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SUPERIOR COURT OF THE STATE OF CALIFORNIA

COUNTY OF LOS ANGELES, CENTRAL DISTRICT

OPPORTUNITY FINANCIAL, LLC,

Plaintiff,

v.

CLOTHILDE HEWLETT, in her official capacity as Commissioner of the Department of Financial Protection and Innovation for the State of California,

Defendant.

And Related Cross-Actions.

Case No. 22STCV08163

Assigned for All Purposes to:
Hon. Timothy P. Dillon, Dept. 73

OPPORTUNITY FINANCIAL, LLC'S OPPOSITION TO CLOTHILDE HEWLETT AND DEPARTMENT OF FINANCIAL PROTECTION AND INNOVATION'S DEMURRER OR, IN THE ALTERNATIVE, MOTION TO STRIKE

Date: February 16, 2023
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I. INTRODUCTION

The Court should overrule Commissioner Clothilde Hewlett's (the "Commissioner") and the Department of Financial Protection and Innovation's ("DFPI") (collectively, "Cross-Defendants") Demurrer because it mischaracterizes Opportunity Financial LLC's ("OppFi") Cross-Complaint and improperly disputes its factual allegations. In doing so, it violates the cardinal rule of pleading challenges: it fails to accept as true OppFi's allegations. For that reason, among others, it fails.

In its Cross-Complaint, OppFi alleges that after the Legislature passed Assembly Bill 539 in 2019 Cross-Defendants secretly adopted a policy of applying **a particular form** of the "true lender doctrine" to determine the applicability of interest rate caps and exemptions thereto under the California Financing Law ("CFL"). (OppFi Cross-Compl., ¶¶ 1, 4, 6-8.) Pursuant to this policy, the "primary factor" in applying the CFL's interest rate caps and exemptions is "which entity – bank or non-bank – has the predominant economic interest in the transaction." (*Id*.) OppFi alleges that Cross-Defendants intend to apply this test "generally, rather than in a specific case" and that it applies to nondepositories that partner with state and national banks, which includes, but is not limited to, OppFi. (*Id*. ¶¶ 6, 25, 46.) Under this policy, OppFi alleges that Cross-Defendants will deem the entity with the predominate economic interest in the transaction the lender for purposes of applying the CFL's interest rate caps. (*Id*.) OppFi alleges that Cross-Defendants have applied this policy to OppFi and, at least one other entity, LoanMart, but, again, the policy is not limited to either OppFi or LoanMart. (*Id*. ¶¶ 25, 46.) OppFi further alleges that, despite adopting this policy, Cross-Defendants did not comply with the Administrative Procedure Act ("APA"), Cal. Gov. Code, § 11340 *et seq*. As such, the policy amounts to an underground regulation.

Cross-Defendants' Demurrer does not meaningfully engage with OppFi's allegations. Instead, in an effort to argue that the alleged policy is not a "regulation" under the APA, Cross-Defendants characterize OppFi's Cross-Complaint as merely challenging "the Commissioner's inquiry into the true lender of OppFi's OppLoans." (Cross-Defs.' Mem. in Supp. of Dem. ("Mem.") at 1.) On that basis, Cross-Defendants argue that the alleged policy is not one of general application. But that is just a mischaracterization of OppFi's allegations. OppFi alleges that the DFPI's true lender policy is intended by Cross-Defendants to apply generally, not just against OppFi. To the

extent Cross-Defendants disagree, a demurrer is not the proper vehicle to resolve the dispute. Indeed, as the case law makes clear, the fact that an agency reveals a policy in the context of a particular adjudication "does not alter its character as a policy of general application and thus a regulation." (*Tidewater Marine W., Inc. v. Bradshaw* (1996) 14 Cal.4th 557, 573.)

Cross-Defendants also argue that their true lender policy is not a "regulation" because in pursuing an enforcement action against OppFi, the Commissioner was merely applying California's preexisting "substance over form" doctrine. This argument suffers from the same fatal flaw as the Cross-Defendants' first argument—it improperly construes OppFi's Cross-Complaint as challenging just the Commissioner's enforcement action against OppFi. It fails for that reason alone. It also fails because it mischaracterizes the alleged policy. OppFi does not allege that the Commissioner was merely applying California's substance over form doctrine, but, instead, that it applied a specific true lender test focused on the entity with the predominate economic interest in the transaction. Again, on demurrer, Cross-Defendants cannot rewrite OppFi's Cross-Complaint, ignore its factual allegations, or dispute them.

Cross-Defendants' last argument is that the Cross-Complaint is procedurally improper. This argument is meritless. As set forth below, under Code of Civil Procedure sections 428.1, 428.5, and 426.3, OppFi was not only entitled, but arguably required, to assert its claims in a cross-complaint. It is a procedurally appropriate vehicle to assert its claims challenging Cross-Defendants' underground regulation. For these reasons, the Court should overrule Cross-Defendants' Demurrer.

II. BACKGROUND

A. OppFi's Cross-Complaint.

OppFi filed its Cross-Complaint on October 17, 2022, at the same time it answered the Commissioner's Cross-Complaint. OppFi's Cross-Complaint "challenges the DFPI's adoption of the so-called 'true lender doctrine' to determine the applicability of the interest rate caps in the [CFL]." (OppFi Cross-Compl., ¶ 1.) OppFi alleges that Cross-Defendants adopted a particular form of the true lender doctrine in which the "primary factor" is "which entity – bank or non-bank – has the predominant economic interest in the transaction." (*Id*. ¶ 4.) The DFPI's analysis also includes evaluating "which entity actually performs lender roles, such as marketing and servicing." (*Id*.)

OppFi alleges that Cross-Defendants intend to apply their true lender policy to nondepositories that partner with state and national banks, rather than in a specific case. (*Id*. ¶¶ 6, 23, 28, 46 [alleging that "DFPI has adopted a generally applicable rule of interpretation, which among other things, provides that applicability of the bank exemption turns on which entity has the predominant economic interest"].) OppFi and LoanMart are ***examples*** of the Cross-Defendants' application of this policy, but the policy is not limited to either of them. (*Id*. ¶¶ 25, 46.) Ultimately, as a policy of general application, OppFi alleges that it can be applied to any entity to determine that it is the so-called "true lender" and, therefore, subject to the CFL's interest rate restrictions. (*Id*.)

The Cross-Complaint explains that the DFPI's adoption of a true lender doctrine was marked by the Legislature's passage of AB 539. Prior to then, it was clearly understood that California law did not regulate bank partnerships. Indeed, the legislative history of AB 539 demonstrates that the Legislature knew that bank partnerships were not subject to the CFL's interest rate caps.[1] In other words, the Legislature understood that the true lender doctrine does not apply to nondepositories who partner with banks and that AB 539 was not intended to, and did not, change that.

As soon as AB 539 was passed, Cross-Defendants and their predecessors began touting AB 539 as a weapon to use against non-depositories that partner with banks. (*Id*. ¶ 7.) But AB 539 did nothing to change the law with respect to bank partnerships and it said nothing about the "true lender doctrine" that OppFi alleges the DFPI adopted. It merely sets maximum interest rates for loans between $2,500 and $10,000. (*Id*. ¶ 21.) Before AB 539, the CFL already set maximum interest rates for loans between $2,500 and $10,000. (*Id*.)

Despite touting AB 539 as a weapon to use against nondepositories that partner with banks, Cross-Defendants did not provide the public with any information about how they would use AB 539 to do so. That is because DFPI knew that AB 539 had no application to bank partnerships at all. Instead, the Cross-Complaint alleges that the "DFPI adopted the true lender doctrine without any

[1] (California Financing Law: Consumer Loans: Charges: Hearing on AB 539 Before the S. Comm. on Banking and Fin. Insts., 2019 Leg., Reg. Sess. 1 (Cal. 2019), https://leginfo.legislature.ca.gov/faces/billAnalysisClient.xhtml?bill_id=201920200AB539 (accessed by clicking on "06/24/19 - Senate Banking and Financial Institutions" hyperlink) [noting that the CFL does not apply to nondepositories partnering with banks and that they are legally able to offer installment loans to Californians without having to be licensed under the CFL].)

formal notice at all, much less fair or adequate notice, and without complying with the APA." (*Id.* ¶ 7.) As the California agency charged with enforcing the CFL, Cross-Defendants had an obligation to comply with the APA's requirements before adopting the true lender doctrine. (*Id.*) More specifically, "[a]s an administrative agency, DFPI had a clear, present, and ministerial duty to provide notice of the proposed regulation, provide a public hearing if requested, provide for an opportunity for interested persons to submit written comments if no hearing was held, and to respond in writing to those comments. (*Id.* ¶ 50.) The Commissioner likewise had a clear, present, and ministerial duty to ensure DFPI's compliance with the APA's rulemaking provisions." (*Id.*) Cross-Defendants failed to comply with any of these requirements.

B. The Commissioner's *Ex Parte* Application to Strike the Cross-Complaint.

On October 19, 2022, the Commissioner filed an *ex parte* application to strike OppFi's Cross-Complaint claiming that OppFi should have sought leave to file an amended complaint. The Court denied the Commissioner's application as it did not meet the standards for *ex parte* relief.

C. The Demurrer.

Cross-Defendants' demurrer asserts three arguments. First, Cross-Defendants argue that the alleged policy is not a "regulation" within the meaning of the APA because "the Commissioner's enforcement action against OppFi is based on the specific facts of OppFi's 'OppLoans' program and is not one of general application." (Mem. at 2.) Second, Cross-Defendants argue that the alleged policy is not a regulation within the meaning of the APA because "the Commissioner is applying long-standing California law to the specific facts of OppFi's loan program with FinWise Bank." (*Id.*) Third, Cross-Defendants argue that "OppFi should not be allowed to utilize two concurrently operative complaints in the same proceedings on the same set of facts." (*Id.* at 3.) As set forth above and below, these arguments are meritless.

III. ARGUMENT

A. Legal Standard

As a matter of law, a demurrer admits the truth of all material factual allegations of the complaint and all facts that may be implied or inferred from those expressly alleged in the complaint. (*Alameda County Land Use Assn. v. City of Hayward* (1995) 38 Cal.App.4th 1716, 1722; *Buchanan*

v. Maxfield Enterprises, Inc. (2005) 130 Cal.App.4th 418, 420–421.) Accordingly, in evaluating a demurrer, the court must accept the allegations of the complaint as true. (*Del. E. Webb Corp. v. Structural Materials Co*. (1981) 123 Cal.App.3d 593, 604.) Moreover, "a plaintiff is required only to set forth the essential facts of his case with reasonable precision and with particularity sufficient to acquaint a defendant with the nature, source and extent of his cause of action." (*Doheny Park Terrace Homeowners Assn. Inc. v. Truck Ins. Exchange* (2005) 132 Cal.App.4th 1076, 1099.) And where the "defendant has superior knowledge of the facts" the plaintiff may plead with "less particularity" so long as the pleading gives notice of the issues sufficient to enable preparation of a defense. (*Okun v. Superior Court* (1981) 29 Cal.3d 442, 458.) Ultimately, if plaintiff's factual allegations and all facts that may implied from them "reveal an actual controversy exists between the parties, the complaint is legally sufficient for declaratory relief." (*Alameda County Land Use Assn.*, 38 Cal.App.4th at p. 1722.)

B. OppFi's Cross-Complaint Pleads Sufficient Facts to Demonstrate an Underground Regulation.

1. The APA's Requirements for an Agency's Adoption of a Regulation.

The APA establishes "basic minimum procedural requirements for the adoption, amendment, or repeal of administrative regulations" by state agencies in California. (Cal. Gov. Code, § 11346.) The APA's rulemaking requirements promote its "goals of bureaucratic responsiveness and public engagement in agency rulemaking." (*Morning Star Co. v. State Bd. of Equalization* (2006) 38 Cal.4th 324, 333.) "One purpose of the APA is to ensure that those persons or entities whom a regulation will affect have a voice in its creation . . . , as well as notice of the law's requirements so that they can conform their conduct accordingly." (*Tidewater Marine W., Inc.*, *supra*, 14 Cal.4th at p. 568-569.)

A regulation subject to the APA has two identifying characteristics. *First*, a regulation has general application. (*Id.* at p. 571.) *Second*, a regulation "'implement[s], interpret[s], or make[s] specific the law enforced or administered by [the agency]'" or governs the agency's procedure. (*Id.* [quoting Cal. Gov. Code, § 11342.600].) An agency may not use or enforce any regulation that was not adopted pursuant to the APA's rulemaking requirements. (Cal. Gov. Code,

§ 11340.5, subd. (a).) A regulation adopted without compliance with these requirements is known as an "underground regulation" and may deemed invalid by a court. (*Bollay v. Off. of Admin. Law* (2011) 193 Cal.App.4th 103, 106.)

Accordingly, "absent an express exception, the APA applies to all generally applicable administrative interpretations of a statute." (*Morning Star Co.*, *supra*, 38 Cal.4th at p. 335.) Thus, an agency's policy of general application that interprets the law the agency is charged with enforcing is a regulation subject to the APA. (*Tidewater Marine W., Inc.*, *supra*, 14 Cal.4th at pp. 572-573 [agency's policy that wage orders applied to crews of certain vessels was a rule of general application that interpreted the law the agency enforces by determining the scope of the wage orders and thus was a regulation]; *Morning Star Co.*, *supra*, 38 Cal.4th at p. 334-335 [agency's unwritten determination that all businesses with 50 or more employees "use, generate, store, or conduct activities" related to hazardous materials and thus were subject to hazardous waste fee was a regulation].) In particular, "[a]n unwritten, generally applicable interpretation of an ambiguous statute 'amount[s] to a regulation' subject to the APA." (*Capen v. Shewry* (2007) 155 Cal.App.4th 378, 383 [citation omitted].)

2. DFPI's True Lender Policy Is a Regulation.

OppFi alleges that DFPI has adopted a policy that, to determine the lender of a loan for purposes of the CFL's interest rate caps and/or for purposes of determining the application of the CFL's exemptions, it is necessary to apply the "true lender doctrine." (OppFi Cross-Compl., ¶ 44.) According to the Commissioner, the primary factor in the analysis is "which entity—bank or non-bank—has the predominant economic interest in the transaction." (Comm. Cross-Compl., ¶ 18.) The Cross-Complaint alleges sufficient facts to demonstrate that DFPI's policy has the two necessary characteristics of a regulation.

First, OppFi alleges facts showing that DFPI's policy is one of general application. (See *Tidewater Marine W., Inc.*, *supra*, 14 Cal.4th at p. 571.) OppFi alleges that DFPI has adopted the true lender test to determine whether ***any*** nondepository working with a state or national bank is subject to the CFL's rate caps, not merely whether OppFi is subject to the CFL for the loans challenged by the Commissioner's Cross-Complaint. (OppFi Cross-Compl., ¶ 46.) In support of

its assertion that the DFPI's true lender policy applies generally, OppFi's Cross-Complaint points to statements made by DFPI personnel, the DFPI's prior enforcement positions, and the enforcement actions against OppFi and LoanMart. (*Id.* ¶¶ 25-26, 30, 46.) These allegations provide further factual support for OppFi's allegation that DFPI's policy applies "generally, rather than in a specific case." (*Tidewater Marine W., Inc.*, *supra*, 14 Cal.4th at p. 571.) Moreover, contrary to the Commissioner's allegations, OppFi's Cross-Complaint is not limited to the "Commissioner's inquiry into the true lender of OppFi's OppLoans." (Mem. at 1.) Instead, OppFi contends that Commissioner's enforcement action against OppFi is just one illustration of DFPI's implementation of the underground regulation. As noted above, the fact that an agency reveals its policy in the context of an enforcement action "does not alter its character as a policy of general application and thus a regulation." (*Tidewater Marine W., Inc.*, *supra*, 14 Cal.4th at p. 573.)

Second, OppFi alleges facts showing that DFPI's policy interprets or implements the CFL. (*Tidewater Marine W., Inc.*, *supra*, 14 Cal.4th at p. 571.) OppFi alleges that DFPI's adoption of the true lender doctrine is an interpretation or implementation of section 22009 or section 22050 of the CFL or both. (OppFi Cross-Compl., ¶¶ 45-46.) Section 22009 *extends* the CFL's interest rate caps to any "finance lender," which the statute defines to mean "any person who is engaged in the business of making consumer loans or making commercial loans." (Cal. Fin. Code, § 22009.) Section 22050 expressly *excludes* from CFL's interest rate caps "any person doing business under any law of any state or of the United States relating to banks." (Cal. Fin. Code, § 22050, subd. (a).) As OppFi alleges, DFPI's adoption of the true lender doctrine guides the determination whether the CFL's interest rate caps in section 22009 or the bank exemption in section 22009 applies based on whether a particular entity has the predominant economic interest in the loan at issue. (OppFi Cross-Compl., ¶ 46.) OppFi thus alleges that DFPI's true lender doctrine interprets or implements the CFL by delineating the scope of the statute.

3. The DFPI's Demurrer Fails Because It Mischaracterizes OppFi's Cross-Complaint and Disputes OppFi's Factual Allegations.

The DFPI does not contend that it complied with the APA's notice requirements or that any statutorily recognized exception applies. (Mem. at 1-13.) Instead, the DFPI argues (1) that "the

Commissioner's enforcement action against OppFi is based on the specific facts of OppFi's 'OppLoans' program and is not one of general application" and (2) that "California common law has long recognized the need to identify the actual lender of money, or true lender, in potentially usurious transactions by looking at substance rather than form." (*Id*. at 2.) Neither of these arguments holds water.

(a) OppFi's Cross-Complaint Challenges DFPI's General Application of the True Lender Doctrine, Not Merely the Commissioner's Enforcement Action Against OppFi.

DFPI's first argument fails because OppFi has not alleged that the DFPI's enforcement action against OppFi is, in and of itself, a regulation. Instead, OppFi alleges that the enforcement action is an illustration of the DFPI's unwritten and secret true lender policy. And that this true lender policy applies generally to all nondepositories providing services to state and national banks.

Cross-Defendants nonetheless insist that interpretations or applications of existing California law are not underground regulations and that the "Commissioner's cross-complaint is based upon evaluating the facts surrounding OppLoans in light of California caselaw and statutes." (Mem. at 6.) These contentions do not withstand scrutiny. Again, DFPI improperly construes OppFi's Cross-Complaint as challenging just the Commissioner's enforcement of the CFL against OppFi, but, as noted above, OppFi is alleging the existence of a policy that applies more generally. In addition, DFPI conflates the interpretation of a regulation with the adoption of a new regulation. An agency may "construe the words" of a validly issued regulation without violating the APA, but it cannot create "new conditions" or "new rules" that apply generally without complying with the APA. (*Aguilar v. Association for Retarded Citizens* (1991) 234 Cal.App.3d 21, 28.)

Here, OppFi alleges that DFPI applies the true lender doctrine, focused on the entity with the predominate economic interest, to determine who the finance lender is for purposes of CFL section 22009 and/or whether the state bank exemption applies under CFL section 22050. The true lender doctrine is not compelled by the plain language of either provision of the CFL or any validly issued regulation. (Cf. *Morning Star Co.*, *supra*, 38 Cal.4th at p. 336 ["[a]s the APA establishes that 'interpretations' typically constitute regulations," an agency's interpretation need not comply with the APA only where "the agency's actions or decisions in applying the law are essentially rote,

ministerial, or otherwise patently compelled by, or repetitive of, the statute's plain language"].) Instead, it creates a new condition for application of these statutes, specifically the condition that for the state bank exemption to apply—that is, to be the "true lender" —the state bank must maintain the predominate economic interest in the loan and must maintain that interest indefinitely. But DFPI points to nothing in California law that previously has defined the predominate economic interest test or articulated when and for how long a lender must retain the predominate economic interest. Under the APA, this policy is a regulation.

The cases DFPI cites are of no help. (See e.g., Mem. at 6 [citing cases].)[2] In *Aguilar*, the agency promulgated a valid Wage Order, which provided a detailed definition for "hours worked." The agency's interpretation of the validly issued Wage Order was not an underground regulation because the agency merely "construed the words" of "a preexisting [] regulation to a particular situation." (*Aguilar*, *supra*, 234 Cal.App.3d at pp. 27-28.) Specifically, the agency determined that time spent sleeping fell within the "broad" pre-existing definition of "hours worked" because it "clearly" includes "time when an employee is required to be at the employer's premises and subject to the employer's control even though the employee was allowed to sleep." (*Id*. at p. 30.) Indeed, the agency's construction was not even contested by the claimant. (*Id*.) Here, in contrast, the DFPI has not issued any regulation that it is purporting to interpret, and it is not applying the plain language of the definition of "finance lender" or the exemption for state banks. It is adding new conditions on who the lender is for purposes of the CFL's interest rate caps; specifically it added the condition that the bank have the predominate economic interest in the transaction.

Cross-Defendants' citation to *Faulkner v. California Toll Bridge Auth.* (1953) 40 Cal.2d

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[2] Indeed, almost none of Cross-Defendants' cases resolve underground regulation questions on demurrer or where there was disputed facts. (See e.g., *Modesto City Sch. v. Educ. Audits Appeal Panel* (2004) 123 Cal.App.4th 1365, 1374 [after proceeding before administrative law judge and trial court the facts at-issue were "undisputed" and the appeal only presented a legal question]; *W. Coast Univ., Inc. v. Bd. of Registered Nursing* (2022) 82 Cal.App.5th 624, 642 [trial court entered judgment on writ of mandate after a trial hearing and a detailed factual record was developed, including nearly 2,000 pages of declarations]; *Bendix Forest Prod. Corp. v. Div. of Occupational Saf. & Health* (1979) 25 Cal.3d 465, 468-69 [agency acted within its jurisdiction in requiring workers to use "gloves or mittens" where there was "no factual dispute in the case" and a validly issued regulation requiring "hand protection" be used].) The only cases involving demurrers, *Faulkner* and *Excelsior Coll. v. Bd. of Registered Nursing*, are readily distinguishable.

317, 324, is similarly misplaced. In *Faulkner*, the claimant challenged resolutions that were passed to approve the construction and financing of a particular bridge between Richmond and San Rafael. Because the resolutions only applied to the particular bridge and were adopted in the course of compliance with a statutory mandate to act on such requests, the resolutions were not "regulations." (*Id*. at pp. 322-325.) Here, OppFi alleges more than a one-off resolution. Instead, OppFi alleges that DFPI's true lender theory applies to any nondepository, including but not limited to OppFi and LoanMart. *Excelsior Coll. v. Bd. of Registered Nursing* (2006) 136 Cal.App.4th 1218, 1239, is inapplicable for the same reasons as *Aguilar* and *Faulkner*. In *Excelsior*, the agency was "merely . . . enforcing the actual language of the statute." (*Id*.)

Along the same lines, Cross-Defendants argue that their true lender doctrine is not a generally applicable rule because it "is not *applied* to 'entities that are a "true lender"' as a class" but, instead, "whether an entity is a 'true lender' is an outcome" of the test. (Mem. at 10 [quoting OppFi Cross-Compl., ¶ 46].) DFPI's argument proves OppFi's point. DFPI's true lender doctrine, as alleged, has general applicability because it can be applied to any nondepository that partners with state and national banks to determine whether it is subject to the CFL's interest rate caps.

(b) OppFi's Cross-Complaint Does Not Allege Enforcement of California's Common Law Substance Over Form Case Law.

Without any connection to the plain language of the CFL, Cross-Defendants argue that they are "merely appl[ying] [] long-standing California law requiring an assessment of substance over form in loan transactions." (Mem. at 7.) This argument, which is based on a series of unproven and meritless assumptions, fails for several reasons.

First, Cross-Defendants never establish that they can adopt and enforce a common law doctrine or cause of action without complying with the APA. All of the cases that the DFPI relies on that reject application of the APA involve interpretations of validly issued statutes or regulations, none involve common law doctrines. (See Cal. Fin. Code, § 326 [Commissioner has the "powers and jurisdiction . . . vested by law in the department and the divisions thereunder."].)

Second, even assuming *arguendo* DFPI could secretly adopt and enforce a common law doctrine, that is not what OppFi alleges. OppFi alleges that the DFPI's true lender policy goes

beyond enforcement of the common law "substance over form" doctrine and includes a specific test for determining who a lender is for purposes of the CFL's finance lender definition and/or application of its exemption for loans made pursuant to bank partnerships. At bottom, Cross-Defendants' demurrer challenges OppFi's factual allegation that the DFPI's true lender policy is more than enforcement of existing law. A demurrer is not the appropriate vehicle for resolving a disputed fact, i.e. whether the DFPI adopted the alleged test or, as DFPI claims, is merely enforcing existing law. (Mem. at 4, 10.) By disputing OppFi's factual allegations, Cross-Defendants' demurrer violates the cardinal rule of pleading challenges. (*Intengan v. BAC Home Loans Servicing LP* (2013) 214 Cal.App.4th 1047, 1058 ["A demurrer is simply not the appropriate procedure for determining the truth of disputed facts." (citation omitted)].) It fails for this reason alone.

Cross-Defendants attempt to side-step this rule by claiming that OppFi's own allegations establish that the DFPI is merely enforcing existing law. (Mem. at 2, 10.) But that is the exact ***opposite*** of what OppFi alleges. OppFi alleges that after the passage of AB 539 DFPI secretly adopted a predominate economic interest true lender doctrine to determine which entity in a bank partnership is the lender for purposes of applying the CFL's interest rate cap and/or the state bank exemption. (OppFi Cross-Complaint, ¶¶ 28, 31-35, 38-46.) More specifically, OppFi alleged: (i) that *before* passage of AB 539, the DFPI and its predecessors did not enforce the CFL's interest rate restrictions on loans made pursuant to bank partnership agreements (*id*. ¶ 28) and (ii) that *after* the California Legislature passed AB 539, the DFPI began claiming that AB 539 somehow changed the law with respect to bank partnerships. (*Id*. ¶ 26.) Specifically, the former Commissioner asserted that the DFPI would "not sit idly if the same exorbitant-interest credit is being marketed, processed, and serviced by the same company as before, distributed through the same channels as before, and to the same target customers as before." (*Id*.) But AB 539 did not purport to change the law with respect to bank partnerships. Instead, it changed the loan amounts to which certain interest rate limits would apply. OppFi further alleges that the DFPI began acting on its secretly adopted regulation by initiating investigations and enforcement actions against non-banks that partnered with banks. (*Id*. ¶ 25.) In launching one such investigation the DFPI specifically claimed that the non-bank was "evading California's newly enacted rate caps through its recent partnership with an

out-of-state bank." (*Id.*) But, again, there is nothing in AB 539 about bank partnerships.

Moreover, OppFi alleges that in her Cross-Complaint against OppFi, the Commissioner relied on the "true lender doctrine" to allege that OppFi is subject to the CFL's interest rate restrictions. (*Id.* ¶ 33.) In making these allegations, the Commissioner did not cite any provision of the CFL, its implementing regulations, or a California state case. Further, the Commissioner adopted a specific formulation of the true lender doctrine, which identified the lender based on which entity held the "predominate economic interest." (*Id.* ¶ 44.) In combination, if accepted as true, a trier of fact could determine that contrary to the DFPI's assertions in its Demurrer it is not merely enforcing existing law, but that it adopted an underground regulation without complying with the APA. (See, e.g., *Cal. Grocers Assn. v. Dep't of Alcoholic Beverage Control* (2013) 219 Cal.App.4th 1065, 1068 [an agency's generally applicable policy is a regulation where "it describes a circumstance to which the statute applies"].)

Third, although pre-existing California cases recognize a "substance over form" approach, none applied the specific true lender test that OppFi alleges that DFPI adopted, which involves focusing on the entity with the "predominate economic interest" in the loan. (Mem. at 7-9 [citing cases].) Neither the phrase nor the concept of "predominate economic interest" appears in any of Cross-Defendants' cases. (*Id.*) Moreover, none involve interpretation of the definition of "finance lender" or application of the state bank exemption under sections 22009 or 22050 of the CFL. (*Id.*)

Cross-Defendants nonetheless emphasize that in *Janisse v. Winston Inv. Co.* (1957) 154 Cal.App.2d 580, 586–587, the court held that the assignee was "in fact the lender[]." (Mem. at 8-9.) Cross-Defendants reliance on *Janisse* is misplaced. As with Cross-Defendants' other authority, *Janisse* did not adopt a predominate economic interest test, it did not purport to interpret the definition of finance lender or the state bank exemption, and the issue presented was fundamentally different than the issue addressed by the DFPI's true lender policy. In *Janisse*, on the face of the transaction, the loan was ***not*** usurious, it expressly provided for a six percent interest rate. The issue was whether the assignment, at a discounted price, constituted an undisclosed interest charge, which would have made the loan usurious. (See *Janisse*, 154 Cal.App.2d at p. 582.) In contrast, the DFPI's policy applies where the transaction ***is*** usurious, but exempt under the state bank exemption. The

DFPI's policy would have no application in *Janisse* and, in turn, *Jainsse* has no application here.

In any event, the issue presented by OppFi's Cross-Complaint is not, as Cross-Defendants frame it, whether, in this case, Cross-Defendants are enforcing existing law, but is instead whether the DFPI adopted an unwritten true lender policy. These are related, but distinct issues. The Commissioner's enforcement action against OppFi is evidence of its adoption of a true lender policy, not the embodiment of it. The Demurrer conflates these two issues time and time again, repeatedly claiming that "[i]n the present case" the "Commissioner is applying existing California law to the specifics of OppFi[.]" (Mem. at 2, 6, 9, 10, 11.) That factual contention cannot be accepted as true for purposes of a demurrer and, even if it could, OppFi is not merely challenging DFPI's enforcement of the "substance over form" approach, but a more specific test focused on the entity with the predominate economic interest.

Finally, in light of the ample authority disagreeing with application of ***any*** form of a true lender doctrine under California law, Cross-Complainants' adoption of the true lender doctrine is unlike any of the cases relied on by Cross-Complainants where the agency was merely applying the plain language of a regulation or statute. (*Sims v. Opportunity Financial, LLC*, Case No. 20-cv-04730-PJH, 2021 WL 1391565 (N.D. Cal. Apr. 13, 2021) [rejecting application of the true lender doctrine to the same bank partnership at-issue in OppFi's underlying Complaint]; *Beechum v. Navient Sols., Inc.,* No. 15-8239-JGB-KKx, 2016 WL 5340454, at *20-21, n.8 (C.D. Cal. Sept. 20, 2016) [rejecting application of a true lender doctrine under California law]; *WRI Opportunity Loans II, LLC v. Cooper* (2007) 154 Cal.App.4th 525, 536 [rejecting effort to look beyond statutory exemption to intent of parties]; *Jones v. Wells Fargo Bank* (2003) 112 Cal.App.4th 1527, 1537-1538 [same].) In light of this contrary authority, DFPI's true lender policy cannot be considered a rote or ministerial interpretation of the law. (*Morning Star Co.*, *supra*, 38 Cal.4th at p. 336 [an agency's interpretation need not comply with the APA only where "the agency's actions or decisions in applying the law are essentially rote, ministerial . . . ."].)

C. Leave to Amend Must Be Granted, If Necessary.

"Unless the complaint shows on its face that it is incapable of amendment, denial of leave to amend constitutes an abuse of discretion[.]" (*McDonald v. Superior Court* (1986) 180

Cal.App.3d 297, 303–304.) This rule applies "not only where a complaint is defective as to form but also where it is deficient in substance, if a fair prior opportunity to correct the substantive defect has not been given." (*Id*.) Here, this is OppFi's initial complaint challenging Cross-Defendants' underground regulation and, as such, is it entitled to leave to amend to the extent that the Court sustains DFPI's Demurrer. (*Id*.)

D. OppFi's Cross-Complaint Is Procedurally Proper.

Cross-Defendants' final argument is that OppFi's Cross-Complaint is "procedurally improper." This argument fails. The California Code of Civil Procedure expressly permits the filing of a cross-complaint by a cross-defendant at the time it files an answer.

First, California Code of Civil Procedure sections 428.10, subdivisions (a) and (b), establish that any party against whom a cross-complaint is filed may file a cross-complaint against the person who filed the cross-complaint against them and other non-parties. Specifically, section 428.10, subdivision (b), states that "[a] party against whom a cause of action has been asserted in a complaint ***or cross-complaint*** may file a cross-complaint setting forth . . . [a]ny cause of action he has against a person alleged to be liable thereon, ***whether or not such person is already a party to the action,*** if the cause of action asserted in his cross-complaint [] arises out of the same transaction, occurrence, or series of transactions or occurrences as the cause brought against him . . . ." (Emphasis added.) Here, OppFi, as a cross-defendant, has a cause of action to assert against the DFPI, a new party, arising out of the Commissioner's Cross-Complaint against OppFi. Under section 428.10, subdivision (b), OppFi's Cross-Complaint against the DFPI is permissible.

Likewise, section 428.10, subdivision (a), states that "[a] party against whom a cause of action has been asserted in a complaint or cross-complaint may file a cross-complaint setting forth . . . [a]ny cause of action he has against any of the parties who filed the complaint or cross-complaint against him . . . ." Here, the Commissioner asserted multiple causes of action against OppFi in a cross-complaint. OppFi, in turn, has causes of actions against the Commissioner. Under section 428.10, subdivision (a), OppFi is expressly permitted to file its Cross-Complaint.

Second, OppFi is permitted to file its cross-complaint, ***without leave,*** with its answer. Pursuant to California Code of Civil Procedure, section 428.50, subdivision (a), "[a] party ***shall*** file

a cross-complaint against any of the parties who filed the complaint or cross-complaint against him or her before or at the same time as the answer to the complaint or cross-complaint." (Emphasis added.) Otherwise, OppFi would need to seek leave under section 428.50, subdivision (c), to file a cross-complaint. Accordingly, under section 428.50, subdivision (a), OppFi was not just expressly permitted to file its Cross-Complaint with its answer, it was required to do so.

Third, if there was any doubt, section 426.30 confirms that OppFi took the appropriate action by filing its cross-complaint with its answer. Under section 426.30, subdivision (a), "if a party against whom a complaint has been filed and served fails to allege in a cross-complaint any related cause of action which (at the time of serving his answer to the complaint) he has against the plaintiff, such party may not thereafter in any other action assert against the plaintiff the related cause of action not pleaded." As used in this statute, "complaint" refers to a complaint or cross-complaint, and "plaintiff" refers to a person who files a complaint or cross-complaint. (Cal. Code Civ. Proc., § 426.10.) This statute makes clear that if OppFi had not filed its cross-complaint at the same time as its answer, it risked waiving its claims.

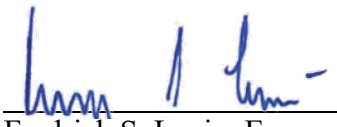
DFPI has no response to this authority. Instead, it just points to section 472, which allows a party to amend its pleading as of right once before an answer or demurrer is filed. This is of no help to the DFPI as OppFi was not amending a pleading but asserting a new claim involving a new party after it had been named in a cross-complaint. As such, section 472 is inapplicable. Without applicable authority, the DFPI then criticizes OppFi's citation to the Rutter Group's California Practice Guide: Civil Procedure Before Trial, which explains that "[n]othing in the statutes or rules prohibits a plaintiff who is served with a cross-complaint, from filing a cross-complaint in turn." (Robert E. Weil et al., *California Practice Guide: Civil Procedure Before Trial* ¶ 6:582.1 (2022) ["Rutter"].) DFPI implicitly concedes that Rutter provides further support for OppFi's filing, but notes that Rutter suggests that "unending" daisy chain pleadings should be "discouraged." But this is not an unending daisy chain of pleadings and, even if discouraged, under the particular facts of this case, OppFi was required to assert its claim by way of cross-complaint, or risk losing it.

IV. CONCLUSION

For the reasons set forth above, the Court should overrule Cross-Defendants' demurrer.

DATED: February 2, 2023

ORRICK, HERRINGTON & SUTCLIFFE LLP

By: 

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PROOF OF SERVICE

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

At the time of service, I was over 18 years of age and not a party to this action. I am employed in the County of Los Angeles, State of California. My business address is 100 Wilshire Boulevard, Suite 1000, Santa Monica, CA 90401.

On February 2, 2023, I served true copies of the following document(s) described as **OPPORTUNITY FINANCIAL, LLC'S OPPOSITION TO CLOTHILDE HEWLETT AND DEPARTMENT OF FINANCIAL PROTECTION AND INNOVATION'S DEMURRER OR, IN THE ALTERNATIVE, MOTION TO STRIKE** on the interested parties in this action as follows:

Clothilde V. Hewlett, Commissioner Mary Ann Smith, Deputy Commissioner Sean M. Rooney, Assistant Chief Counsel Johnny O. Vuong, Senior Counsel Francis N. Scollan, Senior Counsel Allard C. Chu, Senior Counsel DEPARTMENT OF FINANCIAL PROTECTION AND INNOVATION 320 West 4th Street, Suite 750 Los Angeles, CA 90013-2344 Tel: (213) 503-4164 Fax: (213) 576-7181 Email: Johnny.Vuong@dfpi.ca.gov Email: Frank.Scollan@dfpi.ca.gov Email: Allard.Chu@dfpi.ca.gov	Attorneys for Defendant, Cross-Complainant, and Cross-Defendant Clothilde Hewlett, in her official capacity as Commissioner of Financial Protection and Innovation for the State of California; and Cross-Defendant Department of Financial Protection and Innovation

BY E-MAIL OR ELECTRONIC TRANSMISSION: I caused a copy of the document(s) to be sent from e-mail address kmcfarlandrmirez@orrick.com to the persons at the e-mail addresses listed in the Service List. I did not receive, within a reasonable time after the transmission, any electronic message or other indication that the transmission was unsuccessful.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

Executed on February 2, 2023, at Santa Monica, California.

Kathleen McFarland-Ramirez

Kathleen McFarland-Ramirez