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UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF CALIFORNIA

FEDERAL TRADE COMMISSION,

Plaintiff,

vs.

AMERICAN FINANCIAL BENEFITS CENTER, a corporation, also d/b/a AFB and AF STUDENT SERVICES;

AMERITECH FINANCIAL, a corporation;

FINANCIAL EDUCATION BENEFITS CENTER, a corporation; and

BRANDON DEMOND FRERE, individually and as an officer of AMERICAN FINANCIAL BENEFITS CENTER, AMERITECH FINANCIAL, and FINANCIAL EDUCATION BENEFITS CENTER,

Defendants.

Case No: 4:18-cv-00806-SBA

Assigned for all purposes to the Honorable Saundra Brown Armstrong

DEFENDANTS AMERICAN FINANCIAL BENEFITS CENTER, AMERITECH FINANCIAL, FINANCIAL EDUCATION BENEFITS CENTER, AND BRANDON DEMOND FRERE'S OPPOSITION TO FEDERAL TRADE COMMISSION'S MOTION TO STRIKE DEFENDANTS' LACHES, ESTOPPEL, AND OFFSET AFFIRMATIVE DEFENSES

Date: November 14, 2018
Time: 1:00 p.m.
Location: Courtroom 210
1301 Clay Street, 2nd Floor
Oakland, CA 94612

Date Action Filed: February 7, 2018

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I. INTRODUCTION

The Federal Trade Commission's ("FTC") motion to strike ("Motion") must be denied because the affirmative defenses at issue – laches, estoppel, and offset – are properly raised against the FTC and are adequately pled. As many courts have noted, motions to strike are a disfavored tool. *Shaterian v. Wells Fargo Bank, N.A.*, 829 F. Supp. 2d 873, 879 (N.D. Cal. 2011) (quoting *Rosales v. Citibank Fed. Sav. Bank*, 133 F. Supp. 2d 1177, 1180 (N.D. Cal. 2001). The FTC's Motion reveals exactly why courts express this sentiment.

First, the FTC argues that Defendants have not provided fair notice of their laches defense, and fail to assert certain factual elements of the estoppel defense. The FTC is wrong on both counts. Defendants' Answer provides ample factual support for both defenses, and closely follows the level detail provided by other defendants to FTC actions in the Northern District that have survived motions to strike. In contrast, the cases cited by the FTC in the Motion involved affirmative defenses with no factual support. Defendants have provided fair notice here, but even if this Court determines otherwise the Court should grant Defendants leave to amend their Answer.

Second, the FTC argues that the defenses of laches, estoppel, and offset are "legally insufficient and prejudicial." That argument lacks any merit, and suggests that the FTC enjoys a unique status stripping Defendants of affirmative defenses. In so arguing, the FTC ignores dozens of rulings from across the United States denying motions to strike and permitting defendants to raise these exact defenses **against the FTC**. The cases cited by the FTC are universally dissimilar or, alternatively, support Defendants' arguments.

For the reasons that follow, Defendants respectfully request that this Court deny the Motion. The FTC clearly believes itself to be a privileged litigant, exempt from affirmative defenses and routine procedural vehicles such as responding to discovery and retaining experts. All Defendants have asked from the inception of this litigation is the opportunity to defend themselves in court. The FTC has taken every step in their power to prevent that from happening and to unnecessarily increase litigation costs. However, there is simply no legal authority that prevents Defendants from asserting these meritorious affirmative defenses. Basic fairness and due process require they be allowed to do so.

///

II. LEGAL STANDARD

Under Rule 12(f), "[a]ffirmative defenses will be stricken ***only*** when they are insufficient on the face of the pleadings." *Williams v. Jader Fuel Co.*, 944 F.2d 1388, 1400 (7th Cir. 1991) (quotation and citation omitted), emphasis added. "Motions to strike 'are generally disfavored because they are often used as a delaying tactic and because of the limited importance of pleadings in federal practice.'" *Shaterian*, 829 F.Supp.2d at 879 (quoting *Rosales*, 133 F. Supp. 2d at 1180). Given the disfavored status of Rule 12(f) motions, "'courts often require a showing of prejudice by the moving party before granting the requested relief.'" *Sanchez v. City of Fresno*, 914 F. Supp. 2d 1079, 1122 (E.D. Cal. 2012) (quoting *Cal. Dep't of Toxic Substances Control v. Alco Pac., Inc.*, 217 F. Supp. 2d 1028, 1033 (C.D. Cal. 2002)). "If there is any doubt whether the portion to be stricken might bear on an issue in the litigation, the court should deny the motion." *Holmes v. Elec. Document Processing, Inc.*, 966 F. Supp. 2d 925, 930 (N.D. Cal. 2013) (quoting *Platte Anchor Bolt, Inc. v. IHI, Inc.*, 352 F. Supp. 2d 1048, 1057 (N.D. Cal. 2004)).

III. THE DEFENSES OF LACHES AND ESTOPPEL ARE ADEQUATELY PLED.

Being subject to the rules of pleading, an affirmative defense must be pled in "short and plain terms." Fed. R. Civ. Proc. 8(b)(1)(A). The FTC suggests that Defendants must allege additional facts, and do so with "sufficient particularity." Motion, p. 2. That is not the correct standard. Defendants are not required to aver allegations to establish a prima facie claim or defense. *Boykin v. KeyCorp.*, 521 F.3d 202, 212 (2d Cir. 2008). Nor does Rule 8 require answers or complaints to state evidentiary facts. *Cromwell v. Deutsche Bank Nat'l Trust Co.*, No. C 11-2693 PJH, 2012 U.S. Dist. LEXIS 8528, at *2 (N.D. Cal., Jan. 25, 2012) ("[s]pecific facts are unnecessary"). A defendant need only provide "fair notice" to sufficiently plead affirmative defenses. *Simmons v. Navajo Cty., Ariz.*, 609 F.3d 1011, 1023 (9th Cir. 2010); *Wyshak v. City Nat'l Bank*, 607 F.2d 824, 827 (9th Cir. 1979). Here, Defendants have more than met this notice pleading standard, and the Court should reject the FTC's suggestion of a heightened pleading standard.

A. Defendants have Provided Fair Notice of their Laches Defense.

The FTC contends that Defendants have provided "no factual basis" for the defense of laches. Motion, p. 3. The FTC is demonstrably wrong. Below is how Defendants pled their affirmative

defense of laches:

> . . . Plaintiff delayed bringing any action despite having full knowledge of the corporate actions of Defendants for over a year before bringing this lawsuit. Specifically, Plaintiff refused to respond to a letter sent by corporate Defendants on December 30, 2016 to the Chairwoman of Plaintiff, Edith Ramirez, in which the Corporate Defendants sought guidance from the FTC regarding their standard business practices, and provided samples of their mailers and the scripts used by Account Specialists. Plaintiff understood that it would be important to respond to the letter because they had already opened an investigation into Corporate Defendants. Despite that, Plaintiff sat silently and did not respond to the letter at all. In addition, Plaintiff refused to file its lawsuit promptly after Defendants first filed a lawsuit against Plaintiff on August 18, 2017 for declaratory relief. Plaintiff was considering the filing of a lawsuit, as it sent a draft complaint to Defendants on October 3, 2017, yet waited over four months to file its Complaint in this action. Furthermore, Plaintiff engaged in an indiscriminate industry "sweep" that it described as "Game of Loans," and only decided to sue Defendants after gross delay, prejudice to Defendants and in response to Defendants' suit for declaratory relief. **In short, it would be inequitable for Plaintiff to seek equitable relief, including an injunction and the appointment of a receiver, when it had full knowledge of Corporate Defendants business practices yet refused to provide any guidance about what it thought the Corporate Defendants were doing wrong or how such actions could be corrected, and refused to file any lawsuit.**

Answer, ECF No. 162, ¶108 (emphasis added).

The FTC's Motion ignores all of the actual facts alleged, which go far beyond simply alleging the defense. The elements of laches are (1) an unreasonable delay by the plaintiff and (2) prejudice to the plaintiff. *Evergreen Safety Council v. RSA Network, Inc.*, 697 F.3d 1221, 1226 (9th Cir. 2012). Here, the asserted affirmative defense provides fair notice of each element.

The affirmative defense provides fair notice of delay on the part of the FTC. In characteristic fashion, the FTC simply ignores the actual facts alleged. The FTC focuses on the allegations regarding the delay in filing the lawsuit after it shared a draft complaint, but the Answer provides more detail. Specifically, the Answer sets forth that the FTC "refused to respond" to a December 2016 inquiry to the Chairman of the FTC after the FTC had already opened an investigation into Defendants' practices. *See* Answer, ECF No. 162, ¶108. The Answer also references the prejudice suffered by Defendants who could not modify their practices to meet the FTC's unknowable standards. This level of specificity is at least as great as that pled in the answer before Judge Griffith when he denied the FTC's motion to strike on the same defense. *See FTC v. DirecTV, Inc.*, No. 15-cv-01129-HSG, 2015 WL 9268119 (N.D. Cal.

Dec. 21, 2015) (*DirecTV I*); Declaration of James Vorhis ("Vorhis Decl."), ¶ 2, Exh. A [DirecTV Answer].

Moreover, the FTC incorrectly argues that "Defendants here meet neither prong" as if Defendants have the burden to prove their defenses now; but, that is not the question this Court must address. Defendants do not need to *prove* each element at this stage of the litigation. This is an affirmative defense, and Defendants need only provide "fair notice." *Simmons*, 609 F.3d at 1023. The Answer plainly meets Rule 8's requirement to state a defense in "plain and short terms."

Finally, from a pragmatic perspective, what additional information does the FTC seek? The FTC refused to respond to Defendants' requests for guidance while concurrently conducting a *secret* investigation dubbed "Operation Game of Loans" where it was obtaining declarations, as early as March 2017 to support a motion for injunctive relief. *See* ECF Nos. 50-71. To date, the FTC has refused to produce documents about its *secret* investigation, including its delay and whether it abandoned its "sweep" at some point, during discovery. Vorhis Decl., ¶ 3, Exh. C (*see, e.g.,* FRC response to Request for Production No. 4). Thus, Defendants have limited information regarding the scope or timing of that investigation due to the FTC's positions in this litigation. Nevertheless, for purposes of the Motion, Defendants have provided more than adequate detail.

B. Defendants have Adequately Pled the Elements of their Estoppel Defense.

The FTC contends that Defendants have failed to "plead adequately" their estoppel defense. Motion, p. 3.[1] Again, the FTC is wrong. To *prove* equitable estoppel, defendants must show that 1) the FTC knew the facts, 2) the FTC intended that its conduct be acted on, or acted so that Defendants had a right to believe it is so intended, 3) Defendants were ignorant of the true facts, and 4) Defendants relied on the FTC's conduct to their injury. *FTC v. EDebitPay, LLC*, 2011 U.S. Dist. LEXIS 15750, at *29-30 (C.D. Cal. Feb. 3, 2011) (citing *Watkins v. U.S. Army*, 875 F.2d 699, 707 (9th Cir. 1989)). A party raising the estoppel defense against the government must also establish 1) affirmative misconduct beyond mere negligence, 2) the government's wrongful act will cause a serious injustice, and 3) the public's interest will not suffer undue damage by imposition of the liability. *Id.* at *30 (citing *United*

[1] Defendants pled estoppel with the same factual detail as their laches defense. Answer, ECF No. 162, ¶110.

States v. Bell, 602 F.3d 1074, 1082 (9th Cir. 2010)). Again, at this stage, Defendants need not prove these elements. Defendants provide fair notice of these elements in their Answer.

The Answer specifically alleges, among other facts. that the FTC was investigating the corporate Defendants, that the FTC failed to then respond to Defendants' inquiry and submission in December 2016, and that Defendants were ignorant of that investigation. Answer, ECF No. 162, ¶110. When coupled with the other facts included on the face of the Answer, Defendants assert a viable estoppel defense. *See, e.g., SEC v. Sands*, 902 F.Supp. 1149, 1166 (C.D. Cal. 1995).

The FTC's Motion seems to request this Court to make certain factual and legal determinations to rule on the Motion that require consideration of evidence. *See Mukherjee v. I.N.S.*, 793 F.2d 1006, 1009 (9th Cir. 1986) (citing *Lavin v. Marsh*, 644 F.2d 1378, 1382 fn. 6 (9th Cir. 1981)) ("The appropriateness of estoppel turns on the facts of the individual case."). But "[t]he Court should not weigh the evidence for purposes of a motion to strike an affirmative defense." *Sands*, 902 F.Supp. at 1166. Such a determination would be premature, as it is improper for the Court to "delve into an examination of the evidence before it at this time" to determine whether the FTC's conduct, as alleged in the Answer, may constitute affirmative misconduct going beyond mere negligence. *SEC v. Des Champs*, No. 2:08-CV-01279, 2009 WL 3068258, *3 (D. Nev. Sept. 21, 2009) (*citing U.S. v. Gamboa-Cardenas*, 508 F.3d 491, 502 (9th Cir. 2007)).

The FTC also suggests that "unexplained delay does not constitute affirmative misconduct." Motion, p. 3 (citing *Jaa v. I.N.S.*, 779 F.2d 569, 572 (9th Cir. 1986) and *I.N.S. v. Miranda*, 459 U.S. 14, 18-19 (1982)). The Answer does not rely solely on delay, and at this stage of the litigation the citation to those cases is misguided. Both *Jaa* and *Miranda* involved **final** decisions by the Board of Immigration Appeals to deny applications for citizenship. They were not decided in the context of a motion to strike, and the reviewing courts carefully analyzed the evidence to determine if there had been affirmative misconduct. *Miranda*, 459 U.S. at 17-18 ("Although the time was indeed long, we cannot say in the absence of **evidence** to the contrary that the delay was unwarranted); *Jaa*, 779 F.2d at 572 ("There is no **evidence** that the government's delay in this case was anything but neglect.") At this stage of the litigation, the Court is not tasked with a full analysis of the evidence; particularly where the FTC is reticent to produce documentation related to its own press release about the Complaint in this

action.[2]

In sum, the answer includes allegations that provide fair notice, and the FTC has not met its burden of showing that the estoppel affirmative defense should be stricken.

IV. LACHES AND ESTOPPEL ARE NOT INSUFFICIENT DEFENSES AS A MATTER OF LAW, AND MAY BE ASSERTED AS AFFIRMATIVE DEFENSES AGAINST THE FTC

A. Laches is Properly Asserted in Defendants' Answer.

In its Motion, the FTC argues that "[a]s a general rule, laches is not a recognized defense against the government in a civil suit to enforce a public right or protect a public interest." Motion, p. 4. This bald assertion is contradicted by clear authority that holds laches to be a valid defense against the FTC.

First, the FTC ignores numerous decisions where courts have denied motions to strike and determines that the defense of laches may apply to the FTC. Most notably, Judge Griffith rejected multiple attempts by the FTC to strike the defendants' laches defense in the DirecTV litigation.[3] There, the FTC initially filed a motion to strike on the same faulty premise that laches may not be raised against the government in civil lawsuits. Judge Griffith denied that motion in *DirecTV I*, 2015 WL 9268119, noting that DirecTV adequately pled the defense because laches may be pled against the government where there is some "government misconduct" and that the existence of that defense is an issue of fact. *Id*. at *3. The law on that point is quite clear.

Later in the same litigation, the Court denied the FTC's motion for summary judgment on the laches defense because the defense implicated numerous factual issues. *FTC v. DirecTV, Inc.*, No. 15-cv-01129-HSG, 2016 WL 6947503, at *3 (N.D. Cal. Nov. 26, 2016) (*DirecTV II*). Other courts throughout the country have reached the same conclusion. *See, e.g., FTC v. Hope New Modifications, LLC*, No. 09-1204(JBS/JS), 2011 WL 883202, at *5 (D.N.J. Mar. 10, 2011); *FTC v. National Urological Group, Inc*., No. 1:04-cv-3294-CAP, 2005 WL 8155166, at *5 (N.D. Ga. June 24, 2005). The FTC

[2] The FTC also cites to *FTC v. Medicor LLC*, 2001 U.S. Dist. LEXIS 26774, at *11 (C.D. Cal. June 27, 2001) in support of its position. Neither the answer nor the motion to strike briefing from that case is available on PACER. However, that court noted that the defendants indicated that "there are facts supporting a defense of estoppel" in the briefing, which implies there were no facts to support the defense in the answer. However, because this Court cannot evaluate what the *Medicor* court had in front of it when it determined that the essential elements of estoppel were not pled, that case should be disregarded.

[3] The FTC's failure to reference this litigation is telling. Not only are Judge Griffith's opinions directly on point, but attorneys who represented the FTC in the DirecTV litigation are participating in this case.

conveniently ignores these authorities in favor of its baseless arguments that the defense always fails "as a matter of law."

Second, there simply is no "general rule" that laches is not a recognized defense against the government. A number of courts—including the Supreme Court—have indicated that there is no such general principle. *See, e.g., Clearfield Trust Co. v. United States*, 318 U.S. 363, 369 (1943) (ruling that a federal standard applied to determine whether delay was unreasonable and prejudicial and that the sovereignty of the United States did not shield it from such defenses, and stating that "[t]he fact that the drawee [of the check] is the United States and the laches those of its employees are not material"); *United States v. Martell*, 844 F.Supp. 454, 459 (N.D. Ind. 1994) (holding that laches may be asserted against the government); *S.E.R., Jobs for Progress, Inc. v. United States*, 759 F.2d 1, 3 (Fed. Cir. 1985) (the court considered the application of the doctrine against the government by assuming without deciding that such a defense may be brought against the government).[4]

The FTC cites *FTC v. Image Sales & Consultants, Inc.*, 1997 U.S. Dist. LEXIS 18902, at *3-4 (N.D. Id. Nov. 17, 1997), *FTC v. N. Am. Mktg. & Assocs., LLC*, 2012 U.S. Dist. LEXIS 150102, at *5 (D. Ariz. Octo 18, 2012), and *FTC v. Debt Solutions, Inc.*, Case No. 2:06-cv-00298JLR (W.D. Wash, Aug. 7, 2006) to argue the application of a broad general rule that laches may not be asserted against the FTC. These decisions do not undermine the well-reasoned decision of Judge Griffith from this very district. Most egregiously, *Debt Solutions* involved an unpublished decision on an ***unopposed motion to strike***. Ortiz Declaration, Exh. B, Order at p. 1 ("Despite repeated extensions, Defendants have not opposed the motion.").[5] But *Image Sales* and *North American Marketing* are no more helpful as both courts noted the absence of *any* factual allegations to support the affirmative defenses in making those rulings. The FTC cites to the District Court ruling on *Image Sales*, 1997 U.S. Dist. LEXIS 18902 at *3-

[4] *See also United States v. Rhodes*, 788 F.Supp. 339, 343 (E.D. Mich. 1992) (finding that laches applies when the government brings an action); *United States v. Admin. Enters., Inc.*, 46 F.3d 670, 672-73 (7th Cir. 1995) (listing potential scenarios in which a valid laches defense may be asserted, including when the United States acts as a holder of commercial paper) (*citing Clearfield Trust Co. v. United States*, 318 U.S. 363, 369 (1943)); *Cayuga Indian Nation of N.Y. v. Pataki*, 413 F.3d 266, 278-79 (2d Cir. 2005) (agreeing with the Seventh Circuit that a laches defense may be asserted against the United States in three main situations: in the most egregious instances of laches, when there is no relevant statute of limitations, and when the government seeks to enforce private rights).

[5] Moreover, as with almost every case cited by the FTC, the answer provides no factual specificity in the affirmative defense. *See* Vorhis Decl., ¶ 5, Exh. E ("For their seventh Affirmative Defense, the Defendants assert that Plaintiff's claims are barred by the doctrine of laches.").

4, but conveniently omits the preceding Magistrate's Recommendation, which specifically notes that the defendants had provided no factual support of that defense. *FTC v. Image Sales & Consultants*, 1997 U.S. Dist. LEXIS at *5-6 (N.D. Ind. Sep. 17, 1997) ("Moreover, the Defendants offer no specifics as to how the FTC could be guilty of laches even if the doctrine was available"). In *North American Marketing*, the Court specifically stated, "[t]hese defenses contain no reference to supporting facts." 2012 U.S. Dist. LEXIS 150102 at *8.

But as Judge Griffith explained in *DirecTV I*, all that is required are allegations supporting the laches defense sufficient to provide notice to the FTC of Defendants' theory and specific facts that "plausibly" could support such a finding of laches. *Id*. at *3. As discussed above, Defendants did just that. *See* Answer, ECF 162, ¶ 108. Defendants' Answer includes numerous allegations regarding the FTC's unreasonable delay, including specific references to a letter they sent to the FTC, the FTC's draft complaint, and the FTC's industrywide sweep. *Id*.[6] These facts are similar to those alleged in the Answer filed by DirecTV, which survived a motion to strike and motion for summary judgment. Vorhis Decl., ¶ 2, Exh. B. Similarly, this Court should deny the Motion as to the laches defense.

B. Defendants' Estoppel Defense is Applicable Against the FTC.

In its Motion, the FTC contends that "Defendants have not properly pleaded their estoppel defense and, in any event, it is insufficient as a matter of law." Motion, p. 5. The FTC is wrong again.

As with the laches defense, numerous courts have expressly held that estoppel may be raised against the FTC. *See, e.g.*, *DirecTV I*, 2015 WL 9268119, at *3; *DirecTV II*, 2016 WL 6947503, at *3; *FTC v. Alcoholism Cure Corp.*, No. 3:10-cv-00266-J-34JBT, 2010 WL 11474441, at *3 (M.D. Fla. Dec. 13, 2010) ("In support of his affirmative defense of estoppel, Defendant has alleged, among other things, that Plaintiffs have harassed him for years without a 'serious grounding in the law.' . . . Further, he

[6] The FTC suggests laches will lead to a "fishing expedition", but that characterization is both inaccurate and irrelevant. The FTC filed a complaint against Defendants with the goal to shutter the Corporate Defendants. On the day of the filing, the FTC issued a press release stating that the complaint was part of a nationwide operation called Game of Loans (referring to the HBO Series, Game of Thrones, though shuttering legitimate businesses is no game). Vorhis Decl., ¶ 4, Exh. D. Since that time, the FTC has backtracked and attempted to characterize the Game of Loans as a "term to generate media interest" and thereby contradicted its own press releases that had indicated this was a single initiative. *See, e.g.*, Vorhis Decl., ¶ 4, Exh. D [FTC Responses to RFPs, Specific Objection No. 8, response no. 4]. The Court should not credit the FTC's gripe that it might have to participate in discovery on topics related to the Complaint that it filed.

alleges that Plaintiffs have stopped their investigations multiple times, leading him to believe his actions were not illegal. Thus, given the liberal construction owed to his pleadings, Defendant has sufficiently pleaded his affirmative defense of estoppel, and the Court will not strike it."); *FTC v. U.S. Work Alliance, Inc.*, 2009 WL 10669724, at *3 (N.D. Ga. Feb. 24, 2009); *FTC v. Accusearch, Inc.*, No. 06-cv-105-D, 2007 WL 9709752, at *2 (D. Wyo. Mar. 28, 2007); *FTC v. Magazine Solutions, LLC*, No. 07-692, 2007 WL 2815695, at *1 (W.D. Pa. Sep. 25, 2007) (denying motion to strike estoppel defense because the defense was not "redundant, insufficient or immaterial to the matters at issue"); *FTC v. Stratford Career Institute*, NO. 16-cv-371, 2016 WL 3769187, at *2-3 (N.D. Ohio July 15, 2016).

The court in *FTC v. BF Labs Inc.*, No. 4:14-CV-00815-BCW, 2015 WL 12806580, (W.D. Mo. Aug. 28, 2015) aptly reasoned:

> Regardless of the impact of these defenses on liability, the Court finds that there are scenarios where this factual information may be relevant to the appropriate remedy. **Because the Court is reticent to strike** even a potentially marginal defense that causes no discernible prejudice to Plaintiff, the Court declines to strike these defenses. *Id.* (explaining that "the mere presence of redundant and immaterial matter not affecting the substance of the lawsuit is insufficient grounds to strike a pleading"). *Id.* at *3. Denied MTS estoppel and latches (different defendants, same action as above). **The Court is not convinced that these defenses are universally inapplicable in FTC Act cases**. *See, e.g., Hang-Ups Art Enters.*, 1995 WL 914179 at *4 (declining to strike similar defense and explaining that "[t]he facts of the case should decide whether there has been affirmative misconduct by the government such that laches might apply"). Because factual scenarios may exist where the defenses might apply, the Court declines to strike these defenses before Defendants have the benefit of some discovery.

Id. at *3, emphasis added. Similarly, here, the Court should deny the FTC's motion as to the estoppel defense because this defense does not fail as a matter of law, and because the FTC has not even attempted to argue any legitimate prejudice.

The cases cited by the FTC are easily distinguished. For example, the FTC relies on *FTC v. Medlab, Inc.*, Case No. CV-08-0822-SI (N.D. Cal. July 22, 2008), for the purported proposition that "District courts in this circuit have held that the estoppel defense may not be asserted against sovereigns who act to protect the public welfare, such as the FTC." Motion, p. 5. That is not at all what the *Medlab* order states. It does not reference sovereign entities or the public welfare. Instead, the order merely strikes the defense without any elaboration. *See* ECF 170-3 (Ortiz Declaration, Exh.

C). This omission is critical because – yet again – the defendants' answer in that matter provided no factual support for the laches or estoppel defenses. *See* ECF No. 170-4 (Ortiz Declaration, Exh. D, "The causes of action are barred by the doctrine of laches, estoppel, and/or waiver."). And, the FTC's characterization of any impact from the *Medlab* opinion is patently inaccurate. More recently, in 2015, this District has ***permitted*** the estoppel defense to survive the FTC's motion to strike. *See DirecTV I*, 2015 WL 9268119, at *3.

The FTC also argues that "[c]ourts have rejected Defendants 'estoppel by silence' argument, holding that mere inaction cannot support a claim of estoppel because it does not rise to the level of affirmative misconduct." Motion, p. 6. But the cases cited by the FTC are distinguishable. The FTC's citation to *Dickow v. United States*, 654 F.2d 144, 152 (1st Cir. 2011) is particularly egregious. That case involved a challenge by an estate seeking a refund of money paid as part of estate taxes. Under federal law, a taxpayer must file a refund claim within a proscribed time period. *Id.* at 146. The estate argued that the IRS should be estopped from denying a refund claim as tardy because the IRS failed to tell the estate that a second extension had been granted. *Id.* at 151. The Court rejected the estate's argument because the specific federal statute, 26 U.S.C. § 6511(a), is not subject to equitable exceptions under a Supreme Court ruling. *Id.* Thus, the ruling in *Dickow* on the equitable defenses was limited to that specific statute. More important, the Court ***expressly considered*** evidence regarding the estoppel by silence argument. *Id.* at 152-153. The FTC omits a key portion of the ruling in the parenthetical contained in its Motion:

> *The FTC's citation in the Motion*:
>
> > "The argument of estoppel by silence on the part of the busy IRS is…simply a non-starter."
>
> *The actual citation from Dickow*:
>
> > "The argument of estoppel by silence on the part of the busy IRS is, **on these facts**, simply a non-starter."

The omission of these words "on these facts" changes the entire meaning of the sentence in the context of this Motion – the incomplete and misleading quote reflects a stunning lack of candor. Did the FTC think this Court would not read the actual *Dickow* opinion?[7]

[7] *FTC v. Algoma Lumber Co.*, 291 U.S. 67, 80 (1934), involved a final FTC proceeding regarding the

The authorities the FTC relies upon for its misguided estoppel by silence theory, which did not involve motions to strike or comment on the propriety of the estoppel defense as applied against the FTC, in no way undermine the many cases that have found estoppel to apply, including the *DirecTV* rulings.

V. OFFSET IS APPROPRIATELY RAISED IN CASES WHERE CONSUMERS HAVE REALIZED BENEFITS THAT IMPACT THE DETERMINATION OF CONSUMER LOSSES

The FTC broadly states that it is "well settled that for violations of the FTC Act, consumer loss is calculated by the amount of money paid by the consumers, less any refunds made." Motion, p. 6. The FTC further suggests that "[t]he Ninth Circuit has specifically rejected the notion that defendants in FTC cases are entitled to offset the alleged value of a product when determining the amount of consumer injury." Motion, p. 7. The FTC is offering an overly simplistic – and incorrect – argument regarding the law on offset. The Court should deny the FTC's argument because (1) the FTC requests that the Court strike the offset defense in its entirety; (2) courts have denied motions to strike offset filed by the FTC because this defense implicates numerous factual issues and is not barred as a matter of law; and (3) the services and financial impact at issue here are distinct from those considered in the authorities the FTC relies upon in the Motion – here consumers received reduced student loan payments that impact the "consumer loss" standard referenced by the FTC.

As an initial matter, the FTC's statement of the rule applicable to the calculation of damages, that refunds ***must*** be considered by the Court, demonstrates that Defendants' offset defense is valid. *See* Motion, p. 6. In their Answer, Defendants specifically pleaded that any damages should be offset by "benefits received by customers, and/or ***chargebacks or refunds paid to customers***." *See* Answer, ¶ 112, emphasis added. The FTC has not, and cannot, claim that it is improper for the Court to consider evidence or arguments related to chargebacks or refunds in this litigation. The prayer for relief in the FTC's Complaint does not recognize any credit for refunds. Accordingly, offset is a necessary affirmative defense. *See* ECF No. 1, p. 17. Thus, there is no basis for the Court to strike this entire defense.

description of lumber products. However, it is clear that the *Algoma Lumber* court reviewed significant evidence regarding the defendants' estoppel defense.

Second, and more important, offset is a valid affirmative defense to be raised against the FTC. Numerous courts have denied motions to strike on the offset defense because it is not *per se* invalid when raised against the FTC. *See, e.g., FTC v. Bronson Partner, LLC,* No. 3:04CV1866 SRU, 2006 WL 1973572006, at *1-2 (D. Conn., Jan. 25, 2006); *FTC v. Affiliate Strategies, Inc.*, No. 09-4104-JAR, 2010 WL 11470103, at *13-14 (D. Kan. June 8, 2010); *FTC v. BF Labs Inc.*, No. 4:14-CV-00815-BCW, 2015 WL 12806580, at *3 (W.D. Mo., Aug, 28, 2015). As the FTC knows, the defense of offset is highly factual, and it cannot be summarily defeated on a motion to strike by citation to cases with no factual similarity to this litigation. For example, the court in *BF Labs Inc.*, declined to strike defendants' offset defenses explaining that "there are scenarios where this factual information may be relevant to the appropriate remedy. Because the Court is reticent to strike even a potentially marginal defense that causes no discernible prejudice to Plaintiff, the Court declines to strike these defenses." *Id.* at *3; *see also Affiliate Strategies*, Inc., 2010 WL 11470103 at *13-15 (declining to strike offset defense due to limited case law on the subject and because the applicability of the defense was a question of fact).

Third, cases cited by the FTC should be disregarded. Again, the FTC seems to believe that Defendants must have a trial-ready case during the pleading stage. Not so. The FTC fails to recognize a critical distinction between the current case and those it cites. In each of those cases, defendants proposed that equitable monetary relief be decreased by the value of the positive benefits received from the product or services being sold. This case is entirely differently because the services consumers purchased resulted in reduced student loan payments, thereby reducing the amount of consumer loss.

The FTC fails to cite any case that says Defendants may not raise offset as a defense against the FTC in litigation. None of the cases cited by the FTC involved a product or service that would reduce consumers' overall expenses such as is the case here. As one example, the FTC relies on *FTC v. Kuykendall*, 371 F.3d 745, 766 (10th Cir. 2004). That case involved a company marketing magazine sales. *Id.* at 749-750. After the FTC obtained a judgment, the defendant continued to engage in the marketing of magazine sales. The FTC was forced to bring a contempt motion. In evaluating the issue of the equitable damages, the Court expressly stated that "[t]o accurately calculate actual loss, the defendants ***must be allowed to put forth evidence*** showing that certain amounts should offset the sanctions assessed against them…[f]or instance, the defendants might be able to show that some

customers received full refunds of their payments or that others were wholly satisfied with their purchases and thus suffered no damages." *Id.* at 766; *see also FTC v. BlueHippo Funding, LLC*, 762 F.3d 238, 245 (2d Cir. 2014) (after the court uses the defendants' gross receipts as a baseline for calculating damages, the court ***must*** permit the defendants "to put forth evidence showing that certain amounts should offset the sanctions assessed against them") (emphasis added); *see also FTC v. Amy Travel Serv., Inc.*, 875 F.2d 564, 572 (7th Cir. 1989) (the court affirmed the magistrate judge's decision to acknowledge satisfied customers and exclude them in the computation of the restitution damages). Thus, contrary to the FTC's position, *Kuykendall* supports an offset defense here.

FTC v. Commerce Planet, Inc., 815 F.3d 593, 603 (9th Cir. 2016) involved a company that sold membership services for on-line marketing. 815 F.3d at 597-598. The Court considered evidence to offset the FTC's proposed damages figure, but found Defendants could not reliably quantify that amount. And in *FTC v. Publishers Bus. Servs., Inc.*, 540 Fed. Appx. 555, 558 (9th Cir. 2013), cert denied, 134 S. Ct. 2724 (2014), the court remanded the case to determine the injury to consumers, and stated "that does not mean the district court must assume the calculation proposed by the FTC" while referencing express arguments made by the Defendants. It explored one fact that is at issue here – what was the loss to consumers? The issues of offset and consumer loss are highly factual, and require the consideration of evidence from Defendants to contradict the FTC's claimed damages.[8] Cases cited by the FTC do not refute this point, and should be disregarded when considering the applicability of offset as a defense against the FTC. Thus, the Court should deny the Motion and permit the offset defense to remain part of Defendants' Answer.

VI. THE PRESENCE OF THESE AFFIRMATIVE DEFENSES WILL NOT RESULT IN WASTEFUL LITIGATION

This Court should disregard entirely the FTC's suggestions that these affirmative defenses are "wasteful" or "prejudicial." The FTC contends that these affirmative defenses purportedly "distract from the real issues in this case." The FTC's position is nonsensical, and Defendants regret that they

[8] The FTC also cites two opinions issued by Judge Ilston to suggest offset is appropriately stricken. *See* Ortiz Declaration, Exhibit D; *see also FTC v. Medlab, Inc.*, 615 F.Supp.2d 1068 at *3 (N.D. Cal. 2009). However, the FTC declines to note that 1) Judge Ilston still considered certain aspects of defendants' offset affirmative defense at summary judgment, and 2) stated specifically that her ruling on summary judgment was "light of all of the circumstances of this case." This Court, of course, is not making a factual ruling at this stage of the litigation.

have to address this frivolous argument.

The affirmative defenses at issue in the Motion are valid, and Defendants must be permitted to assert them just like any other litigant. The FTC attempts to play God when it states that "[a]n agency charged with enforcement of an important regulatory scheme in the public interest, such as the FTC, should not be thwarted or distracted by conclusory or improbable allegations." It cites to purported "broad, burdensome, and prejudicial" discovery to support that far-fetched notion.[9] But it was the FTC that sued Defendants as part of a nationwide "sweep." It was the FTC that publicly acknowledged this complaint to be part of that larger effort. Discovery narrowly tailored to terminology in the FTC's own press release is not "wasteful" or "prejudicial" – it should be expected. Also, more importantly, the Court should consider only Defendants' Answer when ruling on the Motion, not the FTC's extraneous submissions. *See Williams*, 944 F.2d at 1400.[10]

As the court noted in *FTC v. U.S. Work Alliance, Inc.*:

> **Despite the FTC's argument to the contrary, the effect of briefing and ruling on these defenses was to raise several issues before they are factually ripe and caused the Court to consider purely legal defenses before the Defendants even attempt to utilize them**. The Court is essentially ruling in the dark on hypothetical legal defenses. The Court further notes that in its experience almost every experienced civil litigant will raise precisely these three affirmative defenses (mootness, laches, estoppel) in their answer because failure to do so, even if the defense likely lacks merit, may result in waiver. *See* Fed. R. Civ. P. 8(c). The Court considers the motion to strike in this light.

Id. at *3, emphasis added. The FTC asks this Court to prevent Defendants the ability to defend themselves in this litigation. It has been apparent from the outset of this litigation that the FTC has a single outcome on its mind. But Defendants have the right to litigate this case like any other party.

VII. LEAVE TO AMEND SHOULD BE GRANTED IF THE COURT IS INCLINED TO STRIKE ANY DEFENSE

"Unless it would prejudice the opposing party, courts freely grant leave to amend stricken

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[9] The discovery cited by the FTC was propounded in a different case, *American Financial Benefits Center, et al. v. Federal Trade Commission*, Northern District of California Case No. 17-cv-04817-SBA. The FTC cites no authority for the proposition that a court may strike an affirmative defense because of discovery propounded in a different matter.

[10] The FTC also complaint about the possibility of retaining experts when it already submitted a joint Rule 26(f) report with expert disclosure and discovery deadlines. ECF No. 124, p. 6.

pleadings." *Roe v. City of San Diego*, 289 F.R.D. 604, 608 (S.D. Cal. 2013). If the Court is inclined to grant the FTC's Motion and strike any of Defendants' affirmative defenses, Defendants respectfully request that the Court do so without prejudice and grant leave to amend the Answer.

VIII. CONCLUSION

For the reasons above, this Court should deny the FTC's Motion and let this case proceed onto discovery with these affirmative defenses.

Date: October 2, 2018

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