UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

FEDERAL TRADE COMMISSION, Plaintiff, v. YELLOWSTONE CAPITAL LLC, *et al*. Defendants.	Case No. 20-cv-6023-LAK

PLAINTIFF'S MEMORANDUM OF LAW IN OPPOSITION TO DEFENDANTS' MOTION TO DISMISS PLAINTIFF'S COMPLAINT

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Plaintiff, the Federal Trade Commission ("FTC" or "Commission"), respectfully submits this opposition to the Motion To Dismiss Plaintiff's Complaint (Dkt. No. 17, together with Defendants' Memorandum in Support of Defendants' Motion to Dismiss, Dkt. 18)[1] filed by Defendants Yellowstone Capital, LLC, Fundry, LLC, Yitzhak D. Stern a/k/a Isaac Stern ("Stern"), and Jeffrey Reece ("Reece," together with Stern, the "Individual Defendants") (collectively, "Defendants").

INTRODUCTION

At a time when small businesses around the country are suffering, Defendants have made their lives worse by making false promises and pocketing unauthorized withdrawals from businesses' bank accounts. The FTC's Complaint alleges that Defendants, who offer short-term, high-cost financing products called "merchant cash advances" ("MCAs"), have falsely claimed that their financing does not require collateral or personal guarantees, despite the routine use of these terms in their contracts and, ultimately, in collection lawsuits (Count I). It further alleges that Defendants' contracts have falsely stated that consumers would receive a specific amount of money, when in fact Defendants first deduct sizable fees from that amount (Count II). And finally, it charges that Defendants have made systematic, unauthorized withdrawals from consumers' bank accounts after they have paid off their financing (Count III). The Complaint alleges that Defendants Stern and Reece, the top executives, controlled, knew of, and, at times, personally participated in this misconduct.

Defendants' actions, as alleged in the Complaint, are textbook deceptive and unfair acts and practices prohibited by Section 5 of the FTC Act, 15 U.S.C. §§ 45(a), (n). The FTC brought

[1] Citations to "Mot." refer to Defendants' memorandum of law, Dkt. 18; "Compl." refers to the Complaint, Dkt. 1; "Zullow Decl." refers to the October 16, 2020 Declaration of Evan R. Zullow submitted concurrently with the filing of this opposition.

this action, pursuant to Section 13(b), 15 U.S.C. § 53(b), to enjoin Defendants from continuing to engage in this conduct, and to obtain monetary relief for their injured consumers. Each of the Complaint's three counts easily satisfies Rule 8's requirements for notice pleading, both on the existence of a violation and on each Defendant's liability for these unlawful practices.

Defendants' Motion relies on a series of objections that lack merit. They incorrectly argue that the FTC cannot employ its broad authority to file this action under Section 13(b), despite the Complaint's allegations that the Commission has reason to believe Defendants are violating or are about to violate the law. They also argue that the FTC is foreclosed from seeking equitable monetary relief, despite acknowledging contrary binding precedent from the Second Circuit, and that the Complaint has not sufficiently pled disgorgement, notwithstanding the Complaint's allegations that Defendants took at least millions of dollars from consumers unlawfully. Accordingly, the Court should deny the Motion to Dismiss.

LEGAL STANDARD

"The standard of review on a motion to dismiss is heavily weighted in favor of the plaintiff." *ESPN, Inc. v. Quiksilver, Inc.*, 586 F. Supp. 2d 219, 224 (S.D.N.Y. 2008) (citation omitted). To survive a motion to dismiss, Rule 8(a) requires only that a complaint allege "enough facts to state a claim to relief that is plausible on its face." *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 570, 127 S. Ct. 1955, 1974 (2007); *see also* Fed. R. Civ. P. 8(a). A claim has facial plausibility when the plaintiff pleads factual content that allows the Court to draw the reasonable inference that the defendant is liable for the misconduct alleged. *Ashcroft v. Iqbal*, 556 U.S. 662, 678, 129 S. Ct. 1937, 1949 (2009).

In deciding a motion to dismiss, "the Court must accept plaintiff's factual allegations as true and draw all reasonable inferences in its favor." *U.S. Bank Nat'l Ass'n v. Ables & Hall Builders*, 582 F. Supp. 2d 605, 608–09 (S.D.N.Y. 2008). The issue on a motion to dismiss is not

whether a plaintiff will ultimately prevail but whether the claimant is entitled to offer evidence to support the claims. *ESPN, Inc.*, 586 F. Supp. 2d at 224 (quoting *Villager Pond, Inc. v. Town of Darien*, 56 F.3d 375, 378 (2d Cir. 1995)).

ARGUMENT

I. EACH COUNT STATES A CLAIM FOR RELIEF UNDER SECTION 5 OF THE FTC ACT.

The FTC's detailed Complaint alleges straightforward claims for deception (Counts I and II) and unfairness (Count III), and that the Individual Defendants are liable for these violations in their individual capacities.

A. The Complaint Describes How Defendants Have Misrepresented that Their Financing Does Not Require Collateral or Personal Guarantees (Count I).

To state a claim that Defendants have engaged in deceptive acts or practices under Section 5(a)(1), "the FTC must show three elements: (1) a representation, omission, or practice, that (2) is likely to mislead consumers acting reasonably under the circumstances, and (3) [that] the representation, omission, or practice is material." *FTC v. Med. Billers Network, Inc.*, 543 F. Supp. 2d 283, 303 (S.D.N.Y. 2008) (citation omitted). A court should focus on the overall impression created by the advertising, not its "literal truth or falsity." *Id.* at 304 (citing *FTC v. Sterling Drug, Inc.*, 317 F.2d 669, 675 (2d Cir.1963)). Additionally, "each representation must stand on its own merit, even if other representations contain accurate, non-deceptive information." *Med. Billers Network*, 543 F. Supp. 2d at 304 (citation omitted). A claim is considered material if it "involves information important to consumers and, hence, is likely to affect their choice of, or conduct regarding a product." *FTC v. Five–Star Auto Club*, 97 F. Supp. 2d 502, 529 (S.D.N.Y. 2000) (citation omitted). "Express representations that are shown to be false are presumed material." *Med. Billers Network*, 543 F. Supp. 2d at 304.

Count I alleges that since at least 2015, in a variety of online, mail, and video advertisements, Defendants have falsely represented that their MCAs require neither collateral nor a personal guarantee. Compl. ¶¶ 15-20. These claims are express on the face of the advertisements themselves, which state, for example: "No collateral loans," *id.* ¶ 16(b); "No collateral required," *id.* ¶ 16(d); "No Personal Guarantee Loans," *id.* ¶ 16(f); and "No Collateral required. No collateral, no personal guarantee," *id.* ¶ 17. *See Five-Star Auto*, 97 F. Supp. 2d at 528 ("It is reasonable to interpret express statements as intending to say exactly what they say.") (citation omitted).

The Complaint alleges that these representations are false, and likely to mislead consumers, because Defendants do require collateral and personal guarantees. Specifically, Defendants require business owners to sign a guarantee holding them personally responsible for the entire funded amount when their businesses default. Compl. ¶ 19; *id.* Ex. J at YEL-0000001554-55. Defendants also require consumers to pledge all of their business property, including all financial accounts, equipment, inventory and other assets, which Defendants' contracts literally refer to as "the Collateral." *Id.* ¶ 19; *id.* Ex. J at YEL-0000001554 ("Security Interest" in assets referred to as "the 'Collateral'"), *id.* ¶ 20. And, as described in the Complaint, Defendants have routinely filed collection lawsuits using the personal guarantees to sue the individual business owners and to seek court orders to seize the collateral consumers pledged. *Id.* ¶ 20. Finally, because Defendants' advertising makes these no-collateral, no-personal guarantee claims expressly, courts presume that they are material to consumers. *Med. Billers Network*, 543 F. Supp. 2d at 304.

Defendants argue that this Court should make a speculative inference in their favor that Rule 12 does not allow—that the expressly false claims shown in the full advertisements

appended to the Complaint[2] are cured by some vague "context" they can neither articulate nor point to on the face of the ads themselves. For example, while they argue that *Sterling Drug*, 317 F.2d at 674, instructs the Court to evaluate the advertisements "in [their] entirely," Mot. at 17, Defendants point to nothing in the full ads themselves that could possibly cure or qualify their express misrepresentations. Instead, Defendants offer facts outside of the Complaint—specifically, the status of their websites *60 days after this lawsuit was filed*, Mot. at 17; Chuk Decl. Ex 2, Dkt. 19-2 (attaching website printouts dated October 2, 2020)—which, of course, tell the Court nothing about the content of these sites before this date.[3] Defendants' other case, *Bel Canto Design Ltd. v. MSS HiFi, Inc.*, No. 11-cv-6353 (CM), 2012 WL 2376466, at *16 (S.D.N.Y. June 20, 2012), does not even involve the FTC Act.[4] Finally, to whatever extent Defendants are alluding to "context" outside of the ads themselves, the law is clear that each of Defendants' misrepresentations "must stand on its own merit." *Med. Billers Network*, 543 F. Supp. 2d at 304 (citation omitted).

[2] Exhibit A reflects all relevant information related to the claims at issue, but is partially excerpted. Should the Court wish to view the full site in its entirety, the internet archive captured the website as of last year, at the following URL: https://web.archive.org/web/20190313234443/http://yellowstonecap.com/ (March 13, 2019 capture of yellowstonecap.com, Ex. A to Complaint).

[3] In fact, archived versions of the websites show that the sites were active and made the same representations alleged in the Complaint. *E.g.*, https://web.archive.org/web/20190608124610/http://sbfcash.com/ (June 8, 2019 capture of sbfcash.com, Ex. D to Complaint). Additionally, Defendants' cases, Mot. at 6 n.3, suggest, at most, that the Court could take Judicial Notice of the fact of the *current* state of the websites, not that these facts can be used to infer how they appeared at prior times.

[4] Additionally, the *Bel Canto* court held that the party alleging a misrepresentation under the Lanham Act failed to provide even the most basic information, including "any allegation of the words Bel Canto used, and where it used them"—for example, whether such claims were made on "the website, in the manual, on the warranty card." *Bel Canto*, 2012 WL 2376466, at *16. In stark contrast, the Complaint here attaches the full advertisements, and the Court can see the exact language that Defendants used, where they used it, and that they do not qualify their "no collateral" and "no personal guarantee" representations.

B. The Complaint Describes How Defendants Have Misrepresented that Consumers Will Receive a Specific Amount of Financing (Count II).

Count II similarly states a claim for deception under Section 5 of the FTC Act. The Complaint alleges that Defendants represented to consumers on the first page of their contract the essential bargain: Defendants promise to provide consumers a specific amount of money (the Purchase Price), and, in exchange, consumers pay back a larger amount (the Purchased Amount). Compl. ¶¶ 22, 23. The Complaint excerpts the relevant line from Defendants' contracts:

PURCHASE PRICE:	SPECIFIED PERCENTAGE:	PURCHASED AMOUNT:
$10,000	25%	$14,000

Id. ¶ 23.

In fact, as detailed in the Complaint, this representation is false, and likely to mislead consumers, because Defendants provide consumers with significantly smaller amounts than the promised Purchase Price. *Id.* ¶ 25. Defendants instead withhold substantial fees off the top of that amount for a variety of charges, often amounting to hundreds or thousands of dollars. *Id.* Defendants reference fees in an Appendix several pages into the contract, *id.* Ex. J at YEL-0000001556, but the contract does not explain anywhere that these fees will be subtracted from the Purchase Price amount promised to consumers. *Id.* ¶ 25.

As with Count I, Defendants' misrepresentations here are express, and thus are presumed to be material. *Med. Billers Network*, 543 F. Supp. 2d at 304. Moreover, Defendants misrepresent the essence of their bargain with consumers—how much money consumers will receive—and thus these claims are material for that additional reason. *See Five-Star Auto*, 97 F. Supp. 2d at 529 ("[T]he promises of receiving a free car and earning money were at the heart of marketing the Five Star scheme.").

In their Motion, Defendants point to "a fee schedule" that they claim outlines "applicable fees," Mot. at 18—which the Complaint references, Compl. ¶ 25; but subsequent and vague disclaimers cannot cure a false claim prominently made. *See FTC v. Cyberspace.Com LLC*, 453 F.3d 1196, 1200 (9th Cir. 2006); *FTC v. Brown & Williamson Tobacco Corp.*, 778 F.2d 35, 42-43 (D.C. Cir. 1985). Moreover, as the Complaint explains, Compl. ¶ 25, the fee schedule is itself hardly clear: it does not state that these substantial fees will be subtracted from the Purchased Amount. Compl. Ex. J at YEL-0000001556. Additionally, for some of the large fees, the fee schedule does not even state the specific amount consumers will be obligated to pay. *Id.* (Listing "ACH Program Fee" as a range of "$395.00 or up to 10% of the funded amount," and additional "Bank Fee" as "$195.00 or up to 10% of the funded amount").[5] Finally, Defendants ask rhetorically where else the fees could come from, if not withheld from the Purchase Price, Mot. at 19, but ignore that consumers could have reasonably believed that the fees were baked into the "Purchased Amount" to be repaid over time. In any event, Defendants ask the Court to make inferences in their favor, which Rule 12(b)(6) bars.

C. The FTC's Complaint States a Claim for Unfairness Under the FTC Act Based on Defendants' Unauthorized Withdrawals (Count III).

Count III states a claim for unfairness under the FTC Act by alleging that Defendants made systematic, excess withdrawals from consumers' bank accounts without authorization. Courts regularly conclude that charging or billing consumers without authorization is an unfair practice. *See FTC v. Crescent Publ'g Grp., Inc.*, 129 F. Supp. 2d 311, 322 (S.D.N.Y. 2001); *see*

[5] Accordingly, the mere fact that the first page of Defendants' contract vaguely states "[a] list of all fees applicable under this agreement is annexed hereto in Appendix A" does not resuscitate the contract's complete failure—in the signed Appendix or elsewhere—to inform consumers of the exact amount of the fees or that these fees will be withheld from the promised financing amount.

also, e.g., FTC v. Amazon.com, Inc., No. C14-1038-JCC, 2016 WL 10654030, at *8 (W.D. Wash. July 22, 2016) (collecting cases).

A practice is unfair under the FTC Act if (1) it causes or is likely to cause substantial injury to consumers, (2) which is not reasonably avoidable, and (3) is not outweighed by any countervailing benefits to consumers or competition. 15 U.S.C. § 45(n); *see also FTC v. Verity Int'l, Ltd.*, 124 F. Supp. 2d 193, 203 (S.D.N.Y. 2000). The FTC has satisfied each element.

1. The Complaint Alleges that Defendants' Unauthorized Withdrawals Have Caused Substantial Injury to Consumers.

Courts measure injury "in the aggregate," and hold that substantial injury includes small injuries to a large number of consumers. *Crescent Publ'g Grp., Inc.*, 129 F. Supp. 2d at 322 & n.70; *see also, e.g., FTC v. J.K. Publ'ns*, 99 F. Supp. 2d 1176, 1201 (C.D. Cal. 2000) (citing *American Fin. Services Ass'n v. FTC*, 767 F.2d 957, 973 (D.C. Cir. 1985), *cert. denied*, 475 U.S. 1011, 106 S.Ct. 1185 (1986)). Here, the Complaint alleges that Defendants have caused substantial injury to consumers through their "typical" practice, across all consumers, of withdrawing at least an extra 4-5 daily installment payments after consumers have paid off their financing. Compl. ¶¶ 29, 30, 31. It alleges that these unauthorized withdrawals typically total hundreds or thousands of dollars per consumer, *id.* ¶¶ 29, 35—resulting in at least millions of dollars in aggregate injury. *Id.* ¶ 35. Additionally, the Complaint alleges that Defendants unauthorized withdrawals sometimes exceeded the typical 4-5 days of overcollections. *Id.* ¶ 32. Consumers suffered additional harms, as unsuspecting consumers have been subject to significant overdraft fees when Defendants took funds from them. *Id.* ¶ 33.[6] To the extent that Defendants ever refund these sums to their consumers, they sometimes only do so if consumers

[6] Defendants argue that the contract waived responsibility for any overdraft fees, but that is only for "debiting the specified amounts under the terms of this agreement." Mot. at 9; Compl. Ex. J at YEL-0000001549. Because these additional withdrawals are not authorized, they plainly are not "under the terms of the agreement."

complain and, even then, sometimes take weeks or months to provide refunds. *Id.* ¶ 34; *see also Amazon*, 2016 WL 10654030, at *8 ("the time spent seeking refunds" is a relevant injury).

Defendants throw numerous arguments at these allegations, but none stick. They first quibble with the Complaint's wording, incorrectly suggesting that it alleges unauthorized withdrawals only "in numerous instances." Mot. at 22. In making this argument, however, Defendants ignore that the Complaint specifically alleges aggregate injury ("at least millions of dollars," Compl. ¶ 35), the number of consumers injured ("at least thousands of them," *id.* ¶ 29), the injury typically suffered by each consumer ("amounts ranging from hundreds to thousands of dollars," *id.*), and the fact that these overcollections represented the "typical" consumer experience. *Id.*

Defendants next ask the Court to make factual inferences in their favor, which Rule 12 bars. They argue that the Complaint fails to plead that these unauthorized withdraws were not refunded, Mot. at 22, but that is plainly wrong: the Complaint alleges that Defendants commonly pocketed these unauthorized withdrawals *permanently*. When detailing the consumer injury associated with this practice, the Complaint mentions the possibility of refunds only once—and, even then, to note that "[t]o the extent Defendants refund these unauthorized debits, in numerous instances, *they do so only in response to complaints from customers*." Compl. ¶ 34 (emphasis added). The time seeking refunds is, in any event, a relevant injury. *Amazon*, 2016 WL 10654030, at *8.

Defendants further contend that any overcollections were authorized, but no provision of the contract cited by Defendants in their Motion, Mot. at 21-22, alerts consumers to these systematic unauthorized withdrawals or secures their authorization for them. To the contrary, as the Complaint alleges, Compl. ¶¶ 23-24, the contract specifies a set amount consumers agree to

pay (the Purchased Amount), and Defendants' after-the-fact, strained interpretation of the terms "delivered" and "receives" cannot overcome this allegation. Mot. at 21. Indeed, other language in the contract shows that Defendants were authorized to take only "specified amounts under the terms of the agreement"; and the agreement itself defines the "Purchased Amount" as "the amount specified below"—the "$14,000" in the Complaint's example. Compl. ¶¶ 23-24; *id*. Ex. J at YEL-0000001549. Thus, consumers could hardly have expected that Defendants would take the amount specified in the contract, plus additional payments for an undefined length of time. *See Crescent Publ'g*, 129 F. Supp. 2d at 322 (unclear disclosures did not permit defendant to charge consumers at the end of a "free trial"). Moreover, Defendants certainly do not contend that these contract provisions allow them to keep unauthorized payments for themselves—as the FTC alleges Defendants did. They instead suggest that these overcollections are refunded, Mot. at 22, but nothing in the Complaint suggests that refunds occurred in the typical case.

Finally, Defendants suggest that there were no overcollections at all because, they contend, their contracts allow them to collect various additional fees from consumers on top of the Purchased Amount. Mot. at 23. However, the Complaint certainly does not allege that Defendants' overcollections could be accounted for by fees. Instead, the Complaint alleges that the only typical practice was Defendants' overcollections. Compl. ¶ 29.

2. The Complaint Alleges that the Injury Caused by Defendants' Unauthorized Withdrawals Is Not Reasonably Avoidable by Consumers.

The Complaint alleges facts sufficient to show that consumers could not reasonably avoid Defendants' overcollections. Because consumers never authorized these extra withdrawals, they have no reason to expect or avoid them. *FTC v. Inc21.com Corp.*, 745 F. Supp. 2d 975, 1004 (N.D. Cal. 2010), *aff'd*, 475 F. App'x 106 (9th Cir. 2012) ("the burden should not be placed on defrauded customers to avoid charges that were never authorized to begin with") (citing *Crescent*

Publ'g, 129 F. Supp. 2d at 322). Even then, consumers have no mechanical way to stop these overcollections because Defendants control when they make ACH debits on consumer accounts. Compl. ¶¶ 31, 33.

Defendants suggest that consumers could have requested one-off exceptions to their systematic overcollections. Mot. at 25. But that argument ignores the fact that consumers have no reason to expect this practice in the first place and thus would have "first to suffer an injury and then to find and implement a solution to avoid being injured again." *FTC v. Verity Int'l, Ltd.*, 335 F. Supp. 2d 479, 499 (S.D.N.Y. 2004).[7]

3. The Complaint Alleges No Countervailing Benefits to Defendants Taking Unauthorized Withdrawals from Consumers.

Defendants' unauthorized withdrawals detailed in the Complaint provide no countervailing benefits to their consumers. Indeed, taking money without authorization is a quintessential unfair practice. *See Amazon*, 2016 WL 10654030, at *8; *Inc.21 Corp.*, 745 F. Supp. 2d at 1004. Whatever "convenience to merchants of automated withdrawals" Defendants wish to provide, Mot. at 25, they can easily do so by lawfully obtaining consumers' proper authorization. *See Amazon*, 2016 WL 10654030, at *10 ("the 'benefit' of ensuring a streamlined experience is not incompatible with the practice of affirmatively seeking a customer's authorized consent to a charge").

D. The Complaint Alleges Facts Sufficient For Individual Liability.

Individuals are liable for unfair or deceptive conduct under the FTC Act if "(1) [they] participated directly in the wrongful acts or practices or . . . had the authority to control the

[7] For example, the Defendants allude to one consumer in the FTC's Complaint as a success story, because that consumer complained *after overcollections were already taken* and secured an "exception" from Defendants' typical practice of taking even more unauthorized payments. Mot. at 25 (citing Compl. ¶ 31). Of course, even this consumer had "first to suffer an injury and then implement a solution." *Verity*, 335 F. Supp. 2d at 499.

corporate defendants; and (2) [they] had some knowledge of the acts or practices." *FTC v. Tax Club, Inc.*, 994 F. Supp. 2d 461, 471 (S.D.N.Y. 2014) (quoting *Five-Star Auto*, 97 F. Supp. 2d at 535). As a result, the FTC need not allege that each individual engaged in each unlawful practice in the Complaint – but only that those individuals "had the authority to control the corporate defendants" and "had some knowledge" of the unlawful activity. *Tax Club, Inc.*, 994 F. Supp. 2d at 471 (citation omitted). Additionally, "[t]he FTC need not establish in this context that the defendant had actual and explicit knowledge of the particular [unlawful conduct] at issue," but instead that defendants were "recklessly indifferent," or had an "awareness of a high probability of [unlawfulness] and intentionally avoided learning of the truth." *FTC v. Moses*, 913 F.3d 297, 307 (2d Cir. 2019) (citations omitted). Finally, "[a]n individual's degree of participation in business affairs is probative of knowledge." *Med. Billers Network*, 543 F. Supp. 2d at 320. The Complaint in this case easily satisfies the standard for individual liability under the FTC Act.

First, the Complaint alleges facts sufficient to show that Stern and Reece are key principals who have closely managed and controlled Defendants' business operations at issue in the Complaint. It alleges that Stern is a founder, and the CEO, of the Corporate Defendants, Compl. ¶ 8, and that Reece is their President, *id*. ¶ 9. The Complaint also alleges that Stern and Reece have "formulated, directed, controlled, had the authority to control, or participated in the [unlawful] acts and practices." *Id*. ¶¶ 8-9. Further, as alleged, Stern and Reece have directly managed Defendants' relevant marketing agents, *id*. ¶ 20, as well as Defendants' servicing and payment collection operations that are associated with the unauthorized withdrawals in this case. *Id*. ¶ 36.

Second, the Complaint details specific facts sufficient to reasonably infer that the Individual Defendants not only had control over the unlawful practices, but also that they specifically knew about and participated in the law violations in this case. In connection with Count I, for example, the Complaint details that they have "closely overseen and directed Defendants' day-to-day advertising and marketing efforts," "frequently reviewed and provided feedback and approval for advertising content and claims," and "specifically reviewed copies of advertisements that claim the Defendants do not require collateral." *Id*. ¶ 20. In connection with Count II, the FTC alleges that Stern and Reece have received messages detailing the difference between the amount promised to consumers and the significantly lower amount disbursed to consumers after fees were withheld. *Id*. ¶ 26. In connection with the systematic overcollections alleged in Count III, the Complaint states that they have "directly supervised their in-house servicers and disseminated relevant policies and practices to them," and "have known about, and communicated with their in-house servicers about, the existence of unauthorized overpayments by consumers." *Id*. ¶ 36. Additionally, if there is any remaining doubt as to whether the Individual Defendants had knowledge of their unlawful practices, Defendants admit that they were alerted to the possible illegality of these practices nearly two years ago, when the FTC began its investigation, and yet they persisted in this conduct. *See* Zullow Decl. Ex. 2 (Joint Rule 26(f) Report, Dkt. 16, at 8) (Defendants stating that the FTC engaged in a "nearly two-year pre-suit investigation"); Mot. at 5 (stating that there was a "lengthy civil investigation").[8]

Defendants' cases in support of their Motion are unavailing. For example, unlike *FTC v. Swish Marketing*, No. 09-cv-03814 (RS), 2010 WL 653486, at *5 (N.D. Cal. Feb. 22, 2010), the

[8] The Court may take Judicial Notice of the parties' Rule 26(f) report, because it is a public court filing. *See Purjes v. Plausteiner*, No. 15-cv-2515 (VEC), 2016 WL 552959, at *4 (S.D.N.Y. Feb. 10, 2016) ("The Court may take judicial notice of filings in state or federal court").

Complaint here does not merely allege that Stern and Reece are liable because of their "status as CEO [and President], standing alone," *id.*, but instead specifically describes their direct management and control of marketing, servicing and collections. Compl. ¶¶ 20, 36. Additionally, although Stern's and Reece's relevant roles and responsibilities are "probative of knowledge," *Med. Billers*, 543 F. Supp. 2d at 320, the Complaint does not rest on describing them. To the contrary, unlike in *FTC v. Quincy Bioscience Holding Co.*, 389 F. Supp. 3d 211, 221 (S.D.N.Y. 2019), on which Defendants rely, Mot. at 27, the Complaint details the ways Stern and Reece specifically knew about and participated in the unlawful conduct. For example, they have reviewed ads that made no-collateral claims (the subject of Count I), have received messages detailing the difference between the amount falsely promised to consumers and the significantly-lower amount disbursed to them (Count II), and that they have known about, and communicated with their in-house servicers about, the unauthorized withdrawals (Count III). *See Tax Club, Inc.*, 994 F. Supp. 2d at 473 (concluding that complaint "goes far beyond conclusory allegations ... and general allegations of knowledge" by alleging only that individual defendants had at least twice discussed consumer complaints and chargebacks) (citations omitted). Thus, the Complaint states a claim for individual liability.

II. DEFENDANTS' OTHER ARGUMENTS FAIL

Defendants raise several other arguments for dismissal, but each is equally meritless. First, the FTC has alleged that it has reason to believe that Defendants are violating or are about to violate the FTC Act, notwithstanding Defendants' strained emphasis on the Complaint's use of particular verb tenses. Second, binding Second Circuit precedent allows the FTC to obtain ancillary relief for violations of Section 5. Finally, the FTC has pled sufficient facts to warrant disgorgement.

A. The FTC Has Reason to Believe that Defendants Are Violating or Are About to Violate the Law.

Defendants wrongly argue that the FTC's Complaint does not meet its minimal burden under Section 13(b) of the FTC Act, 15 U.S.C. § 53(b). Under Section 13(b), the FTC need only allege that it "has reason to believe" that Defendants are violating or about to violate the law. And the Complaint alleges a catalogue of facts sufficient to show that the Commission has reason to believe Defendants are violating the FTC Act through ongoing conduct, or, at the very least, that they are about to violate the law—given the high likelihood of recurrence. Thus, it properly brought this lawsuit using its broad authority.

1. The FTC Need Only Allege that the Commission "Has Reason to Believe" that the Defendants Are Violating or Are About to Violate the FTC Act.

Section 13(b) of the FTC Act sets forth a lenient standard—authorizing the FTC to file suit in federal district court in any matter where, at the time of filing, it "has reason to believe" that a defendant "is violating, or is about to violate" Section 5 of the Act. *See FTC v. Vyera Pharm*., LLC, No. 20-cv-706-DLC, ___ F. Supp. 3d ____, 2020 WL 4891311, at *6 (S.D.N.Y. Aug. 18, 2020) (denying motion to dismiss where FTC alleged "reason to believe" that the defendants were engaged in ongoing violations). The relevant portion of Section 13(b) reads as follows:

> Whenever the Commission *has reason to believe*—
>
> (1) that any person, partnership, or corporation *is violating, or is about to violate, any provision of law* enforced by the Federal Trade Commission, and
>
> (2) that the enjoining thereof pending the issuance of a complaint by the Commission and until such complaint is dismissed by the Commission or set aside by the court on review, or until the order of the Commission made thereon has become final, would be in the interest of the public—
>
> the Commission . . . may bring suit in a district court of the United States to enjoin any such act or practice.

15 U.S.C. § 53(b) (emphasis added).

Courts interpreting this statutory language have read the FTC's authority broadly. Some courts have held that the FTC's determinations on "reason to believe" are unreviewable because this language provides no meaningful judicial standards, or would require probing the minds of the Commissioners collectively.[9] Other courts have held that only a limited judicial review is necessary to confirm that the Commission made a "reason to believe" determination.[10] Regardless, under Rule 12(b)(6), at most the FTC must allege facts sufficient to infer that the Commission has a "reason to believe" the Defendants are violating or are about to violate the FTC Act. *See Vyera*, 2020 WL 4891311, at *6. The Complaint easily does so in this case.

2. The Complaint Alleges that Defendants Are Violating the Law.

First, the Complaint satisfies the "is violating"-prong of Section 13(b) because, like *Vyera*, it alleges facts sufficient to show that "as of the time it filed this lawsuit, the FTC had reason to believe that the defendants were at that very moment actively engaged" in violating the FTC Act. *See Vyera*, 2020 WL 4891311, at *6.[11] In the recent *Vyera* decision, the court denied

[9] *See FTC v. Nat'l Urological Grp., Inc.*, No. 1:04-cv-3294-CAP, 2006 WL 8431977, at *5 (N.D. Ga. Jan. 9, 2006) (holding judicial review "impossible" because Section 13(b) provides "no meaningful standard by which to measure the lawfulness of the FTC's actions"); *Boise Cascade Corp. v. FTC*, 498 F. Supp. 772, 779 (D. Del. 1980) (judicial review of FTC reason to believe determination under the FTC Act would require the court to "probe [the Commissioners] mental processes, a practice condemned by the Supreme Court").

[10] *See AMREP Corp. v. FTC*, 768 F.2d 1171, 1177 (10th Cir. 1985) ("All that the law requires is that the FTC actually had some 'reason to believe'"); *Standard Oil Co. of Cal. v. FTC*, 596 F.2d 1381, 1386 (9th Cir. 1979), *rev'd on other grounds*, 449 U.S. 232, 101 S. Ct. 488 (1980) (courts should not disturb the agency's reason to believe determination unless "the complaint was issued solely because of some outside pressure or with complete absence of a 'reason to believe' determination"). Although the Supreme Court reversed the Ninth Circuit's holding that issuance of the administrative complaint was final agency action under Administrative Procedure Act, it expressly reserved decision on the scope of judicial review that is not governed by the APA. 449 U.S. at 245 n.13, 101 S. Ct. at 496 n.13.

[11] Under a tolling agreement between the parties, *see* Zullow Decl. Ex. 1, Defendants waived their right to assert that they are not violating or not about to violate the FTC Act even if they had ceased their ongoing conduct after the tolling date—April 27, 2020. The Court may take Judicial Notice of this agreement. *See, e.g., Walker v. Deutsche Bank Nat'l Tr. Co. for Morgan Stanley Loan Tr. 2005-11AR*, No. 3:16-CV-697(AWT), 2017 WL 1115201, at *5 (D.

defendants' motion to dismiss on this issue, because the FTC alleged that unlawful conduct was ongoing when it filed its lawsuit. *Id.*; *see also In re Sanctuary Belize Litig.*, No. 18-cv-3309-PJM, ___ F. Supp. 3d ____, 2020 WL 5095531, at *57 (D. Md. Aug. 28, 2020) (inquiring whether, "at the time of filing," defendant was violating or about to violate the law). The Complaint here alleges the same—for example, that:

- "Defendants engage in a pattern of deceptive and unfair conduct in connection with the marketing, advertising, and offering of their MCAs." Compl. ¶ 14.
- "Since at least 2015, Defendants have disseminated advertisements that claim that their MCAs do not require collateral or a personal guarantee." *Id.* ¶ 15.
- "Defendants' video advertisements also represent that Defendants do not require collateral or personal guarantees." *Id.* ¶ 17.
- "Since at least 2015, Defendants have withdrawn money from customers' accounts in excess of the amounts customers authorized, by continuing to withdraw daily payments from customers after they have already fully repaid the 'Purchased Amount.'" *Id.* ¶ 29.
- "[C]ustomers each typically pay hundreds (and sometimes thousands) of dollars in these excess, unauthorized payments." *Id.* ¶ 35.
- "Consumers are suffering ... and will continue to suffer substantial injury as a result of Defendants' violations of the FTC Act.... Absent injunctive relief by this Court, Defendants are likely to continue to injure consumers, reap unjust enrichment, and harm the public interest." *Id.* ¶ 50.

The Complaint's frequent use of the present tense, of course, alleges ongoing conduct. Compl. ¶¶ 12 – 14, 16, 17, 19–20, 25, 27, 28, 33, 34, 35. Defendants take issue with the Complaint's use of the "present perfect" verb tense, Mot. at 14-15, but both the Second Circuit and the Chicago Manual of Style make clear that the present perfect can refer to "a past action that has continuing relevance—that 'comes up to and touches the present.'" *Dobrova v. Holder*, 607 F.3d 297, 301-02 (2d Cir. 2010) (quoting Chicago Manual of Style ¶ 5.119 (15th ed. 2003)). The Complaint further emphasizes the ongoing nature of Defendants' conduct by adding phrases

Conn. Mar. 24, 2017).

such as "[s]ince at least 2015." In any event, in other recent cases, courts have declined to dismiss FTC complaints when there is any dispute about whether illegal conduct was ongoing at the time of suit. *See FTC v. Educare Centre Servs*., Inc., 433 F. Supp. 3d 1008, 1016-17 (W.D. Tex. 2020) (declining to dismiss where there is factual dispute about whether conduct had actually stopped before FTC's lawsuit); *In re Sanctuary Belize Litig*., Civil No. PJM 18-3309, 2019 WL 4243079 (D. Md. Sept. 5, 2019) (declining to dismiss case where existence of ongoing or future conduct was disputed). Therefore, Defendants' arguments are unavailing.

3. The Complaint Also Alleges that Defendants Are About to Violate the Law.

Even assuming, *arguendo*, that Defendants' unlawful conduct was not ongoing,[12] the Complaint alleges facts sufficient to show that the FTC has reason to believe Defendants are "about to violate" the FTC Act, because there is a "realistic likelihood of recurrence." *See SEC v. Commonwealth Chem. Sec*., 574 F.2d 90, 98-99 (2d Cir. 1978); *see also, e.g., SEC v. Opulentica, LLC*, 479 F. Supp. 2d 319, 329 (S.D.N.Y. 2007) (applying same standard). In *Commonwealth Chemical*, the Second Circuit considered language in the Securities Exchange Act of 1934 which, almost identically to the FTC Act, authorizes injunctions against a defendant who "is engaged or about to engage" in unlawful conduct.[13] The defendants in that case argued that an injunction was improper because the SEC had sued them 15 months after their last violation, and because they had "voluntarily terminated all connection with [the securities

[12] Contrary to the Defendants' arguments, *see* Mot. at 14, the FTC plausibly alleges that the relevant conduct associated with Count II continued beyond October 2018, even if it ceased before this lawsuit—it took place "[s]ince at least early 2015 *until at least* October 2018," Compl. ¶ 22 (emphasis added). In any event, any reasonable inference should be made in the FTC's favor.

[13] *Compare* 15 U.S.C. § 78u(d)(1) ("Whenever it shall appear to the Commission that any person *is engaged or is about to engage in* acts or practices constituting a violation of any provision of this chapter … it may in its discretion bring an action in the proper district court of the United States, the United States District Court for the District of Columbia, or the United States courts of any territory or other place subject to the jurisdiction of the United States, to enjoin such acts or practices …." (emphasis added)).

business].” *Id*. at 98. The Second Circuit rejected that argument, holding that “[e]xcept for the case where the SEC steps in to prevent an ongoing violation,” the “is . . . or about to” language “seems to require a finding of likelihood or propensity to engage in future violations”—*i.e.*, a “realistic likelihood of recurrence.” *Id*. at 99 (citations omitted).

Additionally, courts in this Circuit look to the following factors to determine whether there is a realistic likelihood of recurrence: (1) “whether the infraction is an isolated occurrence”; (2) “the degree of scienter involved”; (3) “whether defendant continues to maintain that his past conduct was blameless”; and (4) “whether, because of his professional occupation, the defendant might be in a position where future violations could be anticipated.” *Commonwealth Chem.*, 574 F. 2d at 100; *Opulentica*, 479 F. Supp. 2d at 329.

The Complaint here alleges facts to support a realistic—in fact, a very high—likelihood of recurrence: First, the FTC alleges that Defendants’ law violations are far from an “isolated occurrence,” but instead a longstanding “pattern.” Compl. ¶ 14. Second, the Complaint alleges that the Defendants had knowledge of the unlawful conduct at issue in this case. *Id.* ¶¶ 20, 26, 30-31, 36. Additionally, as their Motion makes clear, Defendants purport to be “blameless” for their law violations. *Commonwealth Chem.*, 574 F. 2d at 100. Finally, the Complaint alleges that the Defendants are continuing to promote and offer their financing products to consumers—leaving them well-positioned to continue or resume their longstanding pattern of FTC Act violations. Compl. ¶¶ 12-13; *see also Commonwealth Chem.*, 574 F. 2d at 100.

4. *Shire* Is Not the Law of the Second Circuit and, Regardless, Is Distinguishable from this Case.

Defendants ignore long-standing Second Circuit precedent to argue that the Third Circuit’s decision in *FTC v. Shire ViroPharma*, 917 F.3d 147 (3d Cir. 2019), requires a showing of “imminent” violations in this case to establish that such violations are “about to” occur. Mot.

at 12-15. In fact, as detailed above, the Second Circuit in *Commonwealth Chemical* held that the government need show only a "realistic likelihood of recurrence." *Commonwealth Chem.*, 574 F.2d at 99.

Additionally, the facts of the *Shire* case are clearly distinguishable from this one. In *Shire*, the court held that the FTC did not meet the "is violating" or "is about to violate" standard where *five years* had elapsed since the defendant stopped its unlawful conduct, and where the defendant had divested itself from the product at issue in the case. *See Shire*, 917 F.3d at 159-60. Here, the FTC plausibly alleges that Defendants were violating or about to violate the FTC Act at the time it filed this action and, in further contrast with *Shire*, that the Defendants continue to offer their financing products to consumers. *See Vyera*, 2020 WL 4891311 at *6-7. Defendants fail to point to anything in the record that can overcome these plausible allegations.[14]

B. Section 13(b) of the FTC Act Allows the FTC to Obtain Equitable Monetary and Other Ancillary Relief, as the Second Circuit Has Held.

Defendants argue that the FTC cannot obtain any "ancillary relief"—including equitable monetary relief—"other than injunctive relief under Section 13(b)," Mot. at 28, but the Second Circuit has expressly rejected this argument, *FTC v. Bronson Partners, LLC*, 654 F.3d 359, 365-66 (2d Cir. 2011). Section 13(b) of the FTC Act provides "[t]hat in proper cases the Commission may seek, and after proper proof, the court may issue, a permanent injunction." 15 U.S.C. § 53(b). In *Bronson Partners*, the Second Circuit held that this language "permits courts to grant ancillary equitable relief, including equitable monetary relief." *Id.* The Second Circuit is far from alone in this holding—the overwhelming majority of Circuits hold that the FTC may seek equitable monetary relief under Section 13(b). *See FTC v. Direct Mktg. Concepts, Inc.*, 624

[14] For example, Defendants misplace great weight on their claim that the online advertisements cited in the Complaint were purportedly inactive on October 2, 2020—nearly *two months after this action was filed*. Mot. at 6, 14.

F.3d 1, 15 (1st Cir. 2010); *FTC v. Ross*, 743 F.3d 886, 890-892 (4th Cir. 2014); *FTC v. Sw. Sunsites, Inc.*,665 F.2d 711, 717-18 (5th Cir. 1982); *FTC v. Sec. Rare Coin & Bullion Corp.*, 931 F.2d 1312, 1314–15 (8th Cir. 1991); *FTC v. Pantron I Corp.*, 33 F.3d 1088, 1102 (9th Cir. 1994); *FTC v. Freecom Commc'ns, Inc.*, 401 F.3d 1192, 1202 n. 6 (10th Cir. 2005); *FTC v. Gem Merch. Corp.*, 87 F.3d 466, 468-69 (11th Cir. 1996); *contra FTC v. Credit Bureau Center, LLC*, 937 F.3d 764, 767 (7th Cir. 2019), *cert. granted* 2020 WL 3865251 (U.S. July 9, 2020); *FTC v. AbbVie Inc.*, ___ F.3d ___, 2020 WL 5807873 (3d Cir. 2020).

District courts within the Second Circuit are, of course, bound by the Second Circuit's rulings. *Dennis v. JPMorgan Chase & Co.*, 439 F. Supp. 3d 256, 263 (S.D.N.Y. 2020) ("But the Second Circuit clearly has rejected this view….The Court is bound by this precedent."). Defendants argue that the Court nonetheless should disregard *Bronson Partners* because of the Second Circuit's single citation to the then-governing Seventh Circuit precedent. Mot. at 31. But that hardly shakes "the very foundation" of *Bronson Partners*'s holding—the court also cited cases from the Fifth, Eighth, Ninth, Tenth, and Eleventh Circuits. 654 F.3d at 365. Indeed, the "foundation" of *Bronson*'s holding was the Supreme Court's decision in *Porter v. Warner Holding Co.*, 328 U.S. 395, 66 S. Ct. 1086 (1946). *Bronson Partners*, 654 F.3d at 365-66; *cf. Liu v. SEC*, 140 S. Ct. 1936, 1943 (2020) (citing *Porter*). The Supreme Court will soon decide whether Section 13(b) permits the FTC to obtain monetary relief, *see AMG Capital Mgmt. v. FTC*, No. 19-508 (U.S.), but *Bronson Partners* is controlling on this issue until then and precludes dismissal at this time.

C. The Complaint's Request for Disgorgement Is Appropriate.

Defendants conclude with a plea to strike one particular form of ancillary relief—disgorgement—mentioned in the Complaint's prayer for relief. Mot. at 32. The Second Circuit, however, has held that Section 13(b) of the FTC Act permits the FTC to seek equitable monetary

relief, *Bronson Partners*, 654 F.3d at 369-70, and the Supreme Court's recent decision in *Liu* made clear that disgorgement is an equitable remedy. 140 S. Ct. at 1940.

Defendants counter that the Complaint does not sufficiently allege that Defendants have "received and retained" "ill-gotten monies," Mot. at 33, but that is of course incorrect. At the outset, the FTC is "not required to identify in its complaint the precise amount of disgorgement … sought." *SEC v. Payton*, No. 14-cv-4644-JSR, 2016 WL 3023151, at *3 (S.D.N.Y. May 16, 2016), *aff'd*, 726 F. App'x 832 (2d Cir. 2018) (collecting cases). In any event, the Complaint alleges that Defendants made material misrepresentations in connection with marketing and selling their MCAs, Compl. ¶¶ 15-20 (collateral and personal guarantees); *id.* ¶¶ 21-27 (specific amount of funding to be received), resulting in consumers agreeing to pay money to Defendants, *e.g.*, *id.* ¶ 23 (consumers pay Defendants more than they receive). The Complaint also alleges that Defendants took unauthorized payments from consumers worth at least millions of dollars. *Id.* ¶¶ 28-35. Defendants' curious suggestion that they might not have actually received or retained this money seems unlikely, Mot. at 33. But ultimately their assertion—that Defendants did not keep and retain any of the money they took from their consumers—simply asks the Court to make inferences in their favor, which Rule 12(b)(6) prohibits. As in *Vyera*, the Complaint "provides sufficient notice to [Defendants] of the [FTC's] claims against them, as well as the [FTC's] requested relief." 2020 WL 4891311, at *13.

CONCLUSION

For the foregoing reasons, the Court should deny Defendants' Motion to Dismiss.

Dated: October 16, 2020

Respectfully submitted,

/s/ Evan R. Zullow

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CERTIFICATE OF SERVICE

I, Evan R. Zullow, hereby certify that on October 16, 2020, I electronically filed the foregoing Plaintiff's Memorandum of Law in Opposition to Defendants' Motion to Dismiss Plaintiff's Complaint with the Clerk of the Court using its CM/ECF system, which will send notification of such filing to all counsel of record.

/s/ Evan R. Zullow
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