No. 15-15873

In the United States Court of Appeals for the Ninth Circuit

ITALIAN COLORS RESTAURANT; ALAN CARLSON; STONECREST GAS & WASH; SALAM RAZUKI; LAURELWOOD CLEANERS, LLC; JONATHAN EBRAHIMIAN; LEON'S TRANSMISSION SERVICE, INC.; VINCENT ARCHER; FAMILY LIFE CORPORATION, doing business as Family Graphics; TOSHIO CHINO,
Plaintiffs-Appellees,

v.

KAMALA D. HARRIS,
in her official capacity as Attorney General of the State of California,
Defendant-Appellant.

On Appeal from the United States District Court
for the Eastern District of California (The Honorable Morrison C. England, Jr.)

BRIEF FOR PLAINTIFFS-APPELLEES

Mark Wendorf
REINHARDT, WENDORF & BLANCHFIELD
332 Minnesota Street
St. Paul, MN 55101
(651) 287-2100

Deepak Gupta
Jonathan E. Taylor
GUPTA WESSLER PLLC
1735 20th Street, NW
Washington, DC 20009
(202) 888-1741
deepak@guptawessler.com

Kevin K. Eng
MARKUN ZUSMAN FRENIERE & COMPTON LLP
465 California Street, 5th Floor
San Francisco, CA 94101
(415) 438-4515

Counsel for Plaintiffs-Appellees

CORPORATE DISCLOSURE STATEMENT

None of the plaintiffs-appellees has a corporate parent, and no publicly held corporation owns any stock in any of the plaintiffs-appellees.

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INTRODUCTION

Each time a consumer pays with a credit card, the merchant incurs a "swipe fee." These fees are typically passed on to all consumers through higher prices. But, if a merchant chooses, it may instead pass on the cost only to those customers who pay with credit cards. It may accomplish this by charging two prices: a higher price for those who pay with credit and a lower one for those who pay in cash.

In California, as in all states, it is legal for merchants to engage in such dual pricing. But a California statute enacted at the behest of the credit-card lobby, Cal. Civ. Code § 1748.1, seeks to control how merchants may *communicate* the price difference: It allows merchants to offer "discounts" to those who pay in cash but makes it illegal to impose equivalent "surcharges" on those who pay with credit.

A "surcharge" and a "discount" are just two ways of framing the same price information—like calling a glass half full instead of half empty. But consumers react very differently to the two labels, perceiving a "surcharge" as a penalty for using a credit card. Precisely because the "surcharge" label is far more effective at communicating the true cost of credit cards and discouraging their use, the credit-card industry has long insisted that it be suppressed. California's no-surcharge law in effect says to merchants: If you use dual pricing, you may tell your customers only that they are paying $2 less to pay without credit (a "discount"), not that they are paying $2 more to pay with credit (a "surcharge")—even though they *are*

paying $2 more for credit. Liability thus turns on the words used to describe identical conduct—nothing else.

An example illustrates how the law works. Suppose a merchant charges two different prices for widgets depending on how the customer pays—$100 for cash; $102 for credit. If the merchant says that the widget costs $102 and there's a $2 "discount" for paying in cash, the merchant has complied with California law. But if the merchant instead says that the widget costs $100 and there's a $2 "surcharge" for using credit to account for the swipe fee, the merchant has violated the law. In both scenarios, the merchant charges the customer the same amounts ($100 for cash or $102 for credit). The only difference is how the merchant communicates that information to customers—that is, the content of the merchant's speech.

The plaintiffs here are California merchants who want to use dual pricing and truthfully and prominently inform customers that they will pay *more* for using credit cards, not just *less* for using cash. Stonecrest Gas & Wash, for instance, charges credit-card customers a higher price than cash customers, as California law permits. But the company is forced to frame the price difference as a "discount"—by saying that the credit-card price is the "regular" price and the cash price is "less"—even though it would rather call the difference a "surcharge."

Because California's no-surcharge law regulates only how "prices are conveyed to customers, not the prices themselves," the district court correctly held

that the law regulates speech, not conduct. ER10. When a law makes liability "depend[] on what [people] say," it "regulates speech on the basis of its content." *Holder v. Humanitarian Law Project*, 561 U.S. 1, 27 (2010). The "practical effect" of California's law is to ban one disfavored way of truthfully describing lawful conduct, making it a content-based speech restriction, subject to "heightened scrutiny" and "presumptively invalid." *Sorrell v. IMS Health, Inc.*, 131 S. Ct. 2653, 2667 (2011).

Because the law cannot withstand scrutiny, the district court rightly struck it down as unconstitutional under the First Amendment. ER14. The Attorney General has put forth no legitimate interest in suppressing merchants' efforts to convey the true cost of credit to consumers, much less evidence that the law directly advances any such interest. And ready alternatives exist that would be both *less restrictive* of speech and *more effective* in addressing the state's purported consumer-protection aims: Undisclosed surcharges are independently prohibited by false-advertising law, and the danger they pose could be easily addressed by a simple disclosure requirement in any event. *See*, *e.g.*, Minn. Stat. § 325G.051 (allowing merchants to "impose a surcharge" if "conspicuously" disclosed).

The district court also correctly held that the law is unconstitutionally vague. As other courts have properly understood, the purely semantic distinction between a prohibited surcharge and a permitted (but mathematically equivalent) discount is anything but clear. Indeed, the earliest reported prosecution under a no-surcharge

law targeted a gas-station owner whose cashier made the mistake of truthfully telling a customer that it would cost "five cents 'extra'" to pay with a credit card instead of saying it would cost a "nickel less" to use cash. *People v. Fulvio*, 517 N.Y.S.2d 1008, 1014 (N.Y. Crim. Ct. 1987). Merchants in California, just like the targeted gas station, must either operate in constant fear of inadvertently describing a dual-pricing policy in an illegal way or else refrain from dual pricing entirely.

This case is not the first to raise these issues. Just last month, the Eleventh Circuit struck down Florida's virtually identical law as a content-based speech restriction, finding that it "crumbles under any level of First Amendment scrutiny." *Dana's R.R. Supply v. Florida*, — F.3d —, 2015 WL 6725138, *1 (Nov. 4, 2015). "By holding out *discounts* as more equal than *surcharges*," the Eleventh Circuit concluded, "Florida's no-surcharge law overreaches to police speech well beyond the State's constitutionally prescribed bailiwick." *Id.* at *11. Judge Jed Rakoff (in a decision later reversed) reached the same conclusion about New York's law, holding that it "plainly regulates speech" and is unconstitutionally vague because it "draws the line between prohibited 'surcharges' and permissible 'discounts' based on words and labels, rather than economic realities." *Expressions Hair Design v. Schneiderman*, 975 F. Supp. 2d 430, 444 (S.D.N.Y. 2013). Shortly after that decision, another court pronounced no-surcharge laws (of which there are fewer than a dozen) "anti-consumer" and "irrational," finding "good reason to believe" they will not survive

scrutiny. *In re Payment Card Interchange Fee & Merchant Discount Antitrust Litig.*, 986 F. Supp. 2d 207, 232 (E.D.N.Y. 2013). And still another court, in the gas-station owner's prosecution, held that the law was "impermissibly vague" because it treats "precisely the same conduct . . . either as a[n] [unlawful] offense or as lawfully permissible behavior, depending only upon the *label* the individual affixes to his economic behavior, without substantive difference." *Fulvio*, 517 N.Y.S.2d at 1011. "[I]t is not the *act* which is outlawed, but the *word* given that act." *Id.* at 1015.

Despite all this, the Attorney General argues (at 1, 28) that California's law is a "straightforward business regulation" that "does not implicate" the First Amendment, relying on the general rule that "a pricing practice is not protected speech." That is the same position taken by the Second Circuit in *Expressions Hair Design v. Schneiderman*, which reversed Judge Rakoff's decision on the mistaken belief that a statute restricting what merchants may put on their labels and "sticker[s]"—but not what they actually charge customers—regulates "merely prices," not speech. 803 F.3d 94, 107 (2015). That view, however, ignores the distinction that gave birth to the commercial-speech doctrine in the first place. *Va. Bd. of Pharmacy v. Va. Citizens Consumer Council, Inc.*, 425 U.S. 748 (1976). "Pricing is a routine subject of economic regulation, but the manner in which price information is conveyed to buyers is quintessentially expressive, and therefore protected by the First Amendment." *Expressions*, 975 F. Supp. 2d at 445.

JURISDICTIONAL STATEMENT

The district court had subject-matter jurisdiction over the plaintiffs' claims under 28 U.S.C. §§ 1331 and 1343(a)(3). After granting the plaintiffs' summary-judgment motion on March 26, 2015, the district court entered final judgment in their favor that same day. ER1. The Attorney General timely filed a notice of appeal under Federal Rule of Appellate Procedure 4(a)(1)(A) on April 24, 2015. This Court has jurisdiction under 28 U.S.C. § 1291.

STATEMENT OF THE ISSUES

California's no-surcharge statute, Civ. Code § 1748.1, allows merchants to charge consumers a higher price for paying with a credit card as opposed to paying in cash, but requires the merchant to convey the price difference as a cash "discount" and not a credit-card "surcharge." The issues are as follows:

1. Standing. Did the district court correctly hold that the plaintiffs have standing to challenge the law on First Amendment and vagueness grounds because they have been "forced to modify [their] speech and behavior to comply with [it]"? *Ariz. Right to Life Political Action Comm. v. Bayless*, 320 F.3d 1002, 1006 (9th Cir. 2003).

2. The First Amendment. Did the district court correctly hold that the law "is not an economic regulation that controls what is charged or paid for something," but instead "regulates speech that conveys price information, which is

protected by the First Amendment"? ER10. If so, did the court correctly hold that the law cannot survive First Amendment scrutiny?

3. Void for Vagueness. Did the district court correctly hold that the law is unconstitutionally vague because no one—not even the state—can answer several basic questions about its meaning that "represent legitimate concerns that retailers must face when determining whether to impose a legal dual-pricing system"? ER16.

STATEMENT OF THE CASE AND OF THE FACTS

"What most consumers do not know is that their decision to pay by credit card involves merchant fees, retail price increases, a nontrivial transfer of income from cash to card payers, and consequently a transfer from low-income to high-income consumers." Schuh, et al., *Who Gains and Who Loses from Credit Card Payments?*, Federal Reserve Bank of Boston, at 1 (2010). Although merchants may charge consumers more for using a credit card, they cannot effectively communicate that added cost to consumers because the credit-card companies have succeeded in insisting that any price difference be framed as a cash "discount," rather than a credit-card "surcharge."

This industry-friendly speech code has long been imposed through both private contract and state legislation. But a nationwide settlement in a major antitrust class action required leading credit-card companies to remove their contractual no-surcharge rules in 2013. So state laws like California's have now

assumed sudden importance: They are the only thing stopping merchants from truthfully saying that they impose a credit "surcharge" because credit costs more.

California's no-surcharge statute makes it illegal for any "retailer in any sales, service, or lease transaction" to "impose a surcharge on a cardholder who elects to use a credit card in lieu of payment by cash, check, or similar means." Cal. Civ. Code § 1748.1(a). The law does not, however, outlaw dual pricing: The statute allows retailers to "offer discounts for the purpose of inducing payment by cash, check, or other means not involving the use of a credit card." *Id.*

I. Why labels matter: the communicative difference between "surcharges" and "discounts"

A credit-card "surcharge" and a cash "discount" are just "different frames for presenting the same price information—a price difference between two things." Levitin, *Priceless? The Economic Costs of Credit Card Merchant Restraints*, 55 UCLA L. Rev. 1321, 1330, 1351 (2008). They are equivalent in every way except one: the *label* that the merchant uses to communicate that difference.

But labels matter. "[T]he frame within which information is presented can significantly alter one's perception of that information, especially when one can perceive the information as a gain or a loss." Hanson & Kysar, *Taking Behavioralism Seriously: Some Evidence Of Market Manipulation*, 112 Harv. L. Rev. 1420, 1441 (1999). This difference in perception occurs because of people's tendency to let "changes that make things worse (losses) loom larger than improvements or gains" of an

equivalent amount. Kahneman et al., *Anomalies: The Endowment Effect, Loss Aversion, and Status Quo Bias*, 5 J. Econ. Persp. 193, 199 (1991).

"Consumers react very differently to surcharges and discounts." Levitin, *The Antitrust Super Bowl: America's Payment Systems, No-Surcharge Rules, and the Hidden Costs of Credit*, 3 Berkeley Bus. L.J. 265, 280 (2006). Consumers are more likely to respond to surcharges (which are perceived as *losses* for using credit) than to discounts (which are perceived as *gains* for not using credit). *Id.* Research shows just how wide this gap is. In one study, 74% of consumers responded negatively to surcharges, but fewer than half responded negatively to equivalent cash discounts. *Id.* at 280-81.

The effectiveness of surcharges is why the plaintiffs here seek to impose them. Surcharges inform consumers of the cost of credit and thus create meaningful competition, which in turn drives down that cost. If swipe fees are too high, consumers will use a different payment method, and banks and credit-card companies will have to lower their fees to attract more business.

II. How we got here: the credit-card industry's concerted efforts to prevent merchants from communicating the costs of credit as "surcharges"

The invisibility of swipe fees is no accident. It is the product of concerted efforts by the credit-card industry over many decades. Over the years, the industry has succeeded, both through contractual provisions and legislation, in silencing merchants' attempts to call consumers' attention to the true costs of credit.

A. The industry's early ban on dual pricing and its demise

In the early days of credit cards, credit-card companies banned any attempt at differential pricing between credit and cash in their contracts with merchants. Kitch, *The Framing Hypothesis: Is It Supported by Credit Card Issuer Opposition to a Surcharge on a Cash Price?*, 6 J.L. Econ. & Org. 217, 219-20 (1991). That changed in 1974 after Congress enacted legislation protecting the right of merchants to have dual-pricing systems by granting them a non-waivable right to "offer[] a discount" to induce consumers "to pay by cash, check, or similar means" other than a credit card. Pub. L. No. 93, § 495, 88 Stat. 1500 (1974) (codified at 15 U.S.C. § 1666f(a)).

B. The credit-card industry shifts its strategy to labels

The 1974 legislation was initially considered a victory for consumer advocates. But the credit-card industry, seizing on Congress's use of the word "discount," soon shifted its focus to the way merchants could *communicate* credit pricing to consumers. Aware that how information is presented to consumers can have a huge impact on their behavior—and that many merchants would avoid dual pricing if "surcharges" were outlawed—the credit-card lobby "insist[ed] that any price difference between cash and credit purchases should be labeled a cash discount rather than a credit card surcharge." Tversky & Kahneman, *Rational Choice and the Framing of Decisions*, 59 J. Bus. S251, S261 (1986); *see also* Thaler, *Toward a Positive Theory of Consumer Choice*, 1 J. Econ. Behavior & Org. 39, 45 (1980)

("[T]he credit card lobby turned its attention to form rather than substance. Specifically, it preferred that any difference between cash and credit card customers take the form of a cash discount rather than a credit card surcharge.").

C. The industry's labeling strategy achieves short-lived success at the federal level

For a while, this intensive lobbying paid off. In 1976, the credit-card industry succeeded in getting Congress to enact a temporary ban on "surcharges," despite the authorization for "discounts." Pub. L. No. 94-222, 90 Stat. 197. But by the early 1980s, opposition to the ban grew as the Reagan Administration, consumer groups, and retailers all urged Congress to let it lapse.

1981: Opposition to federal surcharge ban mounts. A member of the Federal Reserve Board, which unanimously opposed the ban, testified about "the obvious difficulty in drawing a clear economic distinction between a permitted discount and a prohibited surcharge." *Cash Discount Act, 1981: Hearings on S. 414 Before the Senate Banking Comm.*, 97th Cong., 1st Sess. 9 (Feb. 18, 1981) (reproduced at SER9). "If you just change the wording a little bit, one becomes the other." SER12. The Board thus proposed "a very simple rule": that both surcharges and discounts be allowed and "the availability of the discount or surcharge be disclosed to consumers." SER10.

Every major consumer-advocacy organization agreed. One advocate testified that the difference between surcharges and discounts "is merely one of

semantics, and not of substance." SER23. But "the semantic differences are significant," she explained, because "the term 'surcharge' makes credit card customers particularly aware that they are paying an extra charge," whereas "the discount system suggests that consumers are getting a bargain, and downplays the truth." *Id.* That is why the cost of credit is best "expressed in the form of [a] surcharge." *Id.* Another advocate put it more pithily: "one person's cash discount may be another person's surcharge." SER19. "Removing the ban on surcharges," he explained, "is an important first step" to "disclos[ing] to consumers the full" cost of credit so they can "make informed judgments." SER21.[1]

By contrast, American Express and MasterCard "strongly" supported the ban, even though they too understood that, from a "mathematical viewpoint," "there is really no difference between a discount for cash and a surcharge for credit card use." SER16-17. And the big banks likewise supported treating "surcharges" and "discounts" differently because a surcharge "makes a negative statement about the card to the consumer" and "talk[s] against the credit industry." SER14, 18.

Congress ultimately gave in to industry lobbying and renewed the ban for an additional three years. Pub. L. No. 97-25, 95 Stat. 144 (1981).

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[1] President Reagan's Federal Trade Commission chairman also opposed the ban, explaining that "a discount and a surcharge are equivalent concepts." *Cash Discount Act*, 97th Cong., 1st Sess. 127.

1984: Congress lets federal surcharge ban lapse. Over the next few years, opposition to the ban only intensified. In 1984, when it was again set to expire, Senator William Proxmire cut to the chase: "Not one single consumer group supports the proposal to continue the ban on surcharges," he observed. "The nation's giant credit card companies want to perpetuate the myth that credit is free." Molotsky, *Extension of Credit Surcharge Ban*, N.Y. Times, Feb. 29, 1984, at D12. Ultimately, despite a massive lobbying campaign, the industry's efforts failed, and the ban lapsed in 1984. Levitin, *Priceless?*, 55 UCLA L. Rev. at 1381.

D. The credit-card industry lobbies states to enact no-surcharge laws and adopts contractual no-surcharge rules

After the national ban expired, the credit-card industry briefly turned to the states, convincing ten states (including California) to enact no-surcharge laws of their own. American Express and Visa went to great lengths to create the illusion of grassroots support for these laws, even going so far as to create and bankroll a fake consumer group called "Consumers Against Penalty Surcharges"—an early instance of the phenomenon now known as astroturfing. SER25 (internal memo from Hill & Knowlton public-relations firm, describing its work in creating the group); *see also* Associated Press, *Consumers Gain Friends in Credit Card Fight*, Ocala Star-Banner, Apr. 2, 1984 (noting that the group was "bankrolled by American Express and Visa"). In California, this group formally sponsored the no-surcharge law as part of its goal of achieving "a permanent ban at the federal level" like the

one previously enacted "[a]t the behest of card issuers." SER48-49. But the real consumer groups (including Consumers Union and Consumer Federation of America) opposed the law because it inhibits transparency, thereby increasing costs and masking an enormous "invisible subsidy" from low-income cash consumers to high-income credit consumers. SER58-59.

In 1985, one year after expiration of the temporary federal ban, California's no-surcharge law was enacted. Despite the strong consumer opposition, the law says that its purpose is "to promote the effective operation of the free market and protect consumers from deceptive price increases for goods and services by prohibiting credit card surcharges and encouraging the availability of [cash] discounts." Cal. Civ. Code § 1748.1(e).

Around the same time, the major credit-card companies changed their contracts with merchants to include no-surcharge rules. No-surcharge laws in California and other states thus function as a legislative extension of the restrictions that credit-card issuers previously imposed more overtly by contract. For instance, American Express's contracts with merchants included an elaborate speech code, providing that merchants may not "indicate or imply that they prefer, directly or indirectly, any Other Payment Products over our Card"; "dissuade Cardmembers from using the Card"; "criticize . . . the Card"; or "try to persuade or prompt

Cardmembers to use . . . any other method of payment." American Express, *Merchant Reference Guide–U.S.*, at 16 (Oct. 2013), *at* http://amex.co/1iwWJ5j.

E. Visa and MasterCard drop their contractual no-surcharge rules

For the next two decades, the issue of swipe fees remained largely in the shadows. Even in the majority of states without no-surcharge laws, the contractual rules ensured that consumers were rarely informed of the true cost of credit. In 2005, however, merchants and trade associations began bringing antitrust claims challenging those rules, culminating in a nationwide class-action settlement under which Visa and MasterCard dropped their surcharge prohibitions on merchants in January 2013. Silver-Greenberg, *Visa and MasterCard Settle Claims of Antitrust*, N.Y. Times, July 14, 2012, at B1.

As a result, state no-surcharge laws—previously largely irrelevant because of parallel contractual rules—have taken on renewed importance.[2]

III. This litigation

In March 2014, after a district court struck down New York's law and Visa and MasterCard agreed to drop their contractual restrictions, five California

[2] Because the contractual rules were in effect for so long, California's law has a sparse enforcement history. In 2001, someone brought a class action against a gas station that listed a "cash price" and a "credit price" but didn't characterize the difference in any particular way. *Thrifty Oil v. Superior Court*, 91 Cal. App. 4th 1070, 1073-78 (2d Dist. 2001). The court held that this "two-tier pricing system," without more, was permissible. *Id.* at 1078.

merchants and their principals brought this lawsuit. Each merchant wants take advantage of the recent settlement and truthfully tell their customers that paying by credit card costs *more* than paying by cash (not merely that cash costs *less* than credit). But California's law makes that language illegal.

A. The plaintiffs

1. Stonecrest Gas & Wash. Stonecrest is a gas station, car wash, repair shop, and convenience store in San Diego. ER106. It typically pays between 2% and 3% of each credit-card transaction in swipe fees. *Id.*

Stonecrest used to include the expense of swipe fees in the prices paid by all customers. ER106. But it determined that charging a single price regardless of payment hid the true cost of credit and gave credit-card customers little incentive to switch to cash. *Id.* So Stonecrest began charging two prices for goods and services depending on how the customer pays, while taking pains to communicate the difference as a cash "discount." ER107.

That is not how Stonecrest wants to frame the price difference. Stonecrest would rather call it a credit-card "surcharge," which the company believes would better inform customers of the high cost of credit without making prices look higher than they are. *Id.* California's law, however, bans that way of describing dual pricing. *Id.* Were it not for that law, Stonecrest would "describe this price difference as a 'surcharge' rather than a 'discount.'" *Id.*

2. Leon's Transmission Service. Leon's provides transmission-repair services throughout Southern California. ER124. It has been passionate about credit-card reform for more than a decade. *Id.* After successfully suing a credit-card processor for charging illegal fees, Leon's agreed to serve as a named plaintiff and class representative in the antitrust litigation that has now resulted in historic relief allowing merchants to convey the cost of credit as a surcharge. ER128. But Leon's may not take fall advantage of that relief because of California's law. *Id.*

Because of that law, Leon's does not tell its customers that it will charge "extra" for credit, nor does it engage in dual pricing (even though it would like to and is allowed to). ER128-29. This means that swipe fees get passed on to all of its customers, cash and credit-card users alike, in the form of higher prices. ER129. And because swipe fees are kept hidden, customers have no disincentive to use credit—just the opposite, in fact, because of the benefits that most credit cards offer—which raises fees even higher. *Id.*

3. Italian Colors Restaurant. Italian Colors is a restaurant in Oakland that is owned and operated by Alan Carlson. ER120. It has found that customers are generally unaware of the cost of credit when ordering food and paying their bill. *Id.* It has thus sought to do what it can to ensure that customers learn of the cost of credit and take it into account when making purchases—not just at the restaurant, but at businesses nationwide. This concern has led Italian Colors (like Leon's) to

serve as lead plaintiff in one of the nationwide class-action lawsuits against the major credit-card companies.

Italian Colors is aware that it may pass on the cost of credit if characterized as a "discount." ER121-22. But the restaurant believes that this way of framing dual pricing would make prices look higher than they are, without conveying to customers that the price difference is attributable solely to the cost of credit—the very message it wants to communicate. ER122. Italian Colors believes that it would be far more effective to truthfully tell its customers that they will pay *more* for credit by saying that the cash price is the regular price and the credit price is extra. ER121. Italian Colors would like to convey the amount of the surcharge on its signs and menus, as well as on the receipts of credit-card-paying customers, which would allow it to "target the customers whose behavior [it] want[s] to impact." ER122. Were it not for California's law, Italian Colors would "charge more for credit card transactions and label that price difference as a 'surcharge' rather than a 'discount.'" ER121. Instead, it stays away from dual pricing altogether. Its owners do not fully understand the difference between a credit-card surcharge and a cash discount, and they do not want to risk violating the law to say something that they believe is only marginally effective at communicating their message. *Id.*

4. Milo's Cleaners. Laurelwood is a family-owned company that operates Milo's Cleaners in North Hollywood. ER111. In the 1990s, Milo's instituted a

dual-pricing policy, which it expressed as an additional fee for credit on top of its "regular" price. *Id.* But it stopped the practice after learning that California barred merchants from characterizing dual pricing in that way. ER111-12. Although Milo's could have called the price difference a cash discount—without changing any of its prices—it instead decided to abandon dual pricing entirely. It does not want to call the credit-card price the "regular" price, and it finds the distinction between a cash discount and credit surcharge to be confusing, so it doubts it could comply with the law in practice. *Id.* If not for that law, Milo's would again "charge different prices and convey the difference as a surcharge so that [its] customers would be made aware of the high costs of credit." ER112.

5. Family Graphics. Family Graphics is a California web-design company. ER116. It too wants to bring swipe fees to customers' attention by saying that there is an additional charge for paying by credit. ER116-17. But it cannot do so because of California's law. Nor does Family Graphics offer dual pricing, because the law bans the most effective way of conveying the cost of credit, and the company is uncertain that it could lawfully implement a dual-pricing system. *Id.*

B. The district court's decision

Shortly after the plaintiffs filed their complaint, the parties exchanged motions for summary judgment. The district court granted the plaintiffs' motion, declared the law unconstitutional, and permanently enjoined its enforcement.

The court began its opinion by describing how the law works in practice. It allows merchants "to charge more for credit card purchases than cash purchases, regardless of the 'normal price' of the item, as long as this price difference is framed as a discount rather than a surcharge." ER5. Thus, "a retailer could charge $102 for a product and give a $2 discount, but could not charge $100 and impose a $2 surcharge, despite the situations being mathematically equivalent." ER3. The law simply "restricts how this $2 price difference is presented to the consumer." *Id.*

Turning to the parties' legal arguments, the court first held that the plaintiffs have standing because there is a "realistic danger" that they would be sued or subject to an enforcement action if they were to violate the law. ER8. On the merits, the court rejected the state's argument that the law regulates economic conduct rather than speech. As the court put it: The law is "not an economic regulation that controls what is charged or paid for something"; it regulates only how "prices are conveyed to customers, not the prices themselves." ER10. Because the law "regulates speech that conveys price information, which is protected by the First Amendment," *id.* the court applied intermediate scrutiny under *Central Hudson Gas & Electric Corp. v. Public Service Commission of New York*, 447 U.S. 557 (1980).

The court easily concluded that the law failed scrutiny. The law applies even to truthful, non-misleading speech, such as when a "retailer display[s] information about the surcharge throughout the store and note[s] that the surcharge [is] due to

merchant fees." ER13. That is "informative and accurate," not deceptive. *Id.* The court determined that "California's law is much broader than necessary" to guard against the risk of "unfair surprise to the consumers at the cash register," a risk that could be addressed by a law simply "mandating disclosure of surcharges." *Id.*

After striking down the law under the First Amendment, the court then held that it is impermissibly vague. The court asked a series of practical questions that any merchant "must face when determining whether to impose a legal dual-pricing system." ER16. The court found that, even with the Attorney General's briefing, the answers to these basic questions were "not clear to the Court," "[n]or are they clear to the Plaintiffs, all small businesses, or even the large national retail chains who have submitted an amicus brief in this case." *Id.*

STANDARD OF REVIEW

This Court reviews de novo the question whether a statute violates the First Amendment. *ACLU of Nev. v. City of Las Vegas*, 466 F.3d 784, 791-92 (9th Cir. 2006). Likewise, "[w]hether a statute or regulation is unconstitutionally vague is a question of law reviewed de novo." *Ass'n des Eleveurs de Canards et d'Oies du Quebec v. Harris*, 729 F.3d 937, 946 (9th Cir. 2013).

SUMMARY OF ARGUMENT

I. The plaintiffs have standing to challenge California's no-surcharge law because they have been "forced to modify [their] speech and behavior to comply

with [it]." *Ariz. Right to Life Political Action Comm. v. Bayless*, 320 F.3d 1002, 1006 (9th Cir. 2003). Each plaintiff wishes to frame the cost of credit as a credit-card "surcharge" rather than a cash "discount," and to truthfully and prominently disclose the amount of the surcharge on its signs and labeling. And each refrains from doing so for only one reason: California's law. It is not unreasonable for them to do so because the Attorney General "has not suggested that the legislation will not be enforced" against them, and the law has not "fallen into desuetude." *Id.* at 1006-07.

II. A. The Supreme Court has made clear that any law whose "purpose and practical effect" are "to suppress speech" based on content requires "heightened scrutiny" under the First Amendment. *Sorrell v. IMS Health Inc.*, 131 S. Ct. 2653, 2663-64 (2011). The no-surcharge statute is such a law. It does not regulate what merchants may *do*: They may charge different prices for cash and credit, set at whatever amounts they wish. The law regulates only what merchants may *say*: Framing the price difference as a cash "discount" is favored; framing it as a credit "surcharge" is illegal. The practical effect, in other words, is to suppress speech.

That was also the law's purpose: It was enacted at the behest of the credit-card lobby (which worried that surcharges "talk against" the industry), while consumer-advocacy groups opposed the law's regulation of "semantic differences" because of the effect that had on consumers. SER18, 23. And the law was openly

justified based on the surcharge label's "psychological[]" ability to "encourage[] desired behavior." SER61.

It is no answer to say, as the Attorney General does, that the law is just a restriction of a "pricing practice." AG Br. 28. Pricing, of course, is a routine subject of economic regulation. But this law regulates only how "prices are conveyed to customers, not the prices themselves." ER10. If a state wants to restrict the way in which merchants may convey truthful "price information" to consumers—without regulating the prices actually charged—it must satisfy First Amendment scrutiny. *Va. Bd. of Pharmacy v. Va. Citizens Consumer Council, Inc.*, 425 U.S. 748, 770 (1976).

B. The no-surcharge law fails scrutiny. It does not directly advance an interest in promoting consumer welfare, is riddled with exceptions that undermine any such interest, and is far broader than necessary to address any risk of deception, which is prohibited by false-advertising laws anyway and could be easily addressed by simple disclosure requirements.

III. Finally, the no-surcharge law is also unconstitutionally vague. It does not clearly define the line between a permissible "discount" and a mathematically equivalent but illegal "surcharge." As a result, merchants must operate in constant fear of inadvertently describing a dual-pricing policy in an unlawful way or else refrain from dual pricing altogether.

ARGUMENT

I. The plaintiffs have standing.

The Attorney General begins her argument by attacking the plaintiffs' standing. She claims (at 16) that "they have not shown *any* injury in fact" because they did not violate the statute and wait to be sued. But "one does not have to await the consummation of threatened injury to obtain preventive relief"—least of all in a First Amendment challenge, where "the inquiry tilts dramatically toward a finding of standing." *Ariz. Right to Life*, 320 F.3d at 1006. "That is so because, as the Supreme Court has recognized, a chilling of the exercise of First Amendment rights is, itself, a constitutionally sufficient injury." *Libertarian Party of Los Angeles Cnty. v. Bowen*, 709 F.3d 867, 870 (9th Cir. 2013). Thus, "[i]n an effort to avoid the chilling effect of sweeping restrictions, the Supreme Court has endorsed what might be called a 'hold your tongue and challenge now' approach rather than requiring litigants to speak first and take their chances with the consequences." *Ariz. Right to Life*, 320 F.3d at 1006. Under that approach, the plaintiffs need only show "a realistic danger of sustaining a direct injury as a result of the statute's operation or enforcement." *Babbitt v. United Farm Workers Nat'l Union*, 442 U.S. 289, 298 (1979).

The plaintiffs have followed the Supreme Court's approach here. Although they have "neither violated the statute nor been subject to penalties for doing so," they have been "forced to modify [their] speech and behavior to comply with the

statute." *Ariz. Right to Life*, 320 F.3d at 1006. Each plaintiff wishes to take advantage of the recent national antitrust settlement, which forced leading credit-card companies to drop their contractual surcharge bans. Each wishes to do so by characterizing the difference between the cash and credit price as a credit-card "surcharge," not a cash "discount." And each wishes to prominently and truthfully communicate the surcharge amount to consumers ahead of time. But they cannot do so because California's law prohibits them from conveying pricing information in that way.

It was "not unreasonable for [the plaintiffs] to modify [their] behavior out of fear of being the object of an enforcement action." *Id.* The Attorney General "has not suggested that the legislation will not be enforced if [the plaintiffs] were to violate its provisions," nor has the law "fallen into desuetude." *Id.* at 1006-07. "Under such circumstances, [the plaintiffs] faced a reasonable risk that [they] would be subject to civil penalties for violation of the statute." *Id.* at 1007; *see Virginia v. Am. Booksellers Ass'n, Inc.*, 484 U.S. 383, 393 (1988) (plaintiffs have standing when "[t]he State has not suggested that the newly enacted law will not be enforced, and we see no reason to assume otherwise"); *Babbitt*, 442 U.S. at 302 (plaintiffs are "not without some reason in fearing prosecution," and thus have standing, when "the State has not disavowed any intention" of enforcing the law). That is enough for standing.

Contending otherwise, the Attorney General makes three arguments. *First*, she claims that the plaintiffs have not articulated a "concrete plan" to violate the law. AG Br. 16. That is false. The plaintiffs' declarations leave no doubt that, were it not for California's law, they would engage in dual pricing (as one plaintiff already does) and characterize the price difference as a credit-card surcharge. *See* ER107-08; ER112; ER117; ER121; ER130. Two plaintiffs have even served as lead plaintiffs in the antitrust litigation that has led to the relief they now seek to enjoy. And another plaintiff previously had dual pricing and labeled the difference a credit surcharge, but stopped doing so when it learned of California's law. ER111-12. That is anything but a "hypothetical intent to violate the law." *Thomas v. Anchorage Equal Rights Comm'n*, 220 F.3d 1134, 1139 (9th Cir. 2000) (en banc).

Second, the Attorney General argues that the plaintiffs lack standing because they are "unable to point to any enforcement efforts against them." AG Br. 18-19. But that's because they have chosen not to violate the statute. As a result, their injury "is, in large measure, one of self-censorship; a harm that can be realized even without an actual prosecution.'" *Ariz. Right to Life*, 320 F.3d at 1006 (quoting *Am. Booksellers Ass'n*, 484 U.S. at 393).

Finally, the Attorney General relies on the law's sparse enforcement history more broadly as proof that the plaintiffs lack standing. But the credit-card companies did not rescind their contractual surcharge bans until 2013, making the

law largely irrelevant until very recently. And other states with identical laws have targeted merchants in recent years for "quot[ing] the price" of a product over the phone and saying that they "charge[] a fee on top of that price for using a credit card," with one state Attorney General's office even going so far as to give the merchants scripts for how they can communicate their prices to customers. *Expressions Hair Design v. Schneiderman*, 975 F. Supp. 2d 430, 444 n.7 (S.D.N.Y. 2013). California has given no reason why it couldn't (or wouldn't) enforce the same statute in the same way here. In any event, "enforcement history alone is not dispositive." *LSO, Ltd. v. Stroh*, 205 F.3d 1146, 1155 (9th Cir. 2000). The plaintiffs just have to show "a realistic danger of sustaining a direct injury as a result of the statute's operation or enforcement." *Ariz. Right to Life*, 320 F.3d at 1006. They have done that here.

II. California's no-surcharge law violates the First Amendment.

A. The statute is a content-based speech restriction subject to heightened First Amendment scrutiny.

The Supreme Court has increasingly insisted that the First Amendment "requires heightened scrutiny" whenever the government creates restrictions that turn on the content of a speaker's words. *Sorrell*, 131 S. Ct. at 2663-64. This scrutiny applies to any law whose "purpose and practical effect" are "to suppress speech" based on its content, even if the law "on its face appear[s] neutral." *Id.*; *see also McCullen v. Coakley*, 134 S. Ct. 2518, 2529 (2014) (applying "First Amendment

scrutiny" to a law that restricted speech "even though the Act says nothing about speech on its face"). Thus, "[t]he fact that [a] statute's practical effect may be to discourage protected speech is sufficient to characterize [it] as an infringement on First Amendment activities." *FEC v. Mass. Citizens for Life, Inc.*, 479 U.S. 238, 255 (1986). If a law makes liability "depend[] on what [people] say," in other words, it "regulates speech on the basis of its content" and First Amendment scrutiny applies. *Holder v. Humanitarian Law Project*, 561 U.S. 1, 27 (2010). Content-based speech restrictions are "presumptively invalid," so often "it is all but dispositive to conclude that a law is content-based." *Sorrell*, 131 S. Ct. at 2667.

"Commercial speech is no exception." *Id.* at 2664. The Supreme Court has long held that this speech—including speech conveying "price information" to consumers—is "protected by the First Amendment." *Va. Bd. of Pharmacy*, 425 U.S. at 770. So if a law's "purpose and practical effect" are to restrict price information or other commercial speech based on its content, as with California's no-surcharge statute, then the law must withstand heightened scrutiny to satisfy the First Amendment. *Sorrell*, 131 S. Ct. at 2663.

1. Both the "purpose and practical effect" of California's law show that it is a content-based (and speaker-based) restriction on speech.

Practical effect. As the district court explained, the no-surcharge law "is not an economic regulation that controls what is charged or paid for something."

ER10. To the contrary, the law allows merchants to charge different prices depending on whether a customer pays with cash or credit, and to set those prices as they wish. The only thing the law regulates "is how those prices are *conveyed* to customers, not the prices themselves." *Id.* (emphasis added). Characterizing the price difference as a cash "discount" is favored; characterizing it as a credit "surcharge" is outlawed. The statute thus prohibits a certain class of speakers (merchants) from communicating a certain disfavored message (framing the added cost of credit as a surcharge) and does so to discourage consumers from acting on that message (by deciding not to use a credit card).

To see how the law works, return to the hypothetical merchant who charges two different prices for a product: $100 for cash and $102 for credit. How is the merchant supposed to comply with the no-surcharge law? If the merchant says that the product costs $102 (for example, by listing that amount on the label) and puts up a sign offering a $2 "discount" to anyone who pays with cash, the merchant has obeyed the law. But if the merchant instead says that the product costs $100 (by listing that amount on the label) and puts up a sign informing customers that there is a $2 credit-card surcharge to account for the swipe fee, the merchant has violated the law. In both circumstances—the lawful and the verboten—the prices charged are identical: The merchant "charges a higher price" for using a credit card ($102 versus $100), and the additional amount is the same ($2). AG Br. 24.

And in both circumstances that amount is truthfully and prominently communicated to customers ahead of time. The only difference is *how* it is communicated—that is, which of the two prices the merchant chooses to frame as the "regular" price on the label, and which it chooses to convey through a separate sign. Put another way, the law does not regulate the setting of prices by merchants, but kicks in only *after* they have been set, by demanding one way of framing them over another. A non-complying merchant can bring itself into compliance simply by changing the way that it frames or communicates its prices to customers, without changing the prices themselves.

For this reason, the Eleventh Circuit recently held that Florida's virtually identical law regulates speech. "After all," the court explained, "what is a surcharge but a negative discount?" *Dana's R.R. Supply v. Florida*, — F.3d —, 2015 WL 6725138, *6 (11th Cir. Nov. 4, 2015). The court then gave its own hypothetical example: "If the same copy of Plato's *Republic* can be had for $30 in cash or $32 by credit card, absent any communication from the seller, does the customer incur a $2 *surcharge* or does he receive a $2 *discount*? Questions of metaphysics aside, there is no real-world difference between the two formulations," making the law "a restriction on speech, not a regulation of conduct." *Id.*[3]

[3] Chief Judge Carnes dissented in *Dana's Railroad Supply*, expressing his view that the statute should be read to prohibit only *undisclosed* surcharges, to save it (continued…)

One need not think hypothetically, however, to see that the no-surcharge law operates as a content-based speech restriction. In the first reported enforcement action of a no-surcharge law, a gas-station owner was arrested, prosecuted, and convicted because his cashier truthfully informed a customer that it cost "five cents 'extra'" to use credit rather than saying that it was a "nickel less" to use cash. *People v. Fulvio*, 517 N.Y.S.2d 1008, 1010 (N.Y. Crim. Ct. 1987). His conviction was set aside, but only because the court found it constitutionally "intolerable" that "precisely the same conduct by an individual may be treated either as a criminal offense or as lawfully permissible behavior, depending only upon the *label* the individual affixes to his economic behavior, without substantive difference." *Id.* at 1011, 1015. The court explained:

> [W]hat [the no-surcharge law] *permits* is a price differential, in that so long as that differential is characterized as a discount for payment by cash, it is legally permissible; what [the law] *prohibits* is a price differential, in that so long as that differential is characterized as an additional charge for payment by use of a credit card, it is legally impermissible. . . . [The law] creates a distinction without a difference; **it is not the *act* which is outlawed, but the *word* given that act.**

Id. at 1015 (bold added).

"from a fatal constitutional flaw" and "a great big First Amendment bullseye." 2015 WL 6725138, *12-*13. But the plaintiffs here seek to impose *disclosed* surcharges, and the state is arguing that it may constitutionally bar them from doing so. And, in any event, the statutory language on which Chief Judge Carnes relied—"imposed at the time of a sale"—is not present here. *Id.* at *11.

Each of these examples (both hypothetical and real) shows that "the content of the retailers' speech must be scrutinized to determine if the price is framed as a permissible discount or an impermissible surcharge, making this a content-based restriction." ER12. Any law "that requires reference to the content of speech to determine its applicability is inherently content-based." *Pagan v. Fruchey*, 492 F.3d 766, 779 (6th Cir. 2007). So too is a law that "permits an idea to be expressed but disallows the use of certain words in expressing that idea." *AIDS Action Comm. of Mass., Inc. v. Mass. Bay Transp. Auth.*, 42 F.3d 1, 8 (1st Cir. 1994). That is what California's law does: Merchants may avoid liability by changing "what they say" rather than what they charge. *Humanitarian Law Project*, 561 U.S. at 27. Nothing more is needed to show that the law is a content-based speech restriction. *See S.O.C., Inc. v. County of Clark*, 152 F.3d 1136, 1145 (9th Cir. 1998) (finding law content-based because it "distinguish[ed] between [two] forms of expression"); *Fonti v. City of Menlo Park*, 146 F.3d 629, 636 (9th Cir. 1998) (finding law content-based because an "officer must read a sign's message to determine if the sign" was legal).

Purpose. The reason the law restricts speech is that this was its purpose. When California enacted the law, it sought to fill the gap left by the federal ban's expiration. That ban had lasted for several years thanks to intense lobbying by credit-card companies, which objected to allowing the surcharge label because it would "talk against the credit industry." *Cash Discount Act, 1981: Hearings on S. 414*,

at 32, 60 (SER14, 18). Those who opposed the ban, like the Federal Reserve Board and the major national consumer groups, also understood that it was aimed at "wording" and "semantics, and not . . . substance." SER12, 23.

There is no reason to believe that California's legislature thought differently. Just as Congress knew that credit surcharges and cash discounts, although "mathematically the same," are "very different" in their "practical effect and impact . . . on consumers," California understood the same. S. Rep. No. 97-23, at 3. Thus, the legislature knew that it was really regulating the different effects of the two labels on consumer perceptions of credit cards. As a memorandum prepared in support of one state no-surcharge law put it: "Surcharges, *even if only psychologically*, impose penalties on purchasers. . . . A cash discount, on the other hand, operates as an incentive and *encourages desired behavior*." SER61 (emphasis added).

But a behavioral effect that "depend[s] on mental intermediation," like the effect of one label versus another, just "demonstrates the power" of speech. *Am. Booksellers Ass'n, Inc. v. Hudnut*, 771 F.2d 323, 329 (7th Cir. 1985). The law affects consumer behavior "only through the reactions it is assumed people will have to the free flow of [credit-card] price information." *Va. Bd. of Pharmacy*, 425 U.S. at 769. In the context of credit cards, this assumption is well placed: "Because of the framing effect, surcharges are far more effective than discounts at signaling to consumers" the costs of credit. Levitin, *Priceless?*, 55 UCLA L. Rev. at 1352.

"The First Amendment does not, however, allow the Government to directly restrict speech in an attempt to control conduct in response to that speech." *Dana's R.R. Supply*, 2015 WL 6725138, *11. As the Supreme Court has repeatedly stressed, states may not pass laws that seek to "diminish the effectiveness" of communication simply because the state has determined that certain speech is too powerful. *Sorrell*, 131 S. Ct. at 2663. "Those who seek to censor or burden free expression often assert that disfavored speech has adverse effects," *id.* at 2670, so courts must "be especially skeptical of regulations that seek to keep people in the dark for what the government perceives to be their own good," *44 Liquormart, Inc. v. Rhode Island*, 517 U.S. 484, 503 (1996). Fear that "the public will respond 'irrationally' to the truth" or "would make bad decisions if given truthful information" is no justification for banning speech. *Id.* Rather than decree such a "highly paternalistic approach," states must "assume that [accurate pricing] information is not in itself harmful, that people will perceive their own best interests if only they are well enough informed, and that the best means to that end is to open the channels of communication rather than to close them." *Va. Bd. of Pharmacy*, 425 U.S. at 770.[4]

[4] As discussed in more detail below (at 37-40), this constitutional challenge casts doubt on *none* of the consumer-protection laws relied on by the Attorney General. Nor does it implicate the current debate over attempts to use the First Amendment as a corporate and political deregulatory tool. *See* Wu, *The Right to Evade Regulation*, The New Republic, June 3, 2013; Purdy, *The Roberts Court v. America*, Democracy, Winter 2012.

But the law here doesn't even have paternalism on its side. Rather, the law is "giv[ing] one side"—the credit-card industry—"an advantage" by muzzling merchants. *First Nat'l Bank of Boston v. Bellotti*, 435 U.S. 765, 785 (1978). A law that "has the effect of preventing" merchants "from communicating with [consumers] in an effective and informative manner," thus hamstringing their "ability to influence [consumer] decisions," is one that "impose[s] a specific, content-based burden on protected speech." *Sorrell*, 131 S. Ct. at 2663-64, 2670. "Attempting to control the outcome of . . . consumer decisions" by restricting truthful speech is just what the First Amendment prohibits the state from doing. *Allstate Ins. Co. v. Abbott*, 495 F.3d 151, 167 (5th Cir. 2007).

2. Because the law cannot withstand scrutiny, the Attorney General spends most of her brief trying to resist it. She makes two contradictory arguments for why scrutiny should not apply. The first is that the law regulates only "deceptive price increases." AG Br. 24. On this view, the law's purpose and practical effect are simply to prohibit false and deceptive advertising—to prevent merchants from "stat[ing] an ostensible price but then, when it comes time for purchase, add[ing] a surcharge on top of that price for credit card users." AG Br. 34.

But California's law obviously sweeps much broader than disclosure. Its prohibition applies even to merchants who truthfully and prominently disclose the amount of the surcharge ahead of time, as the plaintiffs here all wish to do (and as

the recent antitrust settlement requires). And because California already has laws on the books that independently prohibit false advertising, as explained in Part II.B, the sole "practical effect" of the no-surcharge law is to ban *truthful*, *non-misleading* surcharges. But even if, counterfactually, the law were truly aimed at disclosure, that is just another way of saying that it regulates speech: liability would turn exclusively on what is "state[d]," AG Br. 34—not what is charged.

The Attorney General's second bid to avoid scrutiny is her argument that the law does not regulate any speech (misleading or otherwise) but instead "plainly governs what a retailer may *do*, i.e., charge a higher price, not what it may *say*." AG Br. 24. But, again, the statue expressly allows merchants to charge a higher price for using a credit card than for using cash. And it allows them to set the credit-card price for any item at any amount, and so too for the cash price. So what, exactly, does the law regulate if not how those prices are conveyed to consumers? And how, exactly, is that not speech? The Attorney General does not say.

Instead, she takes the position that the law can escape scrutiny because the "plain text" "does not implicate speech." *Id.* But if that were all it took to bypass the First Amendment, then state legislatures could ban all sorts of disfavored speech through clever drafting. Fortunately, that's not the law. Courts must consider a statue's "purpose and practical effect" to determine whether it restricts speech,

Sorrell, 131 S. Ct. at 2663, even if the statute "says nothing about speech on its face," *McCullen*, 134 S. Ct. at 2529.

Ultimately, the Attorney General's argument boils down to the basic proposition that "states have considerable discretion" to pass laws "involving pricing and rate regulations." AG Br. 25. We do not disagree. But the reason "pricing and rate regulations" generally do not implicate the First Amendment is that they actually regulate conduct—they "fix a maximum of charge to be made," for example, or otherwise regulate what is charged or paid for something. *Munn v. Illinois*, 94 U.S. 113, 125 (1876). California's law doesn't.

Consider the authorities the Attorney General cites (at 25-26) to support her argument. They involve laws that:

- prohibit unapproved "rent increases," *Yee v. City of Escondido*, 503 U.S. 519, 524 (1992);
- set a "maximum price for old gas," *Mobil Oil Exploration & Producing Se. Inc. v. United Distrib. Cos.*, 498 U.S. 211, 221 (1991);
- "fix[] the maximum compensation" a private agency may "collect," *Olsen v. Nebraska*, 313 U.S. 236, 241 (1942);
- "authorize[] the fixing of minimum wages," *W. Coast Hotel Co. v. Parrish*, 300 U.S. 379, 386 (1937);
- "fix minimum and maximum … retail prices to be charged" for milk, *Nebbia v. New York*, 291 U.S. 502, 515 (1932); and
- ban insurance commissions "in excess of a reasonable amount," *O'Gorman & Young, Inc. v. Hartford Fire Ins. Co.*, 282 U.S. 251, 255 (1931).

Although the Attorney General asserts (at 25) that these cases involved "statutes like section 1748.1," each one of these laws—unlike California's—directly regulates the total amount charged or paid for something.

If the no-surcharge law actually regulated prices—that is, if it capped the difference between the cash and credit prices, say, or banned dual pricing outright—then it would be a price-control law of the kind the Attorney General cites. And it surely would not trigger First Amendment scrutiny. But that's not this law. In California, merchants are free to set the credit-card price as they please; liability turns on labeling. That feature makes the no-surcharge law fundamentally different from every law the Attorney General cites, including those in the three cases on which she principally relies (at 26-28).

Start with *Glickman v. Wileman Bros. & Elliot, Inc.*, 521 U.S. 457 (1997), which considered whether a compelled subsidy for generic advertising of tree fruits violated the First Amendment. The law imposed "no restraint on the freedom of any producer to communicate any message to any audience" and did not require producers "themselves to speak," but instead "merely required [them] to make contributions for advertising" a "message with which [they did not] disagree." *Id.* at 469-71. The Court upheld the law over a compelled-speech challenge. It did so, however, not because the law didn't involve speech, but because any speech imposition was incidental to a "broader collective enterprise in which th[e]

freedom to act independently [wa]s already constrained by the regulatory scheme." *Id.* at 469. As the Court later explained: The *Glickman* decision "proceeded upon the premise that the producers were bound together" by a statute that "replaced competition with a regime of cooperation," which "Congress [found] to be necessary to maintain a stable market." *United States v. United Foods, Inc.*, 533 U.S. 405, 412-15 (2001). Thus, "the imposition upon their First Amendment right" was "the logical concomitant of a valid scheme of economic regulation." *Id.*

That is a world away from the no-surcharge law. Far from being ancillary to some larger economic scheme (much less one exempted from the antitrust laws and deemed necessary to maintain a stable market), the law regulates how merchants may communicate their prices to consumers, and nothing more. *See id.* at 411-12 (distinguishing *Glickman* and holding law unconstitutional because the speech imposition was "the principal object of the regulatory scheme").

Next is the hypothetical law "setting a minimum price for alcohol products" in *44 Liquormart*. AG Br. 27. That law clearly regulates conduct because it requires "higher prices" through "direct regulation." 517 U.S. at 507. Not so with the no-surcharge law, which permits merchants to charge any two different prices for cash versus credit, and demands only that the merchant use the state's preferred label.

Finally, there is *National Ass'n of Tobacco Outlets, Inc. v. City of Providence*, which involved a prohibition on "reducing prices" for cigarettes through "coupons and

certain multi-pack discounts." 731 F.3d 71, 74 (1st Cir. 2013). After reaffirming that "[p]ricing information concerning lawful transactions" is "protected speech," the court upheld the law because it does not "restrict[] retailers or anyone else from communicating pricing information," but instead regulates conduct. *Id.* at 76. Indeed, it effectively *bans* differential pricing by requiring retailers to charge all consumers the same price for every pack of cigarettes, regardless of whether the consumer uses a coupon or buys multiple packs. That is nothing like the no-surcharge law, which *allows* differential pricing based on how the consumer pays but regulates only how the difference is communicated.

Two last points. The Attorney General contends (at 30) that *Thrifty Oil Co. v. Superior Court*, 91 Cal. App. 4th 1070 (2d Dist. 2001), "undermines the central theme running through plaintiffs' claims, which is that any dual pricing scheme automatically involves an impermissible surcharge." That is not our argument. Our argument is that the legality of a dual-pricing scheme turns entirely on how it is *described*. Nothing in *Thrifty Oil* undermines that point.

The Attorney General also claims (at 28-29) that the First Amendment should not apply because merchants "remain[] free to discuss pricing practices" and "express themselves" in conversations with customers; they just can't call the cost of credit a "surcharge" on labeling and signs. But that is no basis for declining to apply scrutiny. Even assuming that California's law were so limited (and how is a

merchant to know, when Florida's law isn't?), the First Amendment protects more than just conversations. The way in which a merchant chooses to convey price information to consumers—on labels, signs, advertisements, and the like—*is itself speech*. And it's not just any speech, but speech at the heart of the commercial-speech doctrine. *See Va. Bd. of Pharmacy*, 425 U.S. at 770. "Pricing is a routine subject of economic regulation, but the manner in which price information is conveyed to buyers is quintessentially expressive, and therefore protected by the First Amendment." *Expressions*, 975 F. Supp. 2d at 445. Because the "Plaintiffs cannot frame their price how they would like, even though they are allowed to speak with their customers generally about the credit card industry and the merchant fees that the industry charges," the law restricts speech. ER10-11.[5]

The Second Circuit's recent decision holding otherwise fundamentally misunderstands this point. It rests on a belief that a law regulating what merchants put on their "sticker[s]"—but not what they actually charge consumers—"regulates conduct, not speech." *Expressions Hair Design v. Schneiderman*, 803 F.3d 94, 110 (2d Cir. 2015). But the court's own reasoning shows why that is not so: "If a consumer

[5] It does so, moreover, "in the forum most likely to capture [the] attention" of credit-card-paying customers—as a line item on the receipt. *BellSouth*, 542 F.3d at 505; *see also Motor Vehicle Mfrs. Ass'n v. Abrams*, 684 F. Supp. 804, 807 (S.D.N.Y. 1988). Communicating the cost of credit as a line item on the receipts of only those customers who pay in cash (which is what conveying the cost as a "discount" would do) is ineffective because those customers are *already* using cash.

thinks, based on a seller's sticker price, that she will be paying $100 for the seller's goods or services, then she will be annoyed if it turns out that she actually has to pay $103 simply because she has chosen to use a credit card; by contrast, if the sticker price is $103, she will be less annoyed by having to pay $103, even if cash customers only have to pay $100. Nothing about the consumer's reaction in either situation turns on any words uttered by the seller." *Id.* at 108.

That is mistaken. The consumer is "annoyed" in the first instance because she was misled by the sticker price (what the seller said the price was). As Judge Sutton has explained, something "cannot simultaneously be non-communicative" and "yet pose the risk of *communicating* a misleading message." *BellSouth*, 542 F.3d at 510. Even if the merchant said nothing aloud, the way in which a merchant chooses to convey "price information" to consumers is protected speech. *Va. Bd. of Pharmacy*, 425 U.S. at 770.[6]

Misleading commercial speech can of course be regulated. But that's because it gets no constitutional protection—not because it's not speech. *Cent. Hudson Gas &*

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[6] The Second Circuit compounded its error by distinguishing between what it called a "single-sticker-price scheme" and a "'dual-price' scheme." 803 F.3d at 104. But *both* are dual-pricing schemes; the only difference is how the credit-card price is *communicated* (as an additional charge on a sign versus a sticker price). And although the court invoked *Pullman* abstention, this Court has repeatedly held that *Pullman* abstention is "almost never" permitted "in First Amendment cases 'because the guarantee of free expression is always an area of particular federal concern.'" *Courthouse News Serv. v. Planet*, 750 F.3d 776, 784 (9th Cir. 2014); *see Dombrowski v. Pfister*, 380 U.S. 479, 489-90 (1965); *Houston v. Hill*, 482 U.S. 451, 467-68 (1987).

Elec. Corp. v. Pub. Serv. Comm'n of N.Y., 447 U.S. 557, 566 (1980). The plaintiffs here, however, wish to convey truthful, *non*-misleading information: to frame the cash price as the "sticker" price and the price difference as a "surcharge." Because the law restricts that speech, it is subject to heightened scrutiny, which it cannot survive.

B. The no-surcharge law cannot survive intermediate scrutiny.

In recent years, the Supreme Court has left open the question of what form of "heightened scrutiny" applies to restrictions on commercial speech. *Sorrell*, 131 S. Ct. 2667. But because the no-surcharge law fails scrutiny even if subject to a "special commercial speech inquiry," *id.*—that is, even under "pre-*Sorrell*, arguably more government-friendly, precedent"—this Court can "defer extended discussion of *Sorrell* for a more appropriate case." *Valle del Sol Inc. v. Whiting*, 709 F.3d 808, 821 (9th Cir. 2013).

Commercial speech is traditionally subject to intermediate scrutiny under the *Central Hudson* test, which asks four questions: (1) whether the speech "concern[s] lawful activity and [is] not . . . misleading"; (2) "whether the asserted governmental interest" justifying the regulation "is substantial"; (3) "whether the regulation directly advances the governmental interest asserted"; and (4) whether the challenged law "is not more extensive than is necessary to serve that interest." 447 U.S. at 566.

Courts "must review the [state's law] with 'special care,' mindful that speech prohibitions of this type rarely survive constitutional review." *44 Liquormart*, 517 U.S. at 504. The state's burden is "heavy," *id.* at 516, requiring actual evidence, not speculation and conjecture, that each *Central Hudson* factor is satisfied. *Edenfield v. Fane*, 507 U.S. 761, 770-71 (1993). California cannot meet its burden here. Its law "founders at every step." *Dana's R.R. Supply*, 2015 WL 6725138, *9.

1. Dual pricing is legal, and calling the price difference a credit-card "surcharge" is not inherently misleading.

Dual pricing based on whether consumers pay with cash or credit is legal in California. Because that conduct is authorized, speech that simply describes it in a particular way "does not advance an illegal transaction." *BellSouth*, 542 F.3d at 506.

Nor is it "inherently misleading" for the merchant to call the price difference a "surcharge." *In re R.M.J.*, 455 U.S. 191, 203 (1982); *see BellSouth*, 542 F.3d at 506. "Calling the additional fee paid by a credit-card user a *surcharge* rather than a *discount* is no more misleading than is calling the temperature *warmer* in Savannah rather than *colder* in Escanaba." *Dana's R.R. Supply*, 2015 WL 6725138, *9. When a merchant has a dual-pricing system, customers pay more to use a credit card. The merchant does not mislead customers when it informs them of this fact by truthfully characterizing the price difference as a credit "surcharge." Quite the contrary, "if the retailer displayed information about the surcharge throughout the

store and noted that the surcharge was due to the merchant fees, this speech would not be misleading, but would actually be informative and accurate." ER13.

2. The state has no legitimate interest in obscuring the cost of credit-card transactions from consumers.

Because California has no legitimate interest in keeping consumers in the dark about the cost of credit, the state cannot satisfy the second prong. "Unlike rational-basis review, the *Central Hudson* standard does not permit [courts] to supplant the precise interests put forward by the State with other suppositions," or to "turn away if it appears that the stated interests are not the actual interests served by the restriction." *Edenfeld*, 507 U.S. at 768. The Court's analysis, therefore, must be confined to interests actually offered by the state.

California's law says that it seeks to "protect consumers from deceptive price increases." Cal. Civ. Code § 1748.1(e). This asserted rationale, of course, is about speech—not conduct. *BellSouth*, 542 F.3d at 510. But it is also at best a hypothetical concern, which is insufficient under *Central Hudson*. The state's burden cannot be "satisfied by mere speculation or conjecture; rather, a government body seeking to sustain a restriction on commercial speech must demonstrate that the harms it recites are real and that its restrictions will in fact alleviate them to a material degree." *Edenfield*, 507 at 770-71; *see Ibanez v. Fla. Dep't of Bus. & Prof'l Reg.*, 512 U.S. 136, 146 (1994) ("[R]ote invocation of the words 'potentially misleading' does not relieve the state's burden to demonstrate that the harms it recites are real and that

its restriction will in fact alleviate them to a material degree."). A state "must ensure that its fear of consumer confusion is real" before taking the radical step of banning speech. *BellSouth*, 542 F.3d at 509. Here, California has offered nothing.

3. The no-surcharge law does not directly advance any legitimate state interest.

The third prong requires the state to show that the law directly advances the state's asserted interest—that is, that the government's means and ends align. *Edenfield,* 507 U.S. at 771. This prong "seeks to ferret out whether a law ostensibly premised on legitimate public policy objectives in truth serves those objectives." *BellSouth*, 542 F.3d at 507. Here, too, California's law comes up short. It does not directly advance any interest in consumer protection.

If California were really concerned about preventing hidden costs, then it could allow merchants to highlight the extra cost of credit by labeling it a "surcharge" and insist that it be prominently disclosed to consumers, as Minnesota does. *See* Minn. Stat. § 325G.051(1)(a). But California instead requires merchants to label the additional cost in the way that best conceals it. By doing so, the law "actually perpetuates consumer confusion by preventing sellers from using the most effective means at their disposal to educate consumers about the true costs of credit-card usage." *Expressions*, 975 F. Supp. 2d at 446.

In this way, the no-surcharge law undermines the very interests that the commercial-speech doctrine is designed to protect: the "public interest" in the "free

flow of commercial information" to foster "intelligent and well informed" economic decisions by consumers. *Va. Bd. of Pharmacy*, 425 U.S. at 765. When a merchant uses a dual-pricing system, a consumer can reduce the final price paid by paying in cash. Yet the no-surcharge law prohibits the merchant from telling consumers that they will incur an added cost for using credit. "It would be perverse to conclude that a statute that keeps consumers in the dark about avoidable additional costs somehow 'directly advances' the goal of preventing consumer deception." *Expressions*, 975 F. Supp. 2d at 446.

The law is also riddled with "exemptions and inconsistencies [that] bring into question the purpose of the labeling ban." *Rubin v. Coors Brewing Co.*, 514 U.S. 476, 489 (1995). Tellingly, California exempts *itself* from the law. *See* Cal. Gov. Code § 6159(h) (permitting "a court, city, county, city and county, or any other public agency" to "impose a fee for the use of a credit … card"); Cal. Civ. Proc. Code § 1010.5 (permitting California state courts to impose credit-card surcharges on fax filings); Cal. Food & Agr. Code § 31255(b) (permitting state animal-control officers to impose credit-card surcharges). And the no-surcharge law, by its own terms, "does not apply to charges for payment by credit card or debit card that are made by an electrical, gas, or water corporation and approved by the Public Utilities Commission." Cal. Civ. Code § 1748.1(f).

"*Central Hudson* requires a logical connection between the interest a law limiting commercial speech advances and the exceptions a law makes to its own application." *Valle del Sol*, 709 F.3d at 824. What is the connection here? "If this speech is so deceptive and harmful, why is the government allowed to engage in it?" ER13.[7]

These self-serving exemptions "betray[] the frailty" of any asserted anti-deception interest. *Dana's R.R. Supply*, 2015 WL 6725138, *10. The state can "present[] no convincing reason for pegging its speech ban to the identity" of the entity imposing the surcharge. *Greater New Orleans Broad. Ass'n, Inc. v. United States*, 527 U.S. 173, 191 (1999); *see Valley Broad. Co. v. United States*, 107 F.3d 1328, 1334-36 & n.9 (9th Cir. 1997) (holding that a law's "myriad exceptions precludes [it] from directly advancing the government's purported interest" under *Central Hudson*, and declaring it unconstitutional without "reach[ing] the final prong").

[7] *See, e.g.*, State of California Franchise Tax Board, Pay By Credit Card for Individuals, *at* http://bit.ly/1l820Et (imposing "convenience fee" of "2.3% of the tax amount charged" to use a credit card); City & County of San Francisco, Property Tax Payments, *at* http://bit.ly/1yCUMIQ (imposing "convenience fee of 2.25% for credit card payments" of property taxes); City of Huntington Beach, Make a Payment, *at* http://bit.ly/XlHXre (imposing "$3 convenience fee for paying [parking tickets] by credit card"); San Francisco Public Utilities Commission, Payment Options, *at* http://bit.ly/1BiD5CD ("Credit card payments [of public-utility bills] will incur an additional charge of $5.80.")

4. The no-surcharge law is far more extensive than necessary to serve any legitimate state interest.

The state's biggest problem, however, is that the no-surcharge law is far more extensive than necessary to achieve the state's purported goals, thus failing the final *Central Hudson* prong. "[I]f there are numerous and obvious less-burdensome alternatives to the restriction on commercial speech, that is certainly a relevant consideration in determining whether the 'fit' between ends and means is reasonable." *City of Cincinnati v. Discovery Network, Inc.*, 507 U.S. 410, 417 n.13 (1993). Here, "the prohibition against the use of words which could be used to present the information about the surcharge in an accurate and non-misleading manner [is] broader than necessary to prevent the description from being potentially misleading." *Capital Leasing of Ohio, Inc. v. Columbus Municipal Airport Authority,* 13 F. Supp. 2d 640, 669 (S.D. Ohio 1998).

To be clear, we agree that merchants should not impose an undisclosed surcharge or surprise consumers by waiting until the point of sale to inform them of a surcharge. But it is equally clear that the state did not need to enact a new law to prevent that sort of deception. It "already has laws on the books prohibiting false advertising and deceptive acts and practices." *Expressions*, 975 F. Supp. 2d at 447; *see* Cal. Bus. & Prof. Code §§ 17200, 17500. Because the state could address any legitimate concern about consumer deception simply by enforcing its own existing laws, the no-surcharge law is unnecessary. *See BellSouth*, 542 F.3d at 508 ("Even

granting the Commonwealth's assumption that [consumer deception] was a potential problem, . . . why not first enforce existing state law on the point?").

Even if those laws were not already on the books, the no-surcharge statute would still go too far. The statute pointedly "does not limit itself to a prohibition on false or misleading statements as to the charges imposed." *Abrams*, 684 F. Supp. at 807. It regulates all speech framed as a surcharge, no matter how truthful. "States may not place an absolute prohibition" on information that is merely "potentially misleading . . . if the information also may be presented in a way that is not deceptive," as it can be here. *R.M.J.*, 455 U.S. at 203.

If the state were truly worried about consumers being misled by undisclosed surcharges, then "mandating disclosure of surcharges would be the most direct way to prevent consumer deception." ER14 (citing Minn. Stat. § 325G.051(1)(a)). That would accomplish the state's purported objective without "offend[ing] the core First Amendment values of promoting efficient exchange of information." *Nat'l Elec. Mfrs. Ass'n v. Sorrell*, 272 F.3d 104, 113-14 (2d Cir. 2001). Or the state "could have limited its regulation to surcharges that are deceptive and misleading." *Expressions*, 975 F. Supp. 2d at 447. But what it "cannot do, as a constitutional matter, is what its no-surcharge law does: abridge protected speech." *Dana's R.R. Supply*, 2015 WL 6725138, *10; *see also Peel v. Attorney Registration & Disciplinary Comm'n of Ill.*, 496 U.S. 91, 109 (1990).

III. California's no-surcharge law is impermissibly vague.

The law is also too vague. Any law that "fail[s] to give persons of ordinary intelligence adequate notice of what conduct is proscribed" or that "permit[s] or authorize[s] 'arbitrary and discriminatory enforcement'" is void for vagueness. *G.K. Ltd. Travel v. City of Lake Oswego*, 436 F.3d 1064, 1084 (9th Cir. 2006) (quoting *Hill v. Colorado*, 530 U.S. 703, 732 (2000)). These "vagueness concerns are more acute when a law implicates First Amendment rights and, therefore, vagueness scrutiny is more stringent." *Id.* This law cannot survive that stringent scrutiny.

Put yourself in the merchant's shoes. Suppose you offer dual pricing, and you decide to sell a product for $100 if the customer pays in cash and $102 if the customer pays with credit. How do you comply with the law? What can you say? Can you list the price as "$100+2% surcharge"? ER16. "Does that scenario constitute an unlawful surcharge since the percentage is calculated at the cash register?" *Id.* What if you listed the price as $100, but put up "large signs displayed throughout the establishment stating that a 2% surcharge will be applied for purchases made with credit cards?" *Id.* And what if one of your customers calls and asks for your prices? What do you tell them? If she asks you whether you charge more for paying with a credit card, what do you say?

Although the Attorney General dismisses these questions as "hypothetical," AG Br. 39, they "represent legitimate concerns that retailers must face when

determining whether to impose a legal dual-pricing system." ER16. Customers will ask questions about it, and merchants need to know how to respond. *Fulvio* shows these fears to be well founded: The merchant there posted a sign that clearly displayed both the cash and credit prices for gas and instructed his employees to tell customers only that he offered a cash discount. 517 N.Y.S.2d at 1010, 1013. Yet he was prosecuted because his cashier told a customer that it was "five cents 'extra'" to use credit rather than a "nickel less" to use cash. *Id.*

Courts have recognized the difficulty in determining the meaning of no-surcharge laws. *See In re Payment Card Interchange Fee & Merchant Discount Antitrust Litig.*, 986 F. Supp. 2d 207, 232 (E.D.N.Y. 2013) ("No-surcharge laws are not only anti-consumer, they are arguably irrational."); *Expressions*, 975 F. Supp. 2d at 435 ("*Alice in Wonderland* has nothing on [the no-surcharge law]."); *Fulvio*, 517 N.Y.S.2d at 1012 (holding that the no-surcharge law, by prohibiting credit surcharges but permitting cash discounts, is "so vague, uncertain and arbitrary of enforcement as to be fatally defective"). A California appellate court, in trying to decipher the scope of section 1748.1, sensibly refused to interpret it as covering a gas station that prominently disclosed two prices for gas—a "cash" price and a "credit" price—while saying nothing else. *Thrifty Oil*, 91 Cal. App. 4th at 1077. "To conclude otherwise in this case," the court reasoned, "would mean that every two-tier

pricing system includes an unlawful surcharge." *Id.* The court explained that its construction was necessary to avoid "mischief or absurdity." *Id.*

That seems fair enough, but what if a customer had asked the gas station for its prices, and the cashier responded by saying that credit costs "extra" or "more"? What result then? Under other states' identical no-surcharge laws, that speech would be unlawful. *See Dana's R.R. Supply*, 2015 WL 6725138, *1 ("[A] simple slip of the tongue calling the same price difference a *surcharge* runs the risk of being fined and imprisoned"); *Fulvio*, 517 N.Y.S.2d at 1010, 1014 ("[It] is intolerable" that a merchant violates the law if it "is careless enough to describe the higher price in terms which amount to the 'credit price' having been derived from adding a charge to the lower price.").

Is California's law different? If so, what explains the difference? How can two indistinguishable state laws have two different meanings? And if they do, then what does California's law prohibit? And how is a merchant like Stonecrest, which uses a dual-pricing system, to know? What can it look to when trying to communicate its prices to customers? What about those charged with enforcement of the law? What standards should they use, and where do they come from? That none of these questions can be answered with any confidence, let alone by the clear text of the statute, is proof enough of its vagueness.

CONCLUSION

The district court's judgment should be affirmed.

Respectfully submitted,

/s/ Deepak Gupta

Deepak Gupta
Jonathan E. Taylor
GUPTA WESSLER PLLC
1735 20th Street, NW
Washington, DC 20009
(202) 888-1741

Mark Wendorf
REINHARDT, WENDORF & BLANCHFIELD
332 Minnesota Street
St. Paul, MN 55101
(651) 287-2100

Kevin K. Eng
MARKUN ZUSMAN FRENIERE & COMPTON LLP
465 California Street, 5th Floor
San Francisco, CA 94101
(415) 438-4515

Counsel for Plaintiffs-Appellees

December 14, 2015

CERTIFICATE OF SERVICE

I hereby certify that on December 14, 2015, I electronically filed the foregoing Brief for Plaintiffs-Appellees with the Clerk of the Court of the U.S. Court of Appeals for the Ninth Circuit by using the Appellate CM/ECF system. All participants are registered CM/ECF users, and will be served by the Appellate CM/ECF system.

/s/ Deepak Gupta
Deepak Gupta

CERTIFICATE OF COMPLIANCE WITH RULE 32(a)(7)

I hereby certify that my word processing program, Microsoft Word, counted 13,264 words in the foregoing brief, exclusive of the portions excluded by Rule 32(a)(7)(B)(iii).

/s/ Deepak Gupta

December 14, 2015 Deepak Gupta

STATEMENT OF RELATED CASES

As required by Circuit Rule 26-2.6, Plaintiffs-Appellees state that they are not aware of any case pending before this Court that presents related legal issues.