No. 24-50

IN THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

SMALL BUSINESS FINANCE ASSOCIATION;

Plaintiff-Appellant,

– v. –

CLOTHILDE HEWLETT,

Defendant-Appellee.

On Appeal from the United States District Court
for the Central District of California
Case No. 2:22-cv-08775-RGK-SK

BRIEF OF AMICI CURIAE U.C. BERKELEY CENTER FOR CONSUMER LAW & ECONOMIC JUSTICE, CALIFORNIA ASSOCIATION FOR MICROENTERPRISE OPPORTUNITY, CONSUMER FEDERATION OF CALIFORNIA, FREEFROM, HOUSING & ECONOMIC RIGHTS ADVOCATES, THE OFFICE OF KAT TAYLOR, MICROENTERPRISE COLLABORATIVE OF INLAND SOUTHERN CALIFORNIA, PUBLIC COUNSEL, PUBLIC GOOD LAW CENTER, PUBLIC LAW CENTER, AND RISE ECONOMY IN SUPPORT OF DEFENDANT AND AFFIRMANCE

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Federal Rule of Civil Procedure 26.1(a), the undersigned counsel states that the following amici curiae have no parent corporations, and no publicly held corporation owns 10% or more of its stock:

- U.C. Berkeley Center for Consumer Law & Economic Justice
- California Association for Microenterprise Opportunity
- Consumer Federation of California
- FreeFrom
- Housing & Economic Rights Advocates
- The Office of Kat Taylor
- Microenterprise Collaborative of Inland Southern California
- Public Counsel
- Public Good Law Center
- Public Law Center
- Rise Economy

Dated: September 20, 2024

/s/ David S. Nahmias
David S. Nahmias

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INTERESTS OF AMICI CURIAE[1]

Amici curiae the U.C. Berkeley Center for Consumer Law & Economic Justice, California Association for Microenterprise Opportunity, Consumer Federation of California, FreeFrom, Housing & Economic Rights Advocates, the Office of Kat Taylor, Microenterprise Collaborative of Inland Southern California, Public Counsel, Public Good Law Center, Public Law Center, and Rise Economy are a group of organizations with an interest in protecting consumers and small businesses from predatory lending practices. Amici regularly participate in proceedings before the U.S. Supreme Court and the courts of appeal, including this Court, on issues involving constitutional challenges to important consumer and small business regulations. Amici are members of a coalition that was involved in the 2018 legislative restructuring of the California Department of Financial Protection and Innovation (Department or DFPI), formerly the California Department of Business Oversight (DBO). Certain amici also co-sponsored the Commercial Financing Disclosures laws that authorized the DFPI to issue its Regulations and weighed in during the Department's rulemaking. As such, amici have an interest in the ongoing enforceability of the Regulations.

[1] No counsel for any party authored this brief in whole or in part, and no person other than amici curiae, their members, and their counsel made a monetary contribution to the preparation or submission of this brief. Fed. R. App. P. 29(a). The Department consented to the filing of this brief; SBFA objected.

INTRODUCTION AND SUMMARY OF ARGUMENT

The DFPI properly and constitutionally promulgated its commercial financing disclosure regulations to protect solo entrepreneurs and small businesses from fraud and deception in alternative lending products.

The long-unregulated sales-based finance (SBF) industry historically relied on aggressive tactics to induce borrowers into financing schemes with obscure and misleading terms that concealed the high prices of their products.[2] To address this problem, in 2018 the California Legislature enacted Senate Bill 1235, Stats. 2018., ch. 1011, to require that SBF companies disclose necessary factual information about their products, including "[t]he total cost of the financing expressed as an annualized rate." Cal. Fin. Code §§ 22802(b)(6), 22803(f). The Legislature then authorized the Department to determine how that rate should be calculated and expressed. *Id.* § 22804(b).

In promulgating the Regulations at issue here, Cal. Code Regs., tit. 10, § 900 *et seq.*, the Department selected widely used financial metrics to allow small business borrowers to comparison-shop among SBF products, including: estimated APR, payment, and terms; finance charges; payment, and prepayment terms. *Id.* §§ 911, 914; RB at 10-11, 13. These disclosures compel truthful, accurate, and

[2] These products, which include sales-based financing, merchant cash advance (MCA), and open-end credit, are collectively described as "SBF products." *See* Respondent's Br. (RB) at 3-8.

uncontroversial descriptions of SBF products' terms derived from standard arithmetic financial calculations that lenders regularly compute using assumptions of borrower behavior. They are thus the kind of factual disclosures that do not offend the First Amendment. *See Milavetz, Gallop & Milavetz, P.A. v. United States*, 559 U.S. 229, 249-50 (2010).

The mandatory SBF disclosures required are typical of useful government-required disclosures of information, from price labels to nutrition fact panels. *See, e.g.*, *Spirit Airlines, Inc. v. U.S. Dep't of Transp.*, 687 F.3d 403 (D.C. Cir. 2012) (price labels on airline tickets); *N.Y. State Rest. Ass'n v. N.Y.C. Bd. of Health*, 556 F.3d 114 (2d Cir. 2009) (calorie contents on fast food menus). APR and loan terms are calculations already used across various credit markets—and, indeed, by SBF companies themselves—as a result of decades-old obligations under the federal Truth In Lending Act (TILA), 15 U.S.C. § 1601 *et seq.* The same purpose underlying TILA's APR requirement, to create a single measurement that enables an apples-to-apples comparison among credit programs, motivates these Regulations. By mandating disclosure of SBF product terms like estimated APR, the Regulations provide consistency and comparability to small business owners accustomed to seeing this longstanding metric in the context of consumer transactions.

Because the disclosures mandate purely factual and uncontroversial information about SBF products, they merit relatively lenient judicial scrutiny under *Zauderer v. Office of Disciplinary Counsel of Supreme Court of Ohio*, 471 U.S. 626, 651 (1985). The Regulations are reasonably designed to promote clarity in pricing and protect small businesses against predatory SBF lenders. Mandated product information disclosures help protect small businesses against unscrupulous practices in the SBF industry, which have resulted in tens of thousands of small businesses[3] being charged excessively high levels of interest and have forced many into bankruptcy.[4] Furthermore, in light of the serious and pervasive problems that have permeated this market,[5] estimated APR disclosures are readily justifiable and do not unduly burden SBF companies.

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[3] In 2022 some 2-3 million small business sought MCAs. *See* Ann Marie Wiersch, Fed. Reserve, *Small Business Credit Survey: 2022 Report on Employer Firms* 19 (2022), https://perma.cc/Q4PN-GM3R (finding that 10 percent of small businesses surveyed sought MCAs); U.S. Small Bus. Admin. (SBA), *2022 Small Business Profile* (2022), https://perma.cc/H8C7-2EYB (reporting 33.2 million small businesses nationwide that year).

[4] *See* Becky Yerak, *An Easy Financing Source Pushes Some Small Businesses Into Bankruptcy*, Wall Street J. (Feb. 19, 2024), https://tinyurl.com/3z6dmnmz (finding that over 100 businesses that filed for bankruptcy in the previous year attributed their bankruptcies at least partly to MCAs).

[5] *See, e.g.*, Barbara J. Lipman & Ann Marie Wiersch, Fed. Reserve, *Uncertain Terms: What Small Business Borrowers Find When Browsing Online Lender Websites* 11 (2019), https://perma.cc/37Q6-J3F5 ("*Uncertain Terms*"); Eric Weaver et al., Opportunity Fund, *Unaffordable and Unsustainable: The New Business Lending on Main Street* 3 (2016), https://perma.cc/X9G4-DHFD.

Because the Regulations meet the *Zauderer* standard, they satisfy the requirements of the First Amendment. Indeed, they would satisfy even the more demanding intermediate scrutiny of the standard set forth in *Central Hudson Gas & Electric Corp. v. Public Service Commission*, 447 U.S. 557, 577 (1980), standard, were that test applied. Under either standard, the Department's disclosures effectively serve a critical public need: to protect small businesses from predatory lending.

ARGUMENT

I. THE REGULATIONS REQUIRE ROUTINE INFORMATIONAL DISCLOSURES THAT COMPORT WITH THE FIRST AMENDMENT.

For decades, courts have upheld compelled disclosures—like the Regulations here—requiring that commercial entities disclose truthful information about their products in order to protect consumers from fraud and deception. *See, e.g.*, *Zauderer*, 471 U.S. at 651; *CTIA-The Wireless Ass'n v. City of Berkeley*, 928 F.3d 832, 843 (9th Cir. 2019). When laws compel commercial speech to promote truthfulness and accuracy, they are afforded more relaxed judicial scrutiny than limitations on other forms of speech. *See Nat'l Ass'n of Wheat Growers v. Bonta*, 85 F.4th 1263, 1275 (9th Cir. 2023) (*NAWG*) (setting forth the "lower standard applied in *Zauderer*"); *Maryland Shall Issue, Inc. v. Anne Arundel Cty.*, 91 F.4th

238, 250 (4th Cir. 2024) (confirming that "*Zauderer* is the appropriate lens through which we are to analyze" compelled disclosures).

This Court reiterated the *Zauderer* standard for adjudging the constitutionality of compelled commercial speech last year in *NAWG*, 85 F.4th at 1275. As a threshold matter, a court "first must determine whether [speech] concerns purely factual and uncontroversial information"; if so, then the Court "consider[s] whether it is reasonably related to a substantial governmental interest and is not unjustified or unduly burdensome."[6] *Id.*; *see also Moody v. NetChoice, LLC*, 144 S. Ct. 2383, 2439 (2024) (Alito, J., concurring) (similarly articulating the *Zauderer* standard).[7]

The disclosures at issue here meet *Zauderer*'s lenient and well-accepted criteria. The Regulations simply obligate lenders to "include in [their] advertising

[6] This Court has required that the government's interest be "substantial," *see CTIA*, 928 F.3d at 842, in contrast to sister circuits that describe the interest as "legitimate." *See, e.g.*, *RJ Reynolds Tobacco Co. v. FDA*, 96 F.4th 863, 883 (5th Cir. 2024); *Md. Shall Issue*, 91 F.4th at 250; *Am. Hosp. Ass'n v. Azar*, 983 F.3d 528, 541 (D.C. Cir. 2020); *Nat'l Elec. Mfrs. Ass'n v. Sorrell*, 272 F.3d 104, 115 (2d Cir. 2001). Nevertheless, because the Court has defined a "substantial" interest as simply one that is "more than trivial," *CTIA*, 928 F.3d at 844, the government's burden remains relatively modest.

[7] This Court's en banc opinion in *American Beverage Association v. City & County of San Francisco*, 916 F.3d 749 (9th Cir. 2019), did not alter the framework. Because the en banc majority determined that the disclosure there was "unduly burdensome"—and therefore failed a necessary component of the *Zauderer* test—it found no need to apply the other elements of the test. *Id*. at 755-56.

purely factual and uncontroversial information about the terms" of SBF products. *Zauderer*, 471 U.S. at 651; *see* Cal. Code Regs., tit. 10, §§ 911(a)(2)-(4), 914(a)(3), 940(a). That is far from compelling misleading or misrepresentative commercial speech. *See* App. Opening Br. (AOB) at 7-13. Because *Zauderer*'s threshold question is satisfied, the rest of the *Zauderer* test is applied. The required disclosures of estimated APR and other lending terms are reasonably related to California's substantial interest in guaranteeing transparency and clarity in the once lawless SBF market. The confusion and financial harm visited upon small business borrowers before the Regulations were promulgated amply justify the disclosures. And the conciseness of the disclosures along with the continued opportunity for lenders to supplement them with their own statements confirm that the Regulations are not unduly burdensome.

Should this Court determine that the Regulations do not satisfy *Zauderer*'s threshold element—that they are not "factual and uncontroversial"—the result is not their automatic invalidation. Rather, the Regulations would then be scrutinized under the well-established intermediate scrutiny standard set forth in *Central Hudson*, 447 U.S. at 577. Under that framework applied in the context of compelled disclosures, the required disclosures are permissible if the asserted governmental interest is substantial, the disclosures directly and materially advance that interest, and the disclosures are no more extensive than necessary—*i.e.*, there

is a reasonable fit between the ends to be attained and the means chosen to accomplish them. *See Aargon Agency, Inc. v. O'Laughlin*, 70 F.4th 1224, 1232 (9th Cir. 2023). Here, the government has a more-than-substantial interest in addressing the deceptive marketing of complex commercial finance products to small and unsophisticated businesses borrowers. The Disclosures directly and materially advance the Department's interest in providing borrowers with better information and the chance to comparison-shop. And the Regulations are nicely tailored to their objective, not restricting advertising for specific types of financing but simply providing small businesses accurate information that they currently lack. In sum, the Regulations would also pass muster under *Central Hudson*.

Since the Regulations are factual and uncontroversial, however, it is the full *Zauderer* test that properly applies here. That is the standard selected and correctly applied by the district court, *SBFA v. Hewlett*, 2023 WL 8711078, at *9 (C.D. Cal. Dec. 4, 2023), and should be affirmed.

II. THE REQUIRED DISCLOSURES ARE FACT-BASED AND WELL-ACCEPTED FORMS OF PROMOTING FINANCIAL TRANSPARENCY.

Requiring SBF companies to disclose the full cost of their products accords with the First Amendment's commercial speech framework. *See Milavetz*, 559 U.S. at 249 (upholding disclosures that "entail only an accurate statement" about the service provided); *Spirit*, 687 F.3d at 412 (describing "the advertising of prices" as

"quintessentially commercial" and sustaining total price disclosures). By calling on SBF companies to present the costs of credit products using metrics that are widely understood and easily calculable by the lenders themselves, the Regulations compel disclosure of "necessarily factually accurate" data. *NAWG*, 85 F.4th at 1276-77. Nor are lenders forced to express any opinion or stake out a position about their products. *See CTIA*, 928 F.3d at 847 (distinguishing between "inflammatory" and "purely factual" statements); *accord RJ Reynolds*, 96 F.4th at 878. Instead, the disclosures are the kind of garden-variety disclosures that rely on well-established information in ways that decrease the opportunity for deception and misunderstanding. *See Milavetz*, 559 U.S. at 250-51.

A. By Requiring Disclosure of Estimated APR And Other Terms, The Regulations Call For Purely Factual Information About Sales-Based Financing Products.

The total costs that estimated APR and other estimated or actual terms and charges expressed by the disclosures are grounded in "literally true" and "actual, factual information," *NAWG*, 85 F.4th at 1276, about the products that SBF companies offer. That these figures are estimates does not render them misleading, especially when the disclosures qualify that estimated APR may vary from the effective APR depending on circumstances. *See* Cal. Code Regs., tit. 10, §§ 911(a)(5)(C); 914(a)(3)(C).

1. APR Is A Simple Calculation Based On The Factual Terms of Credit Products.

APR is a basic, fact-based formula that expresses what borrowers are charged as a percentage of their loan measured over a common unit of time.[8] It is easily computed for both traditional loans and alternative lending products.[9] APR was adopted by TILA and its interpretive Regulation Z to promote the "informed use of credit . . . so that the consumer will be able to compare more readily the various credit terms available." 15 U.S.C. § 1601(a). APR encompasses all required "finance charges" included in the credit product, including interest and other service fees. *See* 15 U.S.C. § 1605(a).[10] The formula is defined broadly to maximize flexibility, simplicity, and comparability while also guaranteeing "reasonable accuracy." *See* 15 U.S.C. § 1606(a)(1)-(2); 12 C.F.R. §§ 1026.14(a), 1026.22(a).

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[8] *See, e.g.*, Martha C. White, *What is APR?* Wall Street J. (June 21, 2024), https://perma.cc/6X3X-Q9SJ (explaining how to calculate APR); Expert Report of Prof. Adam Levitin, 5-ER-915 (explaining that "APR is a metric of how expensive it would be to carry the financing for a full year").

[9] *See, e.g.*, *Here's What Customers Will Pay*, Affirm, https://perma.cc/W6FJ-KLGB (APR calculator for business loans); Olivia Chen, *Merchant Cash Advance Calculator: Find the True Cost of an MCA*, Nerdwallet, https://perma.cc/B7GL-FL5M.

[10] *See* S. Rep. No. 90-392, at 8 (1967) (noting that lawmakers intended for APR to include "all costs incident to credit").

The total estimated cost to potential customers of SBF products can easily be expressed as an estimated APR.[11] Like traditional lenders, SBF companies must compute the rate they expect to earn on a given transaction in order to decide whether to extend financing, what terms to set, what loss rates to project, etc.—the lender's internal rate of return.[12] On an annualized basis, that rate is the *same* as the rate they expect the borrower to pay, that is, the borrower's estimated APR.[13] In other words, even before the Regulations went into effect, lenders were already calculating estimated APR for their products.

The same APR formula used for traditional loans, which requires making fundamental yet reasonable assumptions, is applicable to SBF products. Potential SBF customers simply must plug their expected payment amounts and their due date into the formula. For traditional loans, the loan agreement sets those expected payments, and—for purposes of APR calculation—it presumes that the borrower's actual repayment behavior matches their projected repayment. Similarly, for SBF products, the financing company estimates the small business borrowers' expected

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[11] *See* Charles H. Green, *Banker's Guide to New Small Business Finance* 98-99 (2014).

[12] *See*, Aly J. Yale, *Internal Rate of Return (IRR)*, Business Insider (July 18, 2024), https://perma.cc/G9FN-9ZUL; Tim Vipond, *Internal Rate of Return*, Corporate Finance Inst., https://perma.cc/BU83-2YAE.

[13] *See* CFPB, Comment to 12 C.F.R. § 1026.22, https://perma.cc/QS2A-L4J6 (stating that the composite APR for a step-rate product involves calculation of internal rate of return).

sales volume. That estimate generates the payment amounts and dates, which can then be plugged into the same APR formula.[14] Thus, contrary to SBFA's assertions, it is entirely possible and factually correct for SBF providers to calculate estimated APR using certain assumptions about term and average receipts income—assumptions which can be tailored to each prospective borrower using the very same information that SBF providers routinely collect and use.[15]

As noted, SBF companies already calculate for their investors and prospective customers much of the information called for by the disclosures. For example—belying SBFA's argument that its companies cannot estimate the term length over which the financing will be paid, AOB at 10, 27—the MCA company CAN Capital provided prospective investors with a table comparing the estimated term lengths of its products to those of a closed-end loan product down to two decimal points.[16] Moreover, commercial lenders regularly offer their own free online calculator to help small business owners compute the "cost of a MCA and

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[14] Sarah George, *How to Convert Factor Rates to Interest Rates* (May 19, 2023), https://perma.cc/ZCK6-BVU7 (encouraging prospective SBF customers to convert the terms of SBF products into traditional APR figures to help estimate and compare total costs); Emma Parker, *How to Calculate the True Cost of a Merchant Cash Advance (MCA)*, Clarify Capital, https://perma.cc/AYH4-4RRD;

[15] Green, *supra*, at 100-101 (calculating estimated APR and terms based on a given return on investment for an MCA); Levitin Report, 5-ER-917-18.

[16] Eric Rapp et al., *CAN Capital Funding LCC Series 2014-1: Presale Report* 3, 20 (2014), https://perma.cc/66Q7-HWXU (disclosing a "expected weighted-average annual return [i.e., an Estimated APR] . . . of approximately 48%").

the effective APR."[17] These internal calculations and pre-existing tools also belie SBFA's contention that it is impossible or irrelevant to calculate an estimated APR. Additionally, they demonstrate the market demand for this information.

2. The Regulations Are Intended To Facilitate Apples-to-Apples Factual Comparisons of Credit Products, Just Like Other Well-Accepted Disclosures.

The estimated APR and other disclosures are akin to other disclosures that are designed to enable consumers to easily evaluate the terms of different types of loan products based on their factually accurate attributes, regardless of their precise features. Prior to TILA's enactment, banks and other lenders did not uniformly express their costs in standardized metrics.[18] Consequently, consumers had no simple way to compare the costs of loans, resulting in widespread confusion and ample opportunity for fraud and predation.[19] To address deception in the credit market, Congress enacted TILA to mandate disclosures of the cost of credit as an

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[17] Funder Intel, *The Ultimate MCA Calculator*, https://perma.cc/AS8A-69QN; Upwise Capital, *MCA Calculator*, https://perma.cc/NE5V-U6RR.

[18] Christopher L. Peterson, *Truth, Understanding, and High-Cost Consumer Credit: The Historical Context of the Truth in Lending Act*, 55 Fla. L. Rev. 807, 814 (2003).

[19] Elizabeth Renuart & Diane E. Thompson, *The Truth, The Whole Truth, and Nothing but the Truth: Fulfilling the Promise of Truth in Lending*, 25 Yale J. on Reg. 181, 217 (2008).

APR.[20] The drafters designed the APR to be a "composite rate which includes all charges incident to credit" expressed in a "uniform system of disclosure."[21] Lawmakers called for clear disclosures of the cost of credit "[a]s a matter of fair play to the consumer."[22]

Mandated disclosure of the full costs of credit in an easily understood and comparable way is consistent with other well-accepted factual disclosures in the marketplace, like nutrition labels or college graduation rates. *See*, *e.g.*, *N.Y. State Rest.*, 556 F.3d at 135-136 (upholding calorie disclosure requirements intended to address obesity); *Mass. Ass'n of Private Career Schs. v. Healey*, 159 F. Supp. 3d 173, 197-199 (D. Mass. 2016) (affirming disclosure regulations on for-profit schools). Congress in fact analogized APR disclosure to other measures of disclosing factual information about everyday consumer products.[23] As Senator William Proxmire, the lead sponsor of TILA, described:

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[20] *See* Anne Fleming, *The Long History of "Truth In Lending*," 30 J. Pol'y His. 236, 249-55 (2018) (describing the legislative history of APR); Levitin Report, 5-ER-914 (calling APR "the centerpiece of the TILA disclosure regime").

[21] S. Rep. No. 90-392, at 2, 8; *see also* H.R. Rep. No. 90-1040, at 13 (1967) (stating that lawmakers' objective to allow customers to "compare the cost of credit and to make the best informed decision" in a "uniform manner").

[22] H.R. Rep. No. 90-1040, at 9.

[23] *See, e.g.*, H.R. Rep. No. 90-1040, at 9 ("Now that the right of consumers to be fully informed is protected when they shop in the supermarkets, the time has come to protect that right for shoppers who seek credit.").

> Just as the consumer is told the price of milk per quart and the price of gasoline per gallon, so must the buyer of credit be told the 'unit price.' . . . Without easy knowledge of this unit price for credit, it is virtually impossible for the ordinary person to shop for the best credit buy. This is true, of course, because different offerings of credit may vary with respect to the amount of debt, the number of payment periods under which it is to be repaid, and the amount to be paid per period.[24]

In this way, APR disclosures resemble nutrition labels in that they provide information to consumers "in a standard format that is easily accessible and easy to use" and "help consumers make informed . . . choices." *N.Y. State Rest.*, 556 F.3d at 135-136; *see Am. Meat Inst. v. USDA*, 760 F.3d 19, 31 (D.C. Cir. 2014) (en banc) (*AMI*) (Kavanaugh, J., concurring) (observing that "no one questions the federal government's ability to require purely factual 'nutrition labels,' such as a product's calorie count or sugar content"). Like nutrition labels, they also account for some expected variation between the disclosed amount of a given term and its actual amount. *See N.Y. State Rest.*, 556 F.3d at 121-22 (sustaining disclosure that included disclaimer that "there may be variations in calorie content values"). Likewise, the APR disclosures are simply a "mathematical formula based on publicly-available data" that can be calculated based on the providers' own information. *Mass. Ass'n*, 159 F. Supp. 3d at 197-99 (sustaining disclosures of

[24] 113 Cong. Rec. 2,042 (1967) (statement of Sen. Proxmire).

graduation rate and job placement rate); *accord S. Cal. Inst. of Law v. Biggers*, 613 F. App'x 665, 666 (9th Cir. 2015).

As with APR in consumer credit products, estimated APR for SBF products is simply a fact-driven value that facilitates comparison shopping. The Department acknowledged the value of APR's "apples-to-apples" approach when it chose to adopt it as a similar metric for the Regulations, as did the Legislature when it later enacted Senate Bill 33 to make permanent the annualized rate disclosure, *see* Stats. 2023, ch. 376.[25] The Department also defined APR in a manner consistent with and expressly referencing federal Regulation Z. *See* Cal. Code Regs., tit. 10, § 940(a) (citing 12 C.F.R. pt. 1026).[26] Much like TILA, the Regulations contemplate finance charges in APR computation expansively. *Compare* 15 U.S.C. § 1605(a), *with* Cal. Code Regs., tit. 10, § 940. The Regulations also provide clear guidance on how small business lenders must calculate and present their estimated APR; further, like

[25] DFPI, *Final Statement of Reasons: Commercial Financing Disclosures*, PRO 01/18, at 30 (2022); S. Comm. on Banking & Fin. Insts., Rep. on S.B. 33, 2023-2024 Reg. Sess., at 8 (Cal. 2022) ("S.B. 33 Analysis") ("APR serves as a helpful metric in signaling the relative benefits of the term structures of otherwise similar financing products.").

[26] *See also Final Statement of Reasons* at 28 (concluding that APR disclosures were not "at odds with TILA" and Regulation Z).

TILA, they are crafted to permit some variation between estimated and effective APR. *See id.* §§ 911(a)(5)(C); 914(a)(3)(C).[27]

The Regulations, in sum, call for the disclosure only of accessible, familiar, and factual information.

B. The Disclosures Rely On Uncontroversial Metrics That Are Well Understood and Widely Accepted.

The Regulations mandate disclosure of readily understood, easily determinable, apolitical—and thus uncontroversial—credit information. In the compelled speech context, statements may be deemed "controversial" if their conclusion is not shared by a "strong . . . consensus" of the relevant expert community, *NAWG*, 85 F.4th at 1278 (*i.e.*, describing that situation as objectively controversial), or if they force businesses "to take sides in a heated political controversy," *CTIA*, 928 F.3d at 848 (*i.e.*, subjectively controversial). In other words, a statement may be controversial either if its truthfulness "is not settled or is overwhelmingly disproven or . . . [if it] raises a live, contentious political dispute." *RJ Reynolds*, 96 F.4th at 881 & n.57 (citing *NAWG*, 85 F.4th at 1277-78). That is a far cry from what the Regulations demand.

[27] *See also* DBO, *Initial Statement of Reasons: Commercial Financing Disclosures*, PRO 01/18, at 37-38 (2020) (explaining that DFPI's intention for the federal APR standard to apply to "maximize[] the likelihood [SBF] recipients will understand the rate disclosure").

Disclosure of the full costs of SBF products to allow customers to comparison shop is not "controversial." Instead, it is rooted in "factually straightforward, evenhanded, and readily understood" information with a noted 'historical pedigree.'" *AMI*, 760 F.3d at 34 (Kavanaugh, J., concurring); *see also Recht v. Morrisey*, 32 F.4th 398, 417 (4th Cir. 2022) (upholding disclosures on attorney advertisements calling for "well known" information). For example, as discussed above, estimated APR is a mathematical equation that has been commonplace in credit markets for over fifty years. APR is now "the bedrock piece of information consumers consider" in evaluating credit products.[28] The Department repeatedly "borrowed" particular APR requirements from TILA for SBF product disclosures and made adjustments to the final Regulations to better mirror TILA and minimize customer confusion.[29] In addition, disclosure of estimated APR and other terms cannot be controversial (or misleading) when SBF companies have regularly conveyed them to their investors and customers. *See supra* Section II.A.1; *see Nationwide Biweekly Admin., Inc. v. Owen*, 873 F.3d 716, 734 (9th Cir. 2017) (a lender "cannot credibly hold out this disclaimer as evidence

[28] Renuart & Thompson, *supra*, at 217 (summarizing a study showing that "91% of the population was 'aware' of the APR" in credit products and that "82% of all respondents said that the APR was the 'most important thing to look at when comparing credit card offers'").

[29] *See, e.g.*, *Final Statement of Reasons* at 40, 71, 73, 81, 98.

that it is already providing potential customers with accurate information while also claiming that the required disclosures are misleading").

A controversy is also not raised by the presence of some disagreement within the industry about the appropriate calculation of actual APR—especially where the disclosures expressly inform borrowers of potential variation. *See NAWG*, 85 F.4th at 1278 (noting "uncontroversial" does not mean "unanimous"). By contrast, SBFA's proposed alternative metric, Annualized Cost of Capital, was rightly rejected by the Department because it "lack[ed] the industry recognition, a track record, or familiarity . . . that APR possesses."[30]

Finally, the Regulations do not require commercial lenders to enter hot-button political debates. *See CTIA*, 928 F.3d at 848. Calculation of estimated APR is "non-ideological," *Env't Def. Ctr. v. EPA*, 344 F.3d 832, 850 (9th Cir. 2003); it is merely an application of a simple formula using information that SBF providers have available. The fact that some members of the California Legislature initially questioned the approach of estimated APR in the debate over Senate Bill 1235, *see SBFA*, 2023 WL 8711078, at *7-8, does not mean that the Regulations are controversial or carry "baggage." AOB at 37-40. To the contrary, "ideological baggage has no relevance to the first *Zauderer* prong." *RJ Reynolds*, 96 F.4th at 880; *cf. Recht*, 32 F.4th at 418 (rejecting the argument that litigation over a

[30] *Final Statement of Reasons* at 44.

disclosure renders it controversial). Furthermore, that debate is now resolved. Last year, the Legislature unanimously amended the Commercial Financing Disclosures Law in Senate Bill 33, which expressly recognized the Regulations. Stats. 2023, ch. 376 ("The bill would make conforming changes to the provisions describing the regulations adopted by the commissioner governing these disclosure requirements"), *id.* § 6, *enacted at* Cal. Fin. Code § 22806 (eff. Jan. 1, 2024). The Legislature was fully aware of the disclosures in enacting Senate Bill 33 and chose not to disapprove them.[31]

The Regulations compel SBF companies to present their products using fact-based, well-understood terms. Accordingly, the Regulations require purely factual and uncontroversial disclosures that satisfy the threshold *Zauderer* inquiry.

III. THE REGULATIONS ARE REASONABLY RELATED TO CALIFORNIA'S INTEREST IN PROMOTING PRICE TRANSPARENCY IN THE SMALL BUSINESS LENDING MARKET.

Because the initial *Zauderer* inquiry is satisfied, the Court may then proceed to the remainder of that lenient standard. The SBF disclosures satisfy the rest of the *Zauderer* test because they are reasonably related to a substantial state interest and are neither unduly burdensome nor unjustified.

California has a significant interest in promoting a truthful and transparent small business lending market. *See, e.g.*, *Edenfield v. Fane*, 507 U.S. 761, 769

[31] *See* S.B. 33 Analysis at 3 (describing the promulgation of the Regulations).

(1993) (noting that a state's "interest in ensuring the accuracy of commercial information in the marketplace is substantial"). Markets function better when guardrails exist to promote the "the free flow of commercial information" and restrict deceptive behavior. *Va. State Bd. of Pharma. v. Va. Citizens Consumer Council, Inc.*, 425 U.S. 748, 765 (1976) (explaining that the regulation of commercial speech is needed to ensure that "private economic decisions . . . be intelligent and well informed"). Such guardrails "further[], rather than hinder[]" the values that animate the First Amendment. *CTIA*, 928 F.3d at 852; *see Chamber of Commerce v. SEC*, 85 F.4th 760, 771-72 (5th Cir. 2023) (holding that SEC rules addressing "information asymmetry" in the securities market satisfied *Zauderer*); *Owen*, 873 F.3d at 734-35 (upholding California mortgage refinance solicitations disclosures intended to prevent consumer deception). Furthermore, government-mandated disclosures of estimated prices and terms are well-accepted mechanisms to promote transparency in the marketplace and routinely pass constitutional muster. *See, e.g.*, *Azar*, 983 F.3d at 540-41 (upholding hospital rate disclosures); *Poughkeepsie Supermarket Corp. v. Dutchess Cty.*, 648 F. App'x 156 (2d Cir. 2016) (sustaining item price sticker ordinance); *Spirit*, 687 F.3d at 414-15 (sustaining airline total price disclosures).

By calling for estimated APR and other terms, the Regulations seek to enhance transparency of SBF products, protect small businesses, and promote

California's interest in clearer and more competitive credit markets. Prior to the enactment of Senate Bill 1235, a lack of uniform standards characterized the commercial financing market, resulting in confusion among small business owners regarding the true cost of financing.[32] Moreover, online lending and other non-traditional financing products relied on "aggressive, and often misleading" tactics[33] that obscured their often exorbitant effective APRs.[34] One analysis of these contracts found that the average undisclosed APR charged was 94 percent, and that some APRs exceeded 350 percent—and even higher.[35] SBF products were also marketed in ways that misled customers into accepting higher-priced financing than they anticipated.[36]

In addition, SBF products particularly targeted solo entrepreneurs and very small businesses, who—as the California Legislature later recognized—largely

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[32] Barbara J. Lipman & Ann Marie Wiersch, Fed. Reserve, *Alternative Lending Through the Eyes of "Mom-and-Pop" Small-Business Owners* 14-15 (2015), https://perma.cc/F6EW-HFKB.

[33] Evan Zullow, Sandhya Brown, & Malini Mithal, FTC, *Strictly Business Forum Staff Perspective* 6 (2020), https://perma.cc/2WMU-DRXE/.

[34] Carolina Martinez & Heidi Pickman, *California Passes Historic Truth in Small-Business Lending Law—Congress Should Take Note*, The Hill (Oct. 5, 2018), https://thehill.com/blogs/congress-blog/politics/410049-california-passes-historic-truth-in-small-business-lending-law/ (citing 2015 survey administered by DBO).

[35] Weaver, *supra*, at 3.

[36] *See, e.g.*, *Uncertain Terms*, *supra*, at 11 (finding three providers' publicly advertised products had hidden estimated APR equivalents of about 70 percent, 45 percent, and 46 percent).

lack commercial expertise and thus are more akin to ordinary consumers than sophisticated corporations.[37] Nationwide, over 81 percent of businesses have no employees whatsoever,[38] meaning that they are owned and operated by single individuals or families. In California, 99 percent of all businesses are deemed small businesses, and of those, 98 percent have fewer than 20 employees.[39] Meanwhile, according to one recent survey, over 77 percent of small businesses expressed concern about accessing capital.[40] As such, the market for MCAs and similar financial products is significant, as is the opportunity for abuse and deception.

The 2018 Commercial Financing Disclosure Law (Senate Bill 1235) and the DFPI's Regulations serve to protect small business from these predatory practices and further California's substantial interest in a free-flowing small business finance marketplace. The law's annualized rate disclosures were intended to provide SBF customers with "the information they need to make good decisions" and help them

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[37] Ann Marie Wiersch et al., Fed. Reserve, *Click, Submit 2.0: An Update on Online Lender Applicants from the Small Business Credit Survey* 4-6 (2019), https://perma.cc/LEA4-SLR7 (finding that younger, smaller, and higher-credit-risk small businesses are more likely to seek alternative financing online); S.B. 33 Analysis at 3 (explaining that the small businesses to be protected "may not have sophisticated knowledge of financing products").

[38] SBA, *Frequently Asked Questions* (2023), https://perma.cc/Z7H5-A2CR.

[39] Cal. Off. of the Small Bus. Advocate, *How Small Business Drives California's Economy*, https://perma.cc/5MCJ-N3SN.

[40] Goldman Sachs, *Glass Half Full* (2024), https://perma.cc/Q3XZ-D869.

"better understand the terms and costs of the financing available."[41] The DFPI reasonably determined that use of estimated APR disclosure—as opposed to "brand new or uncommon disclosure metrics"—simplified compliance for providers, provided small businesses the opportunity to "comparison shop," and "avoid[ed] confusion" for borrowers already familiar with the concept of APR.[42] The DFPI based that determination on thorough expert analysis from forty-two stakeholder groups, businesses, and advocates.[43] It then issued meaningful disclosures to ensure that SBF products in California are presented to customers on a level playing field.

IV. THE DANGERS OF PREDATORY SMALL BUSINESS FINANCING JUSTIFY THE REGULATIONS AND DO NOT UNDULY BURDEN LENDERS.

Having established the proper nexus between the Regulations and California's interest in transparency in the SBF market, the Department need only show that its measures are neither unjustified nor unduly burdensome. *See Am. Beverage Ass'n*, 916 F.3d at 756. The proliferation of confusion and deception in the SBF market that precipitated Senate Bill 1235 and the Regulations justifies the disclosures. The abusive practices engaged in by the small-business lending

[41] S. Comm. on Banking & Fin. Inst., Rep. on S.B. 1235, 2017-2018 Reg. Sess., at 4 (Cal. 2018) ("S.B. 1235 Analysis").

[42] *Initial Statement of Reasons* at 45-50.

[43] *Id.* at 38

industry are well documented and substantiate the Legislature and the Department's minimal intervention in the market. *See supra* notes 32-40.

The Regulations, which are intended to address widespread deceptive practices, also do not pose any unwarranted burden on SBF companies. The First Amendment does not protect false, misleading or deceptive commercial advertising. *See In re R. M. J.*, 455 U.S. 191, 203 (1982). Moreover, disclosures that are "reasonably crafted" to compel truthful and accurate statements about the products and mitigate the opportunity for deception do not pose an undue burden. *United States v. Philip Morris USA Inc.*, 855 F.3d 321, 328 (D.C. Cir. 2017) (finding that "the means-end fit is self-evidently satisfied" in such circumstances). As noted above, SBF companies previously engaged in deceptive advertising tactics that tricked customers into accepting extraordinarily high-cost products.[44] Accordingly, requiring lenders to accurately depict the true cost of these products—while not limiting their ability to market those products—is fully warranted.

Furthermore, that the *commercial* financing market will be unharmed by the Regulations is suggested by the dearth of economic harm suffered by *consumer* lenders after TILA mandated the disclosure of their products' APRs. During the congressional debate over TILA, the retail credit industry unsuccessfully lobbied to

[44] *See, e.g.*, *Uncertain Terms*, *supra*, at 11.

exempt revolving credit accounts from the law.[45] Representatives contended that inclusion of all relevant charges for revolving credit in a single APR disclosure was "non-workable," would "create false and misleading information," and would "confuse and bewilder the customer."[46] The U.S. Chamber of Commerce also expressed concern that APR disclosure of revolving credit plans would cause retailers to engage in "guesswork" and quote "false rates" to customers.[47] Nevertheless, the sky did not fall on the consumer credit industry after mandatory APR disclosures were introduced. In fact, in the years after TILA's passage, usage of credit cards—a type of revolving credit product—soared, as did industry profits.[48] Moreover, the disclosure regime is now widely accepted without serious industry objection.[49]

The evidence so far suggests the increasing regulation, including the DFPI's disclosure requirements, has similarly not engendered any undue hardship to SBF

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[45] *See* S. Rep. No. 90-392, at 10; 113 Cong. Rec. 18,402 (statement of Sen. Proxmire) (noting that TILA's language on revolving credit plan disclosures was the "most widely discussed subject" in the legislation).

[46] *See Hearings Before the Subcomm. on Consumer Affairs of the H. Comm. on Banking & Currency on H.R. 11601*, 90th Cong. 667-70 (1967) (statement of George H. Kimball, Nat'l Retail Merchants Ass'n).

[47] *Id.* at 854 (statement of F. Turner Hogan, U.S. Chamber of Commerce).

[48] Fleming, *supra*, at 257; Robin Stein, *The Ascendancy of the Credit Card Industry*, PBS Frontline (Nov. 23, 2004), https://perma.cc/3BLC-ENUZ.

[49] Peterson, *supra*, at 881.

companies. Since the Legislature passed Senate Bill 1235 and the DFPI finalized the Regulations in 2022, the worldwide SBF industry has steadily *grown* by at least five percent annually, with the greatest increase in North America, and is projected to continue growing at similar rates.[50] Notably, last year new e-commerce giants like Amazon and Doordash entered the MCA market, which points to a lack of significant hurdles that regulations like the disclosures pose.[51]

* * *

The regulations represent a reasonable step toward establishing a fairer and more transparent SBF market in California and empowering small business owners with the information they need to avoid predatory financing products and select the most suitable options for their needs. The Department's Regulations provide small business borrowers with accurate, factual, well-understood, and noncontroversial information about the full cost of SBF products. Because they are reasonably related to the state's interest in transparency in the SBF market, are fully justified

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[50] *See* Adroit Market Research, *Merchant Cash Advance Market by Type* (Oct. 2023), https://perma.cc/N5TB-CH2J (documenting growth from 2019 to 2023 and projecting a 5.03 percent growth in the sector over the next decade); Allied Market Research, *Merchant Cash Advance Market Size, Share, Competitive Landscape and Trend Analysis Report* (Apr. 2024), https://perma.cc/5TDP-VEF7 (projecting a 7.2 percent ten-year growth rate).

[51] *See* Press Release, Amazon Launches New Merchant Cash Advance Program Provided by Parafin, Amazon (Nov. 1, 2022), https://perma.cc/642P-H777; Ami Kassar, *DoorDash Is Getting Into the Business of Merchant Cash Advances. Here's the Fine Print*, Inc. (Feb. 22, 2022), https://tinyurl.com/4dtn5rmr.

by the market's problems that predated Senate Bill 235, and do not unduly burden lenders, the disclosures fully satisfy the requirements of the First Amendment.

V. THE REGULATIONS ALSO SATISFY INTERMEDIATE SCRUTINY UNDER *CENTRAL HUDSON*.

Because the Regulations compel only purely factual and uncontroversial information, they need not satisfy a standard more rigorous than the full *Zauderer* test. However, even if this Court were to determine that the required disclosures are for some reason nonfactual or controversial, they would withstand intermediate scrutiny under *Central Hudson*. *See Cal. Chamber of Commerce v. Council for Educ. & Rsch. On Toxics*, 29 F.4th 468, 480 (9th Cir. 2022) (affording the government a "second bite at the apple" under *Central Hudson*); *Spirit*, 687 F.3d at 415 (applying both *Zauderer* and *Central Hudson* and concluding that the Regulation satisfied either test).[52]

The *Central Hudson* test, in the context of compelled disclosures, requires (1) that the government demonstrate a substantial interest, (2) that the disclosure directly and materially advance that interest, and (3) that there be a reasonable fit between the disclosure and the problem to be remedied. *Aargon*, 70 F.4th at 1232.

[52] Should the Court determine *Central Hudson*, not *Zauderer*, applies, it may analyze this matter de novo under that standard. *See Farris v. Seabrook*, 677 F.3d 858, 864 (9th Cir. 2012) (a lower court's application of erroneous legal standard is reviewed de novo); *Prete v. Bradbury*, 438 F.3d 949, 960 (9th Cir. 2006) (in First Amendment cases, constitutional questions of fact are reviewed de novo). Remand is unnecessary. *See NAWG*, 85 F.4th at 1282.

The Regulations meet that standard. First, California has a substantial—indeed, compelling—interest in preventing the deceptive marketing of complex SBF products to small and unsophisticated businesses that are their principal customers. *See Edenfield*, 507 U.S. at 769; *supra* Section III.

Second, the Disclosures directly and materially advance the Department's stated interest in enabling small business borrowers to have "more information about the actual costs and terms of financing . . . and comparison shop," as well as to "[i]ncrease[] protection of businesses seeking commercial financing."[53] The Department's careful analysis, based on studies it conducted and comments it received, plus the significant testimony that the Legislature received in enacting Senate Bills 1235 and 33, sufficiently show that the Regulations effectively advance California's interest in protecting small businesses. *See Pub. Citizen Inc. v. La. Attorney Disciplinary Bd.*, 632 F.3d 212, 221 (5th Cir. 2011) (stating that this element may be satisfied with "empirical data, studies, and anecdotal evidence").[54]

Finally, the Regulations are sufficiently tailored to achieve their objective. To satisfy this prong, the Department need only demonstrate that the disclosures are "in proportion to the interest served." *Aargon*, 70 F.4th at 1234. The Regulations are exactly that. They go no further than to provide small businesses

[53] *Initial Statement of Reasons* at 2.

[54] *See, e.g.*, S.B. 1235 Analysis, at 4-5; *Final Statement of Reasons* at 48.

accurate information they currently lack when comparing an array of financial products. *See Del Webb Comms., Inc. v. Partington*, 652 F.3d 1145, 1153 n.6 (9th Cir. 2011) ("The First Amendment does not prohibit the State from insuring that the stream of commercial information flow cleanly as well as freely"). The Regulations do not prohibit or restrict commercial advertising by lenders. *See Aargon*, 70 F.4th at 1234 (upholding law requiring prior notice of medical debt collection that did not ban or restrict the practice). The Department also carefully chose to require the disclosure of metrics that lenders have demonstrated they already know how to calculate, and it worded the disclosures to make clear that estimated terms are indeed "estimates," and that some variation from actual terms should be expected. *See World Wide Rush, LLC v. City of Los Angeles*, 606 F.3d 676, 687 (9th Cir. 2010) (explaining that this Court's "First Amendment jurisprudence . . . contemplates some judicial deference for a [government's] reasonably graduated response to different aspects of a problem").

Having found that the small business lending market was fraught with confusion and predation, the California Legislature empowered the DFPI to promulgate regulations that made comparison shopping possible. The Department did so, resorting to familiar and standardized financial metrics. The Regulations it promulgated serve a critical public need and square fully with the requirements of the First Amendment.

CONCLUSION

For the foregoing reasons, the judgment of the district court should be affirmed.

Dated: September 20, 2024

Respectfully submitted,

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CERTIFICATE OF SERVICE

I 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. I further certify that all participants in the case are registered CM/ECF users and that service will be accomplished by the appellate CM/ECF system.

Dated: September 20, 2024

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CERTIFICATE OF COMPLIANCE

This brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B) and 9th Cir. R. 32-1 because it contains 6,996 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(f). This brief also complies with the typeface requirements of Fed. R. App. P. 32(a)(5)(A) 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. The text is in 14-point Times New Roman type.

Dated: September 20, 2024

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