as an attorney. In addition, she claimed that extreme stress brought about by the massive debt was aggravating her mental condition and health and reducing the effectiveness of her medical treatment. The United States Bankruptcy Court discharged Plaintiff's student loan debts. It found that forcing the Plaintiff to pay off the student loans presented such a stress on the Plaintiff that she suffered an undue hardship, which would be alleviated by discharge of the indebtedness. The United States District Court affirmed. The student loan creditors appealed to the United States Court of Appeals for the Eighth Circuit claiming that there was not an undue hardship under 11 U.S.C. Section 523(a)(8). They claimed that the Plaintiff and her husband earned enough money after subtracting for living expenses to pay off the debt over several years and that the undue hardship exception was not intended to discharge debts because of the effect on the debtor's mental health.

**HOLDING:** Affirmed.

**REASONING:** The court first applied the rule from 11 U.S.C. Section 523(a)(8) that there is no discharge in bankruptcy for educational loans or loans funded or secured by governmental or nonprofit units "unless excepting such debt from discharge… will impose an undue hardship on the debtor." The court determined that the decision to discharge indebtedness as a result of undue hardship is a question of law. Where the evidence shows financial obligations likely to harm health, and in turn affect the debtor's financial outlook, it was ruled proper to take such facts and circumstances into account. The court went on to state that "we will not adopt an interpretation of "undue hardship" that causes the courts to shut their eyes to factors that may lead to disaster, both personal and financial, for a suffering debtor." The court then determined that undue hardship would be determined based on the "totality of the circumstances" test from *In re Long*, 322 F.3d 549, 554 (8th Cir. 2003).

The court will determine, from the "totality of the circumstances," if there is undue hardship based on 1) the debtor's past, present and reasonably reliable future financial resources; 2) calculation of the debtor and dependent's reasonably necessary living expenses; and 3) other relevant facts and circumstances of case. The court determined that the Bankruptcy Court's finding that there was undue hardship was not clearly erroneous. They found that the harmful effect of the debt on Plaintiff's fragile mental health was supported by facts that showed continuing debt would cause Plaintiff to be voluntarily or involuntarily terminated from her employment. Another factor the court found as support was the diagnosis of both the Plaintiff's and Defendant's medical experts that the Plaintiff had major recurrent depression and dysthymia, a depression-type disorder. Finally, the court found additional support from the fact that her mental health has, does, and will continue to hamper her financial situation (past, present and future earnings).

**The court found additional support from the fact that her mental health has, does, and will continue to hamper her financial situation.**

## CONSUMER CREDIT

### TAX-EXEMPT DESIGNATION BY IRS CAN'T SHIELD COMPANY FROM CREDIT REPAIR ACT SUIT

Zimmerman v. Cambridge Credit Counseling Corp., 409 F.3d 473 (1st Cir. 2005).

**FACTS:** Kelly and Andrew Zimmerman ("Consumers") entered into a contract with Cambridge Credit Counseling Corporation ("Cambridge") for credit counseling services. Prior to entering into the contract, the Consumers saw Cambridge advertising that they were a nonprofit organization helping debtors to manage their debt by obtaining lower interest rates, eliminating fees and re-aging debt. Therefore, the Consumers believed that Cambridge would charge lower fees for their services and hired them.

Cambridge is organized as a charitable organization under Massachusetts law. The company has obtained an Internal Revenue Service's ("IRS") determination that it is tax exempt under I.R.S. § 501(c)(3). This section specifies that charitable and educational organizations whose net earnings do not benefit either shareholders or individuals are exempt from federal taxation.

A few months after enrollment with Cambridge, being dissatisfied with their services, the Consumers decided to cancel the contract. Then, they sued Cambridge and other related entities alleging violations of the Credit Repair Organizations Act ("CROA"). The CROA creates a cause of action for consumers harmed by the unscrupulous business and advertising practices on the part of credit repair organizations. 15 U.S.C. § 1679 *et seq.* However, the CROA does not permit lawsuits against any nonprofit organization which is exempt from taxation under section 501(c)(3) of the IRS.

Cambridge moved to dismiss the complaint. The trial court granted the motion on the grounds that Cambridge was excluded from CROA under 15 U.S.C § 1679a(3)(B)(i). Consumers appealed.

**HOLDING**: Vacated and remanded.

**REASONING:** The Consumers contended that the trial court erred in applying the CROA exclusion in this case because Cambridge was not operating as a nonprofit organization. In order to be excluded from the CROA under 15 U.S.C. § 1679a(3)(B)(i), a credit repair organization must actually operate as a nonprofit organization and be exempt from taxation under section 501(c)(3).

The court addressed Cambridge's arguments that a credit repair organization must only have received section 501(c)(3) designation from the IRS to qualify for the exclusion and that the phrase "exempt from taxation under 501(c)(3)" defines "nonprofit organization." The court held that the IRS's classification of the organization as tax-exempt entity was not dispositive of whether organization came within exemption from CROA for tax-exempt nonprofit entities; the entity was required to show that it was

actually operating as nonprofit. The court clarified the standard to be applied in deciding whether an organization meets the "nonprofit" requirement of the exclusion. After an analysis of the statutory language and of Congress's intentions in drafting the statute, the court concluded that "nonprofit" status depended on proof that entity was actually operating as a nonprofit organization and did not distribute profits to shareholders or others. The court stated that this was consistent with the standard definition of the term and determined that it was the standard to be applied. The Consumers argued that Cambridge was not operating as a nonprofit entity, as their executives had received very high salaries, and is therefore subject to the CROA. The court agreed and, accordingly, vacated and remanded the judgment.

### CONSUMER'S STATE LAW CLAIMS ARE NOT PRE-EMPTED BY REGULATIONS PROMULGATED BY THE U.S. OFFICE OF COMPTROLLER OF CURRENCY

Ramon Blanco v. Keybank, ____F.Supp. 2d ___ (D. Ohio 2005).

**FACTS:** Plaintiff Ramon Blanco enrolled in career training program offered by the Academy of Weston, Inc. In order to finance the education, Blanco entered into a Student Enrollment Contract with the Academy that included certain financial terms and disclosures relating to his student loan. Keybank arranged for and offered financing for Blanco's student loan, and Plaintiff executed a promissory note in favor of Keybank. Keybank also provided Blanco with a Truth in Lending Act (TILA) Disclosure Statement describing the amount financed, the interest rate used, and other required disclosures. Keybank received full value for the loans by selling them as part of a pool of loans that ultimately became KeyCorp Student Loan Trust 2002-A. JP Morgan and Bank One, as eligible trustee of the KeyCorp Student Loan Trust 2002-A, currently held the notes executed by Plaintiff. Keybank serviced the loans. At some point after plaintiff executed the promissory note, but before he completed his education, the Academy closed its doors. Plaintiff never received the education for which the loan was intended to pay. The defendants moved to dismiss the Plaintiff's Second Amended Complaint at the District Court Northern District of Ohio. Blanco raised two claims, one under non-compliance with TILA and a second under violation of Ohio's Retail Installment Sales Act (RISA).

**HOLDING**: Denied Summary Judgment (both issues).

**REASONING**: Under the second cause of action, the court addressed whether the plaintiff adequately alleged that the defendants were liable under Ohio's Retail Installment Sales Act (RISA), Ohio Rev. Code Section 1317.032 (C). Section 1371.032 of RISA, a consumer protection statute, allows a consumer to make certain defenses as affirmative claims against the seller of goods or services obtained pursuant to purchase money loan installment note, as well as against the holder of a purchase money loan installment note. The defenses provided by the RISA include: (i) That the subject of the consumer transaction was not furnished or delivered by the seller in accordance with the agreed upon terms of the transaction; and (ii) That the subject of the consumer transaction did not conform to any express or implied warranty made by the seller. Ohio Rev. Code Section 1317.032(A). Section 1317.032 (C) allows the consumer to "assert the cause of action to recover from the holder…of the purchase money loan installment note…the amount of any payments made to the holder, …If [certain conditions apply]." Ohio Rev. Code Section 1317.032 (C).

The plaintiff alleged that KeyBank, as holder of the purchase money loan installment note, was liable for Academy's failure to "furnish or deliver" his training. The plaintiff thus sought to recover from KeyBank the payments he made on the loan. Defendant KeyBank argued (1) that RISA does not apply to financial institutions such as KeyBank, and (2) even if it did, the National Bank Act preempts RISA.

The court reasoned that independent loans from a bank or loan company are generally considered outside the purview of RISA. *Bank One, Dayton, N.A. v. Doughman*, 59 Ohio App.3d 60 (Hamilton County 1988). The language of sections 1317.031 and 1317.032, however, suggest that RISA may cover financial institutions in certain circumstances. Although a transaction between Defendant KeyBank and the plaintiff was not a "consumer transaction" within the meaning of the statute, the specific language of Section 1317.032(C) requires only that a "consumer transaction" has occurred between buyer and seller. That the buyer's defense need only "aris[e] out of the consumer transaction" further broadens the scope of the provision. The court found that the KeyBank loans may have constituted "purchase money loan installment notes," under RISA. Because Plaintiff alleged that Academy cooperated with KeyBank to channel customers to Key on a regular basis, the court found that the loans between Plaintiff Blanco and Key may constitute purchase money installment notes for the purpose of RISA.

The question remained whether the National Bank Act preempts RISA. The parties did not dispute that, of the three types of preemption – so called field preemption, conflict preemption, and express preemption – conflict preemption was the applicable doctrine in the present case. Conflict preemption occurred where the state law is in "irreconcilable conflict" with federal law. *Barnett Bank, N.A. v. Nelson*, 517 U.S. 25, 31 (1996). The Defendants argued that the National Bank Act, 12 U.S.C. Section 24, preempts Plaintiff's RISA claim. That statute gave the national bank the power:

> To exercise…all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidence of debt; by receiving deposits; by buying and selling exchange, coin, and bullion; by loaning money on personal security; and by obtaining issuing, and circulating notes according to the provisions of title 62 of the Revised Statutes.

12 U.S.C. Section 24 (Seventh). Specifically, Defendants claimed that RISA impermissibly interferes with the ability of national banks to negotiate promissory notes, lend money, and collect outstanding loans. The question was one of congressional intent.

In *Abel v. KeyBank*, 313 F. Supp. 2d 720, Judge Gaughn held that these regulations support the conclusion that the National Bank Act preempts RISA. She reasoned:

> In essence, the RISA provisions read into each promissory note (arising from a consumer transaction) a requirement that any holder, including a national bank, assume the liability of the

> seller under certain circumstances. The Court finds that this type of state imposed liability significantly interferes with a national bank's ability to negotiate promissory notes and lend money. As defendants point out, the RISA provision essentially requires national banks to become insurers for sellers vis a vis consumers.

*Id*. at 727. As a decision of a sister court, the *Abell* decision was not binding upon the present court.

*Abell* cited cases involving state laws that were either significantly more burdensome or more directly controlling than in the present case. In the instant case, the state law did not directly control the federal bank activity. While the statute could impose additional liability on national banks, altering the terms of liability did not constitute "obstruct[ing], impair[ing], or condition[ing] a national bank's ability to fully exercise its powers' to negotiate promissory notes. If, as Defendant seemed to urge, the National Bank Act preemption were interpreted to include any action that merely burdens the bank's business operations, it would also make invalid other state and local regulations (such as state laws prohibiting discrimination in lending) that encumber bank's ability to negotiate commercial transactions. Congress did not intend to preempt these laws. Several well-established court decisions hold that the federal bank law does not preempt other state laws that incidentally affect national banks' business transaction. Where, as in this case, a state law has only incidental effect on the operation of a national bank, the National Banking Act does not preempt the applicable state law.

In areas traditionally governed by state law, courts must assume that "the historic police powers of the States were not to be superceded by [federal law] unless that was the clear and manifest purpose of Congress." *Gen. Motors Corp. v. Abrams*, 897, F.2d 34, 41 (2d Cir. 1990) (quoting *Pacific Gas & Elec. Co. v. Energy Resources Conservation & Dev. Comm'n*, 461 U.S. 190, 206 (1983)). Further, "Because consumer protection law is a field traditionally regulated by the states, compelling evidence of an intention to preempt is required…" Indeed, the OCC regulations provided that state laws in the areas of "rights to collect debts" and "acquisition and transfer of property," are valid and not subject to preemption to the extent that they "only incidentally affect the exercise of national bank powers." 69 Fed. Reg. 1904, 1917.

The Plaintiff posited an argument not raised in *Abel*. He argued that the Federal Trade Commission "holder rule" should be used to interpret the preemptive scope of the National Bank Act narrowly. The FTC Holder Rule required sellers to inform buyers to the buyer's right to assert claims and defenses against the holder that the buyer has against the seller. It was designed to ensure that "creditors will be responsible for seller misconduct" because "customers [should not have] to assume all risk of seller misconduct, particularly where creditors who profit from consumer sales have access to superior information combined with means and capacity to deal with seller misconduct…" 40 Fed. Reg. 53524.

The Plaintiff claimed that RISA cannot conflict with federal law because the FTC intended the FTC holder rule to do precisely what RISA also does, that is, to make a holder liable for a seller's misconduct. The court held plaintiff's argument as persuasive. The agency's reference to the availability of state remedies is difficult to reconcile with an approach that precludes such remedies. Although national banks are not directly subject to the FTC's authority, the federal agency's discussion of state remedies for violation of the FTC holder rule suggests that the holder rule was not intended to preempt state regulation.

## ARBITRATION

### A NONPARTY MAY BE COMPELLED TO ARBITRATE IF IT SEEKS, THROUGH THE CLAIM, TO DERIVE A DIRECT BENEFIT FROM THE CONTRACT CONTAINING THE ARBITRATION PROVISIONS

In re Weekley Homes, L.P., 176 S.W.3d 740 (Tex. 2005).

**FACTS:** Vernon Forsting ("Forsting") contracted with Weekley Homes, L.P. ("Weekley") for the construction of a house. His intention in purchase of the home was to live with his only child, Von Bargen, her husband, and their three sons. Von Bargen negotiated directly with Weekley on many issues before and after construction. However, only Forsting executed the various financing and closing documents, including the Real State Purchase Agreement that contained an arbitration clause. Shortly after closing, Forsting transferred the home to a trust whose sole beneficiary was Von Bargen.

After completion, numerous problems arose with the home. After a brief move and while repairs were made to the home, Von Bargen requested and received reimbursement. Unsatisfied with the repairs, Forsting, Von Bargen, and the Turst filed suit against Weekley asserting various claims for breach of contract, negligence, and other causes of action. Von Bargen sued for personal injuries that allegedly resulted from Weekley's negligent repairs.

Weekley moved to compel arbitration of all claims under the Federal Arbitration Act ("FAA"). The trial court refused to compel arbitration of Von Bargen's claim because she did not sign the Purchase Agreement. Accordingly, Weekley sought mandamus relief to compel the trial judge to enforce the arbitration agreement.

**HOLDING:** Writ of mandamus granted.

**REASONING:** The court reasoned that a nonparty may seek to compel arbitration if it deliberately sought and obtained substantial benefits from the contract itself. Not only did Von Bargen resided in the home, she directed how Weekley should construct many of the homes features, demanded repairs, received financial reimbursement for expenses, and conducted settlement negotiations with Weekley. The court reasoned that while Von Bargen never based her personal injury claim on the contract, her prior exercise of other contractual rights and her equitable entitlement to other contractual benefits prevented her from avoiding the arbitration clause here. The court held that since Von Bargen obtained substantial actions from Weekley by demanding compliance with provisions of the contract, she cannot equitably object to the arbitration clause attached to them.