Case No. 09-16703

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

MATTHEW C. KILGORE and WILLIAM BRUCE FULLER,

Plaintiff-Appellants

v.

KEYBANK, NATIONAL ASSOCIATION

and

GREAT LAKES EDUCATION LOAN SERVICES, INC.,

Defendants-Appellees.

BRIEF OF AMICUS CURIAE STATE OF MONTANA TO SUPPORT REVERSAL OF THE JUDGMENT REGARDING FEDERAL PREEMPTION

On Appeal from the United States District Court
for the Northern District Of California
Case No. 3:08-CV-02958-TEH

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES

TABLE OF AUTHORITIES
(Cont.)

TABLE OF AUTHORITIES
(Cont.)

FEDERAL MATERIALS

MONTANA MATERIALS

TABLE OF AUTHORITIES
(Cont.)

OTHER AUTHORITIES

INTEREST OF AMICUS CURIAE

The State of Montana, through the Office of the Attorney General, joined by the undersigned states' Attorneys General, respectfully submits this Amicus Brief pursuant to Fed. R. App. P. 29(a). As Chief Legal Officers of the States, the Attorneys General are responsible for enforcing the State Consumer protection laws, such as the Montana Unfair Trade Practices and Consumer Protection Act. Mont. Code Ann. §§ 30-14-101 (2009), et seq. Montana consumers have suffered similar harm to the Plaintiffs in this action because KeyBank made loans to students who attended Silver State Helicopters flight school locations in several states. Further, the matter at issue in this appeal--federal preemption of state consumer protection laws--directly affects the States' ability to protect their citizens and enforce their laws.

SUMMARY OF THE ARGUMENT

KeyBank argues for a standard of conflict preemption that is more expansive than intended by Congress. KeyBank's proposed standard also presents a significant departure from recent United States Supreme Court decisions limiting the scope of federal preemption. KeyBank urges a wholesale expansion of the preemption doctrine that, if adopted, would

adversely affect the Attorney General's ability to protect Montana consumers and would insulate banks from liability for knowingly aiding and abetting a third party to willfully disregard the law. Because federal preemption jurisprudence has far reaching consequences, this amicus brief addresses this single issue:

> Did the district court erroneously expand federal preemption doctrine by determining that neutral state consumer protection laws that are consistent with federal law are nevertheless preempted by the National Bank Act?

As discussed below, the district court incorrectly held that generally applicable state consumer protection laws are barred by federal preemption under the National Banking Act (NBA).

ARGUMENT

I. THERE IS NO CONFLICT PREEMPTION. GENERALLY APPLICABLE STATE LAWS DO NOT SIGNIFICANTLY INTERFERE WITH THE BUSINESS OF BANKING.

The presumption has always been against preemption of state laws. "Congress does not cavalierly preempt state law causes of action." Bates v. Dow Agrosciences, 544 U.S. 431, 449 (2005) (citations omitted); Kroske v. US Bank Corp., 432 F.3d 976 (9th Cir. 2005). The two guiding cornerstones of the Supreme Court's preemption jurisprudence are (1) Congress's purpose

and (2) "the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress." Wyeth v. Levine, 129 S. Ct. 1187, 1194-95 (2009). "Because consumer protection law is a field traditionally regulated by the states, compelling evidence of an intention to preempt is required in this area." General Motors Corp. v. Abrams, 897 F.2d 34, 41-42 (2d Cir. 1990).

The Supreme Court has explained how these general rules apply to state regulation of national banks:

> In defining the pre-emptive scope of statutes and regulations granting a power to national banks . . . normally Congress would not want States to forbid, or to impair significantly, the exercise of a power that Congress explicitly granted. To say this is not to deprive States of the power to regulate national banks, where . . . doing so does not prevent or significantly interfere with the national bank's exercise of its powers.

Barnett Bank, N.A. v. Nelson, 517 U.S. 25, 33 (1996). The preemption test established by the Supreme Court in Barnett, is therefore not whether the law causes *any* impairment of the exercise of banking powers; the test is whether such impairment is *significant* or entirely prevents the exercise of banking powers. Id.

Federal agencies may not overreach in promulgating rules that preempt state law. Preemptive intent may not be founded "on an untenable interpretation of congressional intent and an overbroad view of an agency's

power to pre-empt state law." Wyeth, 129 S. Ct. at 1199. Specifically, federal laws do not preempt state laws "that are predicated on the duty not to deceive." Altria Group v. Good, 129 S. Ct. 538, 551 (2008). "Federally chartered banks are subject to state laws of general application in their daily business to the extent such laws do not conflict with the letter or the general purposes of the NBA." Watters v. Wachovia Bank, N.A., 550 U.S. 1, 11 (2007) (citations omitted).

The Office of the Comptroller of the Currency (OCC) cautioned national banks and their subsidiaries that they are subject to state laws that prohibit unfair or deceptive acts or practices. See Guidance on Unfair or Deceptive Acts or Practices, OCC Advisory Letter 2002-3, 2002 WL 521380 (Mar. 22, 2002). The OCC Advisory Letter expressly cites the Federal Trade Commission Act and unfair or deceptive acts "specifically prohibited by regulation." Id., at 3. The specific regulation at issue in this case, the "Holder Rule," 16 C.F.R. 433, was promulgated by the Federal Trade Commission (FTC) to prevent abuses of commercial law in which a "consumer was legally bound to pay the creditor the full price of the goods plus all the finance charges *even though the goods were defective or never delivered or the transaction was procured by fraud*." Jonathan Sheldon, Carolyn Carter, and Deanne Loonin, National Consumer Law Center,

Protecting and Improving the Best Thing the FTC Has Ever Done: The Holder Rule, p. 1 (emphasis in original), http://www.nclc.org/images/pdf/udap/letter-ftc-holder.pdf.

Requiring banks to refrain from aiding and abetting their partners' violation of the law before disbursing funds poses no significant impairment to national banking power. Banks are accustomed to looking at contract documents and examining contractual relationships between borrowers and third party sellers. Indeed, as alleged in the complaint, KeyBank reviewed and approved the student service contract before it allowed Silver State Helicopters to become a preferred partner. Pl. Third Amended Compl. for Inj. Relief, ¶ 25, 49, Dec. 16, 2009. Any additional resources a bank spends to ensure compliance with the Holder Rule, as it checks to ensure compliance with other laws, would be de minimus and certainly would not impose a significant burden.

It is simply not the case, as the district court suggested, that a bank's only options are "including the Holder Notice in its promissory notes, or by not making the loan in the first place." Kilgore v. KeyBank, 2010 U.S. Dist. LEXIS 35592, *37 (N. D. Cal. 2010). Nor does state consumer protection law affect the terms of credit offered by KeyBank because consumer protection law requires nothing further than what is already required by federal law.

Rather, to avoid aiding and abetting a violation of the law, a bank's best option is simply to refrain from knowingly disbursing loan proceeds to a seller who has failed to include the Holder Notice in its consumer contracts. KeyBank has not shown that simply ensuring that the contracts its borrowers have with the seller contain the Holder Notice before disbursing the loan funds prevents or significantly impairs the business of banking or that doing so is unduly burdensome. Without such a showing, there can be no conflict preemption.

Furthermore, requiring banks to ensure their business partners are following the law is consistent with the purpose and intent of the Holder Rule. The Holder Rule allows consumers to:

> [R]aise seller-related claims against the holder. The consumer has a practical means of obtaining redress, by simply stopping payment on the portion of the debt representing fraud. The creditor in turn has an incentive to police its sellers to avoid losing money on its loans. In the case of a loss, the creditor is in a much better position than the consumer to recoup this loss from the seller.

Sheldon, Carter, and Loonin, *supra*, at 1. To construe a bank's duty otherwise is to turn the Holder Rule on its head and provide immunity to banks that willfully and knowingly facilitate a seller's violation of the law. See Gonzalez v. Old Kent Mortgage Co., 2000 U.S. Dist. LEXIS 14530, at *13 (E.D. Pa. 2000).

II. THE DISTRICT COURT'S RULING IS AN IMPROPER EXPANSION OF THE PREEMPTION DOCTRINE AND DISREGARDS RECENT SUPREME COURT AUTHORITY LIMITING FEDERAL PREEMPTION.

True to the presumption against preemption, the progression of Supreme Court rulings in Watters, Altria, Wyeth, and, most recently, Cuomo stand as guideposts defining the narrow scope of federal preemption, consistently reminding the federal agencies not to overstep their bounds, and preserving enforcement of state laws. Watters, 550 U.S. 1 (2007); Altria, 129 S. Ct. 538 (2008); Wyeth, 129 S. Ct. 1187 (2009); Cuomo v. The Clearing House Ass'n, L.L.C., 129 S. Ct. 2710 (2009).

The Supreme Court in Watters v. Wachovia Bank, N.A determined that the federal law vesting visitorial powers solely in the OCC extended to non-bank operating subsidiaries of national banks. 550 U.S. at 21, 127 S. Ct. at 1572. It reiterated the Barnett standard allowing state regulation that does not prevent or significantly interfere with a national bank's exercise of powers. Id., at 12. The Court did not address, however, whether Congress intended to vest the enforcement of valid state law against national banks entirely in the hands of a federal agency. Despite the fact that the Court did not directly address it, the preemption issue was nonetheless contentious. In dissent, Justice Stevens wrote, "[n]ever before have we endorsed

administrative action whose sole purpose was to preempt state law rather than to implement a statutory command." Id., at 44 (Stevens, J., dissenting).

The Supreme Court, by contrast, found no preemption of state unfair trade practices claims in Altria Group v. Good, 129 S. Ct. at 551. In distinguishing the general applicability of the duty not to deceive under state law from the federal regulatory authority of the Federal Cigarette Labeling and Advertising Act (Labeling Act), the Court noted that the duty not to deceive has nothing to do with smoking and health. Id., at 547; 15 U.S.C. § 1331. "Although both of the Act's purposes are furthered by prohibiting States from supplementing the federally prescribed warning, neither would be served by limiting the States' authority to prohibit deceptive statements in cigarette advertising." Altria, 129 S. Ct. at 544. The Court reached this decision despite the fact that a stated purpose of the Labeling Act is to protect commerce from the ill effects of nonuniform requirements, the Labeling Act contained two express preemption provisions, and a FTC industry guidance letter allowed the use of descriptive terms, which Plaintiffs claimed were deceptive implied misrepresentations. Id., at 551; 15 U.S.C. §§ 1331, 1334.

The Court similarly determined that state law claims were not preempted in Wyeth v. Levine, 129 S. Ct. at 1199. Although the Food and Drug Administration (FDA) deemed the risk disclosures on a drug label

sufficient, a patient brought a state law product liability claim alleging the manufacturer failed to adequately warn of the risk of directly injecting its drug into a patient's vein. Id., at 1192. Not only was there was strong evidence that Congress did not intend FDA oversight to be the exclusive means of ensuring drug safety and effectiveness, but Wyeth "failed to demonstrate that it was impossible for it to comply with both federal and state requirements." Id., at 1192, 1198. Absent clear evidence of the impossibility to comply with both federal and state requirements, a court will conclude that it is possible to comply with both. Id., at 1198. When it is possible to comply with both federal and state law, there is no significant impairment and state law is not preempted. Id.

The Supreme Court continued to narrow the scope of federal preemption when it recently held that an OCC regulation unreasonably prohibited a state attorney general from bringing an action against a national bank to enforce state laws. Cuomo, 129 S. Ct. at 2721. This was an issue not resolved in Watters. Despite the fact that Congress declined to exempt national banks from all state banking laws and the National Banking Act does not prohibit ordinary enforcement of state law, the OCC nonetheless promulgated a rule saying "that the State may not *enforce* its valid, non-pre-empted laws against national banks." Id., at 2715, 2718, 2720

(emphasis in original). In articulating the Court's definition of legitimately preempted visitorial powers as contrasted with non-preempted regulation, the Court stated, "[o]ur cases have always understood 'visitation' as the right to oversee corporate affairs, quite separate from the power to enforce the law." Id., at 2716. A state's inability to enforce its valid, non-preempted laws against national banks would yield a "bizarre" circumstance where the State's "bark remains, but the bite does not." Id., at 2718. The Court recognized that the OCC rule "attempts to do what Congress declined to do: exempt national banks from all state banking laws," and ruled that it was an impermissible attempt to preempt valid and enforceable state law. Id., at 2720, 2721.

In contrast to the progression of Supreme Court precedent, recent Ninth Circuit rulings on federal preemption in Rose v. Chase Bank USA, N.A. and Martinez v. Wells Fargo Home Mortgage have found federal preemption of state laws. Rose, 513 F.3d 1032, 1038 (9th Cir. 2008), Martinez v. Wells Fargo Home Mortgage, 598 F.3d 549, 558 (9th Cir. 2010). In Rose, this Court determined that a California state law that required specific language and disclosures on convenience checks was preempted. Rose, at 1038. Earlier this year in Martinez, a Ninth Circuit panel found that setting charges and fees for home mortgage refinancing is incidental to the express power of engaging in real estate lending under the NBA. Martinez, at 558. Both cases

relied on the Supreme Court's decision in Watters. Rose, at 1036-38, Martinez, at 555, 556.

The district court's reasoning in Kilgore, which found viable causes of action, but dismissed the case on federal preemption grounds, is inconsistent with Supreme Court precedent and is not compelled by existing Ninth Circuit precedent. Kilgore, at ¶ 44. The instant case is distinguishable from Watters and both Ninth Circuit cases. At issue in Watters was a state's attempt to exercise visitorial powers, which is expressly preempted by Congress, over national banks. Watters, 550 U.S. at 21. Visitorial powers, the general inspection of banking activities, are not at issue in the instant case. As the Court further articulated in Cuomo, a state's use of subpoena power to inspect bank records infringes on the OCC's exclusive visitorial powers, but state substantive law is not preempted. Cuomo, 129 S. Ct. at 2721. Rather, as in Altria, and Wyeth, the matter turns on the application of state substantive law. The Ninth Circuit cases are also inapplicable here. This Court has not previously explored the scope of the Holder Rule. Rose preempted a state law that required specific language and disclosures above those required by federal law. Here, state consumer protection laws require no specific language. While the Holder Rule requires sellers to provide specific notice, KeyBank need not include anything additional in its contracts. To comply

with the law, it must simply check that the bank's partners have included language in their contracts in compliance with federal law. Unlike in Martinez, this case does not ask the Court to step into the shoes of business and determine the fairness of fees charged by a bank.

Alternatively, if this Court finds insufficient distinction between the case at bar and Rose and Martinez, it should nonetheless depart from this precedent because neither case takes into account the U.S. Supreme Court's most recent jurisprudence limiting federal preemption. Generally, a panel of a circuit court cannot overrule the decision of a prior panel. United States v. Gay, 967 F.2d 322, 327 (9th Cir. 1992). However, "[a]n exception to this rule arises when 'an intervening Supreme Court decision undermines an existing precedent of the Ninth Circuit, and both cases are closely on point.'" Id. (citing United States v. Lancellotti, 761 F.2d 1363, 1366 (9th Cir. 1985). "[T]he issues decided by the higher court need not be identical in order to be controlling. Rather, the relevant court of last resort must have undercut the theory or reasoning underlying the prior circuit precedent in such a way that the cases are clearly irreconcilable." Miller v. Gammie, 335 F.3d 889, 900 (9th Cir. 2003) (en banc). At that point, "a three-judge panel should consider itself bound by the later and controlling authority, and should reject the prior circuit opinion as having been effectively overruled." Id. at 893; see also

Galbraith v. County of Santa Clara, 307 F.3d 1119, 1123 (9th Cir. 2002); United States v. Lancellotti, 761 F.2d 1363, 1366 (9th Cir. 1985); Spinelli v. Gaughan, 12 F.3d 853, 855 n.1 (9th Cir. 1993).

Recent Ninth Circuit precedent has departed from the U.S. Supreme Court's fresh guidance on federal preemption and has instead relied on older cases. The Ninth Circuit panel in Rose relied heavily on three Supreme Court cases: Watters, Barnett, and Franklin. Rose, 513 F.3d 1032 (citing Watters, 550 U.S. 1; Barnett, 517 U.S. 25; Franklin Nat. Bank of Franklin Square v. New York, 347 U.S. 373 (1954)). A year after the Rose decision, the Supreme Court signaled its shift toward a narrower preemption doctrine in the Altria, Wyeth, and Cuomo cases. Altria, 129 S. Ct. 538; Wyeth, 129 S. Ct. 1187; Cuomo, 129 S. Ct. 2710. Though this Court decided Martinez in March of this year, the holding does not reflect the most recent developments embodied by Altria, Wyeth and Cuomo, citing only precedent from other circuits and Watters. Martinez, 598 F.3d 549 (citing Friedman v. Market St. Mortgage, 520 F.3d 1289 (11th Cir. 2008); Santiago v. GMAC Mortgage Group, 417 F.3d 384 (3d Cir. 2005); Kruse v. Wells Fargo Home Mortgage, 2006 U.S. Dist. LEXIS 26092, at *12-21 (E.D.N.Y. May 3, 2006); Watters, 550 U.S. 1)). Therefore, because neither case considers the most relevant and

recent Supreme Court jurisprudence, both are ripe for reversal based on intervening Supreme Court precedent.

The consistent guidance of the Supreme Court in narrowly interpreting federal preemption is readily applicable to the circumstances before this Court. While the Court has steadfastly refused to allow states visitorial powers over national banks, it has just as resolutely refused to expand preemption to state substantive laws. Allowing preemption where there is an absence of significant impairment, as in the instant case, inappropriately expands the doctrine of preemption. Under Supreme Court authority, banks are not entitled to special rules nor are they exempt from regulations that generally protect consumers of a bank's products and services. Banks are no different from any other business that engages in commerce in a state and are subject to the same generally applicable rules governing their conduct: be fair, do not make misrepresentations, and follow the law. See, e.g., McClellan v. Chipman, 164 U.S. 347 (1896).

III. EXPANDING THE PREEMPTION DOCTRINE TO GENERALLY APPLICABLE STATE LAWS NEGATIVELY IMPACTS THE STATE'S ABILITY TO PROTECT CONSUMERS.

Upholding the district court's ruling will expand the preemption doctrine to generally applicable state consumer protection laws and will inhibit a state attorney general's ability to protect consumers from abusive practices.

A federalist system of government is premised on shared power between federal and state governments. "The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people." U.S. Const. amend. X. James Madison recognized the profound importance of state regulation to everyday consumer transactions: "The powers reserved to the several States will extend to all the objects which, in the ordinary course of affairs; concern the lives, liberties, and properties of the people, and the internal order, improvement, and prosperity of the State." The Federalist No. 45, at 303 (James Madison) (Independent Journal, Jan. 26, 1788). Historically, States have effectively used their police powers to regulate businesses that operate within their jurisdictions. In Cuomo, the Court noted that states' powers at the time of the enactment of the NBA included the ability to examine a

corporation's manner of conducting business, enforce the corporation's own regulations, and obtain court orders to exercise control "whenever a corporation was abusing the power given it . . . or acting adversely to the public." Cuomo, 129 S. Ct. at 2716 (quoting Horace LaFayette Wilgus, Private Corporations, in 8 American Law and Procedure § 157, pp. 224-25 (James Parker Hall ed., 1910)).

Congress continues to respect the states' role in effective regulation. For example, in 1994, Congress expressly subjected interstate branches of national banks to state law, including consumer protection and fair lending laws. The House Conference Report stated:

> States have a strong interest in the activities and operations of depository institutions doing business within their jurisdictions, regardless of the type of charter an institution holds. In particular, States have a legitimate interest in protecting the rights of their consumers, businesses and communities. . . . Congress does not intend that the Interstate Banking and Branch Efficiency Act of 1994 alter this balance and thereby weaken States' authority to protect the interests of their consumers, businesses, or communities.

H.R. Rep. No. 103-651, at 53 (1994), as reprinted in 1994 U.S.C.C.A.N. 2068, 2074.

States have long been the front line defenders of their citizens through state consumer protection laws, and the presumption against preemption applies with full force here. General Motors Corp. v. Abrams, 897 F.2d

at 41-42 (state lemon law not federally preempted because it neither harms the consumer nor unconstitutionally burdens federal regulation.) For example, states' consumer protection statutes provided critical protection for consumers when the subprime mortgage crisis hit:

> Remedies under state consumer protection statutes may be more effective than weak federal and state predatory lending statutes. . . . Moreover, states can serve as laboratories of reform, enacting creative solutions, uniquely tailored to the state's concerns. For example, Massachusetts made the unprecedented move of declaring a temporary moratorium on foreclosures. These various state mechanisms are responsive to issues already discussed that are particularly acute for the subprime borrower, and more effectively address the causes of abusive subprime transactions than simple disclosure rules.

Arielle L. Katzman, Note, A Round Peg for a Square Hole: The Mismatch Between Subprime Borrowers and Federal Mortgage Remedies, 32 Cardozo L. Rev. 497, 540-41 (Nov. 2009). Long before Congress acted to address toxic mortgages and the subprime crisis, the states were dealing with the fallout. "From 2004 to 2009, over half of the states adopted laws to address foreclosure scams." Lauren K. Saunders, Preemption and Regulatory Reform: Restore the States' Traditional Role as "First Responder," p. 18 (National Consumer Law Center, Sept. 2009). In 2009, Congress gave the FTC authority to address these scams and it is now considering a rule following the models and experiences of the states. Id. State regulators took more than 7,000 mortgage enforcement actions in 2008 alone and continue to

provide protection to consumers. See Mark Pearce, Viewpoint: Far from Blame, States Deserve Vital Regulatory Role, American Banker (Aug. 26, 2009).

Whether states are enforcing consumer protection laws in the arena of mortgage foreclosures, privacy laws, discrimination statutes, contract disputes, or bankrupt vocational schools, the states have used consumer protection law to build a strong record of protecting consumers. See Minnesota v. Fleet Mortgage Corp., 158 F. Supp. 2d 962 (D. Minn. 2001) (state could bring an action to enforce state fraudulent and deceptive trade practice laws against a national bank); Alaska v. First Nat'l Bank of Anchorage, 660 P.2d 406 (Alaska 1982) (state could sue national bank to enforce state consumer protection laws); Peoples Sav. Bank v. Stoddard, 102 N.W.2d 777 (Mich. 1960) (attorney general's suit applied state antitrust law to a national bank); General Motors Corporation, 897 F.2d 34 (New York Lemon Law not federally preempted by a consent order entered into by a federal administrative agency).

The banking industry is inextricably related to consumer affairs. Preserving the states' power to protect the welfare of its citizens is essential to effective regulation. The district court's ruling represents an expansion of the preemption doctrine and strikes at the heart of local regulation and the

Attorney General's authority to enforce state consumer protection laws governing the most basic consumer transactions.

CONCLUSION

The Attorney General of the State of Montana requests that this Court follow Supreme Court precedent and reverse the holding of the district court. Plaintiff's claims under the California Consumer Protection Act are not in conflict with the National Banking Act and thus are not federally preempted.

Respectfully submitted this 3rd day of September, 2010.

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STATEMENT OF RELATED CASES

Amicus is unaware of any related cases pending before this Court.

CERTIFICATE OF SERVICE

I hereby certify that I electronically filed the foregoing with the Clerk of the Court for the United States Court of Appeals for the Ninth Circuit by using the appellate CM/ECF system on (date) .

Participants in the case who are registered CM/ECF users will be served by the appellate CM/ECF system.

Dated: September 3, 2010

Kelley L. Hubbard
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CERTIFICATE OF COMPLIANCE PURSUANT TO FED. R. APP. P. 32(A)(7)(C) AND CIRCUIT RULE 32-1 FOR CASE NUMBER 09-16703

I certify that:

Pursuant to Fed. R. App. P. 32(a)(7)(C) and Ninth Circuit Rule 32-1, the attached Amicus Brief is

☒ Proportionately spaced, has a typeface of 14 points or more and contains 4,031 words.

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Dated: September 3rd, 2010

/s/ Kelley L. Hubbard
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