.

unconscionability). Taken together, these factors undermine borrowers' agreement to tribal arbitration.

Grounds also exist for finding that the loan contracts' requirement that consumers submit disputes to tribal arbitration is substantively unfair to consumers. Two district courts have examined the sole instance of arbitration of a claim under these loan contracts and have concluded, for a variety of reasons, that this arbitration provision does not provide consumers with a valid mechanism for resolving disputes.

That arbitration proceeding, which is still pending, was initiated earlier this year after the U.S. District Court for the Southern District of Florida dismissed a borrower's suit and ordered the parties to submit the claims to arbitration pursuant to an arbitration clause identical to the one at issue here. Last month, however, the court vacated that order and reinstated the case, concluding on the basis of new evidence that the arbitration required by the contract is unavailable. *Inetianbor v. Cashcall, Inc.*, __ F. Supp. 2d ___, 2013 WL 4494125, at *6 (S.D. Fla. Aug. 19, 2013). The contract required that all disputes arising from the loan agreement be arbitrated "by the Cheyenne River Sioux Tribal Nation by an authorized representative in accordance with its consumer

dispute rules . . . ." *Id.* at *1. But the court found that the arbitration proceeding conducted on the Reservation did not comply with these terms. For one thing, the arbitrator, Robert Chasing Hawk, was not conducting the arbitration as an "authorized representative" of the Tribe as required by the contract. In fact, there was no evidence that the Tribe even conducts arbitration through authorized representatives. Indeed, Mr. Chasing Hawk acknowledged during the arbitration that he had been selected by the defendants and that the Tribe was uninvolved in this "private business deal." *Id.* at *4. The *Inetianbor* court also found that tribal arbitration was unavailable because the contract required the arbitration to be conducted according to the Tribe's "consumer dispute rules" but no such rules existed. *Id.* at *5-6.[21]

In responding to this Court's limited remand, the district court in the instant case also concluded that arbitration was unavailable. The court found that Mr. Chasing Hawk's lack of training in law or arbitration and his affiliations with the defendants—including the fact that Mr. Chasing Hawk was personally selected by defendant Martin

[21] The unavailability of governing law and rules may also contribute to a finding that the contract is unfair, and therefore unconscionable. *See supra* note 15.

Webb and his daughter works for one of the lending entities—are inconsistent with the role of a disinterested and unbiased arbitrator and with arbitration generally. Dist. Ct. Findings at 3-4.

The district court also pointed to the conclusions of the New Hampshire Banking Department, which issued a Cease and Desist order after finding that defendant Western Sky Financial, LLC, "was nothing more than a front" for Cashcall "to evade licensure by state agencies and exploit Indian Tribal Sovereign Immunity to shield its deceptive practices . . . ." *Id.* at 5. As a result, the New Hampshire Banking Department concluded that the scheme to employ Western Sky in this manner constituted an "unfair or deceptive act or practice . . . ." The court below found this determination persuasive and unrebutted by any of the parties. The district court therefore concluded that the "promise of a meaningful and fairly conducted arbitration is a sham and an illusion." *Id.* at 6.

These findings strongly suggest that the arbitration agreement at issue is substantively unconscionable because the terms of the contract are "so one-sided as to oppress or unfairly surprise an innocent party." *Rosen*, 242 Ill.2d at 60, 949 N.E.2d at 647. The contracts here, under

terms supplied by the defendants, dictate an exclusive mechanism for resolution of consumer disputes that—as the two district courts' findings discussed above demonstrate—is wholly illusory, depriving consumers of a fair opportunity to assert claims and defenses against the defendants.

These concerns are not, as the defendants have suggested, remedied by provisions in at least some of their loan contracts allowing consumers to opt out of arbitration. The defendants have made their position clear that the forum selection provisions in their contract require consumers who opt out of arbitration to assert claims in Tribal Court, a forum that, as discussed above, lacks subject matter jurisdiction over these disputes. Moreover, the remoteness of a tribal forum imposes additional burdens on consumers seeking to vindicate claims that the defendants do not face. For the vast majority of consumers, who can little afford the expense, travel to the Reservation to participate in either arbitral or court proceedings is simply infeasible. *Cf. Williams*, 139 Ill.2d at 72, 563 N.E.2d at 487 (contractual forum selection clause "fixing venue in [a distant forum] in . . . collection suits

effectively deprives [borrowers] of their day in court").[22] Thus, both the arbitration and forum selection clauses in the defendants' loan contracts operate in the same manner: they pressure financially-distressed consumers to abandon legal claims or defenses.

CONCLUSION

This case presents unique circumstances that may warrant invalidating as unconscionable provisions in the defendants' loan contracts requiring tribal arbitration of borrowers' claims. Although the FTC's challenge to defendants' practices inducing consumers into Tribal Court presents distinct issues, the FTC's claims may inform the Court's analysis here, because aspects of the defendants conduct that make it

[22] The defendants do not dispute this, but aver that consumers may participate in arbitration on the Reservation by telephone. But the selection of a forum that makes in-person participation feasible only for the lenders, but not the borrowers, combined with the difficulty of obtaining the law to be applied during such arbitration, might be deemed unfair.

unfair and deceptive under the FTC Act are relevant to an unconscionability inquiry.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

I certify that this brief complies with the type-volume limitation set forth in Fed. R. App. 32 (a)(7)(B), in that it contains 6,709 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii), and complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6), because it has been prepared in a proportionally spaced typeface using Microsoft Word 2010 in Century Schoolbook 14-point font.

s/ Michele Arington
MICHELE ARINGTON

CERTIFICATE OF SERVICE

I hereby certify that on September 13, 2013 I filed and served the foregoing with the Court's appellate CM-ECF system. I certify that all participants in the case are registered CM/ECF users and that service will be accomplished by the CM/ECF system.

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