Complaint Against New York Life Dismissed in Action Testing Application of California's Usury Laws

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In a recent ruling, *Lujan v. New York Life Insurance Company*, a federal judge in the Northern District of California rejected the plaintiffs' claim that New York Life violated California's usury law by charging compound interest on their loans without a written agreement. At issue were two laws: (i) Section 2 of a 1918 California ballot initiative, which states that "interest shall not be compounded … unless an agreement to that effect is clearly expressed in writing and signed by the party to be charged" and (ii) the later enacted Article XV of California's Constitution, which exempts certain classes of lenders from Section 2 and gives the California Legislature authority to regulate them. The court, tracking the language of Article XV, concluded that because "compound interest is a 'charge' upon a loan and also 'compensation' received from a lender," Article XV regulated compound interest and, therefore, conflicted with and superseded Section 2. Since the insurer was exempt from Article XV, it was exempt from Section 2.

The *Lujan* court also agreed with New York Life's contention that, even if the compound interest provision of the Initiative applied, the plaintiffs' claims fail because the insurer was in compliance with Section 2's requirement that compound interest be clearly expressed and agreed upon in writing. The plaintiffs had argued that New York Life was not in compliance and therefore not authorized to charge compound interest because plaintiffs had signed only their respective life insurance applications—not the policies themselves, which plaintiffs admitted have language authorizing the compounding of interest upon premium and policy loans. The court, looking to the California Insurance Code and case law, recognized that an application and a policy constitute the entire contract if, as was the case here, the application is endorsed upon or attached to the policy. It was also key that the plaintiffs' policies stated that the policy and application were parts of a larger "entire contract." According to the court, "[p]laintiffs did sign an agreement when they signed the application that comprised the larger agreement for insurance."

Lujan is the most recent example of a court's view of the California usury law's impact on insurers' efforts to charge compound interest on loans.(1) As the plaintiffs have appealed the ruling, the industry might soon be able to look to a Ninth Circuit ruling for clarity on the issue.

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(1) See *Martin v. Metropolitan Life Ins. Co.*, 2016 WL1427556 (N.D. Cal. Apr. 12, 2016) (insurers were exempt from the compound interest provision); *Washburn v. Prudential Ins. Co. of Am.*, 2015 WL 7454039 (N.D. Cal. Nov. 24, 2015) (admitted insurers are exempt from restrictions on the charging of compound interest). *But see Wishnev v. Northwestern Mut. Life Ins. Co.*, 2016 WL 493221 (N.D. Cal. Feb. 9, 2016) (certain lenders were exempt from the maximum interest rate provisions of the Initiative, but not the compound interest provision).