STATEMENT OF ISSUES

The Complainant is informed and believes, and based upon such information and belief, alleges and charges as follows:

I.

Sezzle and its Application

1. Sezzle, Inc. (Sezzle) applied to the Commissioner of Business Oversight (Commissioner) for a lender’s license under the California Financing Law (Fin. Code, § 22000, et seq.) (CFL) on or about September 24, 2019 (Application).

2. Sezzle was incorporated in Delaware on January 4, 2016 and its principal place of business is located at 251 1st Avenue N, Suite 200, Minneapolis, Minnesota 55401.
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3. Sezzle describes itself on its website at www.sezzle.com as a “fin-tech company with a purpose. . . . A company driven to financially empower the next generation. A generation comfortable with technology, but uncomfortable with traditional financial institutions.”

4. Sezzle offers a product that allows consumers residing throughout the United States to enter into installment loans of small amounts in order to purchase products online at over 6,800 participating merchants.

5. Sezzle’s Application describes its business as “provid[ing] interest free on-line financing to consumers.”

6. Sezzle describes its product to consumers as follows:

Get what you want now. Pay over time. 4 installments. 6 weeks. 0% interest. 25% today. 25% in 2 weeks. 25% in 4 weeks. 25% in 6 weeks. No Interest, ever. Sezzle doesn’t charge interest and you pay no fees if you pay on time. No impact to your credit score. Using Sezzle will never affect your credit score. Instant Approval. Signup takes no more than a few minutes. Instantly find out how much you’re approved to spend.

7. Sezzle targets younger consumers who are unable to qualify for traditional purchase finance products, like credit cards.

8. Sezzle has not previously applied for a license to lend in California because Sezzle does not consider its financing product a loan.

9. Rather, Sezzle contends that, “[w]ith respect to California consumers, Sezzle purchases credit sale contracts from merchants who sell goods to consumers.” Sezzle further contends that it’s purchases of credit sale contracts do not constitute loans under California law and, thus, are not subject to the CFL.

10. The Commissioner disagrees and seeks to deny Sezzle’s Application due to Sezzle’s making of loans to Californians without a license.

II.

Applicable Law

11. The CFL “shall be liberally construed and applied to promote its underlying purposes and policies,” which include protecting California borrowers, “ensur[ing] an adequate supply of credit to borrowers in this state,” and “develop[ing] fair and economically sound lending practices.”
12. The Department of Business Oversight, through the Commissioner, has jurisdiction over the licensing and regulation of persons engaged in the business of lending pursuant to the CFL.

13. “Upon reasonable notice and opportunity to be heard, the commissioner may deny the application for a finance lender [if] [t]he applicant . . . has violated any provision of [the CFL] or the rules thereunder or any similar regulatory scheme of the State of California or a foreign jurisdiction.” (Id., § 22109, subd. (a)(3).)

General rule: Making loans requires a license

14. It is a violation of the CFL to “engage in the business of a finance lender . . . without obtaining a license from the commissioner.” (Id., § 22100, subd. (a).)

15. A finance lender “includes any person who is engaged in the business of making consumer loans . . . .” (Id., § 22009.)

16. A consumer loan “means a loan . . . the proceeds of which are intended by the borrower for use primarily for personal, family, or household purposes.” (Id., § 2203.)

17. Put simply, a loan is a “grant of something for temporary use,” and the business of lending money is the business of providing temporary use of money. (Black’s Law Dictionary (11th ed. 2019); Boerner v. Colwell Co. (1978) 21 Cal.3d 37, 44 [a loan is the “hir[ing] of money”]; Milana v. Credit Discount Co. (1945) 27 Cal.2d 335, 339.)

An exception to the rule: non-evasive, bona fide credit sales are not treated as loans under the law

18. In California, merchants may sell goods in exchange for cash (a “cash sale”) or in exchange for a consumer’s promise to pay later (a “credit sale”). (Verbeck v. Clymer (1927) 202 Cal. 557, 562-563.)

19. Merchants may charge a premium for credit sales without the transaction being subject to the state’s loan laws and without the premium being subject to the state’s usury limit. (Id. [“[T]he owner of property . . . may offer to sell at a designated price for cash or at a much higher price on credit, and a credit sale will not constitute usury however great the difference between the two prices . . . .”] [emphasis added]; Milana, 27 Cal.2d at 340.)

20. Although not regulated in California as loans, most credit sales payable in installments
are otherwise subject to consumer protection laws, including the Unruh Act (Civil Code, § 1801, et seq.), which at the time of Boerner provided limits on credit sale premiums. (See Boerner, 21 Cal.3d at 46.)

21. However, wary of misuse, California’s common law only excepts the making of bona fide credit sales from the state’s lending laws. (Id. at 45.)

22. The CFL expressly incorporates the common law’s limited exception for credit sales. (Fin Code, § 22054 [The CFL “does not apply to bona fide conditional contracts of sale involving the disposition of personal property . . . .”] [emphasis added].)

23. The CFL sets forth an additional limit, providing that only credit “sales agreements . . . not used for the purpose of evading” the CFL are excepted from regulation under the CFL. (Id. [emphasis added].)

24. “[T]he courts, alert to the resourcefulness of some lenders in fashioning transactions designed to evade the usury law, have looked to the substance rather than the form of such transactions in assessing their effect and validity, and in many cases have struck down . . . arrangements bearing little facial resemblance to what is normally thought of as a ‘loan’ . . . of money.” (Boerner, 21 Cal.3d at 44-45; Milana, 27 Cal.2d at 340 [“[C]ourts have been alert to pierce the veil of any plan designed to evade the usury law and in doing so to disregard the form and consider the substance.”].)

25. “[T]he issue is whether or not the bargain of the parties, assessed in light of all the circumstances and with a view to substance rather than form, has as its true object the hire of money . . . .” (Boerner, 21 Cal.3d at 44.)

26. In assessing the substance of a transaction, courts consider “[a]ll of the negotiations, circumstances and conduct of the parties surrounding and connected with their contracts . . . .” (Milana, 27 Cal.2d at 341.)

1 Contracts documenting consumers’ promises to pay credit sales in installments are typically referred to as “retail installment contracts.” (Black’s Law Dictionary (11th ed. 2019).) One example of retail installment contracts are “conditional sales contracts,” which are “contract[s] for the sale of goods under which the buyer makes periodic payments and the seller retains title to or a security interest in the goods.” (Id.)
27. California law permits third parties to purchase a merchant’s non-evasive, bona fide credit sales contracts without such purchases necessarily subjecting the transactions to the state’s loan laws. (*Boerner*, 21 Cal.3d at 45 [“the fact of assignment in and of itself has no significant effect on the characterization of the transaction according to its substance”] [emphasis in original].)

28. Nevertheless, extensive third-party involvement in the underlying credit sale may cause transactions to be deemed loans, regardless of the form. (*Id.* at 50 [noting “the most troublesome aspect of the subject transactions from the point of view of assessing their true substance: the role of the third-party financing institution”?]).

29. Extensive third-party involvement may cause transactions to be deemed loans even if the underlying credit sale is bona fide. (*Front Line Motor Cars*, 35 Cal.App.5th at 168 [“[A]n indisputable predicate fact in [prior cases] is that the credit sales were bona fide. The issue in those cases was whether — given the buyers’ and sellers’ mutual intent to consummate bona fide credit sales — the participation of the finance companies converted the credit sales into transactions involving loans.”].)

30. *Boerner* is the “seminal case differentiating a credit sale from a loan,” (*Front Line Motor Cars*, 35 Cal.App.5th at 164), and appears to set the boundary of permissible third-party involvement in an otherwise non-evasive, bona fide credit sale.

31. Although no court in California has considered whether transactions like those structured and marketed by Sezzle are loans, the common law provides three pertinent principles in evaluating third-party participation when considering the substance of a transaction.

32. First, a transaction may be considered a loan, despite its form, if a third-party’s involvement with the merchant goes beyond that necessary to effectuate the purchase of credit sales.

2 (*See, e.g., id.*, 21 Cal.3d at 44 [considering whether third-party’s purchase of vacation home builder’s credit sales constituted making a loan to consumer]; *Milana*, 27 Cal.2d at 340 [considering whether third-party’s purchase of merchant’s account receivables constituted a loan to the merchant]; *West Pico Furniture Co. v. Pacific Finance Loans* (1970) 2 Cal.3d 594, 603-604 [same]; *Front Line Motor Cars v. Webb* (2019) 35 Cal.App.5th 153, 164.)
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(Glaire v. La Lanne-Paris Health Spa, Inc. (1974) 12 Cal.3d 915, 925 [“Where, as appears here, a finance company assumes so close a relationship with a seller that it becomes an integral part of the seller’s financing program, the finance company must” be considered a lender.].)

33. Second, a transaction may be considered a loan, despite its form, if the role of the third party and terms of the transaction are not fully disclosed to the consumer. (See Boerner, 21 Cal.3d at 53.)

34. Third, a transaction may be considered a loan, despite its form, if the third party does not bear the full risk of consumer performance under the credit sale. (See Milana, 27 Cal.2d at 342; West Pico, 2 Cal.3d at 605.)

III.

Findings

Sezzle’s merchants make evasive credit sales contracts that are not bona fide.

35. Unlike any reported California case on this issue, Sezzle markets its financing products to consumers before the consumers have decided to shop at a particular merchant or to purchase a particular product. Sezzle encourages its users to only shop at merchants who accept Sezzle. The most prominent feature of Sezzle’s website is a directory or virtual mall of Sezzle merchants, including promotions for “featured” merchants. Resulting from Sezzle’s direct consumer marketing, Sezzle recruits new merchant with the claim that merchants who offer Sezzle “increase[] sales and order volumes.” As Sezzle tells potential partners on its website, “[w]e’re especially popular with younger users - shoppers 18 and older that might not have access to traditional lines of credit.”

36. A sine qua non of a credit sale contract is a contract between a merchant and their customer. However, Sezzle’s consumers and merchants do not enter into contracts with each other. There is no existing contract for Sezzle to purchase, and there is no manifested intent from merchants to make sales on credit to consumers. Sezzle’s contracting process with consumers is as follows:

i. Consumers can establish an account with Sezzle in advance of any purchase or any visit to a merchant website. To create an account, consumers must agree to the Sezzle User Agreement (User Agreement) and must “approve Sezzle to make a credit inquiry as an aid to approve
my use of Sezzle for this and future purchases.” Despite the reference to a specific purchase, the User Agreement may be executed prior to the involvement of any Sezzle merchant or the contemplation of any specific purchase.

ii. The User Agreement is between Sezzle and its users. Sezzle’s merchants are not parties to the User Agreements. The User Agreement is a non-negotiable, clickthrough agreement, subject to unilateral changes post-execution by Sezzle. The User Agreement is changed by Sezzle often. The currently effective User Agreement is available online at https://legal.sezzle.com/user.

iii. The first two sentences of the User Agreement, located in Section 1.1, declare that “[t]his Agreement describes the terms between Sezzle . . . and you . . . for the financing provided by Sezzle to you for the goods and/or services you purchased from the Sezzle Merchant. Through this Agreement, Sezzle has extended you credit and the right to defer payment for the goods and/or services you have purchased.” There are at least eight other parts of the User Agreement that refer to Sezzle providing direct consumer financing.3 The “user” in the User Agreement is defined as the “person or entity who uses Sezzle Services to purchase products or services from Merchants.”

iv. In the User Agreement, consumers also agree to Sezzle’s “Sezzle Card Holder Addendum,” which is described in the User Agreement as follows: “Sezzle offers an interest free installment loan/retail installment credit card that allows users to make purchases from Sezzle Merchants (‘Sezzle Card’). Any purchase made using the Sezzle Card is subject to the Sezzle Card Holder Addendum.”

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3 (See Sections 1.2 (“Sezzle may unilaterally decide to change this Agreement from time to time, including your credit limit . . .‘”); 2.1 (“Sezzle is a payment processing platform designed to allow Users to finance and buy products today and pay for them later, through a down payment followed by installment payments.”); 2.2 (referencing “your promise to pay the amount of the goods and services financed by . . . Sezzle” and “confirming the financing of any purchases through . . . Sezzle”); 2.6 (“We provide you with financing for your purchases.”); 3.1 (“You can use Sezzle to pay for purchases of goods and services from Sezzle Merchants . . .”); 3.2 (“We may, at our discretion, impose limits on the amount of money you can use to purchase goods or services . . .”); 4.1 (obtaining authorization to identify “business risks that may exist to Sezzle in offering financing to you”); and, separate “legal definition” for “Merchant Account” (“an account created with Sezzle by the Merchant for the purposes of accepting Sezzle as a payment option”.)
37. Sezzle structured its merchants’ purported credit sales to evade any consumer protection obligations Sezzle may have otherwise owed to consumers under the Unruh Act or the federal Truth in Lending Act (15 U.S.C. § 1601 et seq.) by limiting the number of installment payments to four.

Sezzle’s role in the transaction causes the transactions to be loans regardless of their form.

38. Sezzle’s involvement with its merchants goes well beyond any non-lending relationship yet permitted by California courts, and the credit sales purportedly purchased by Sezzle do not justify Sezzle’s extensive involvement. (Compare Boerner, 21 Cal.3d at 53 & n. 17 [noting that third-party financer’s provision of forms to document transaction was “beneficial” given the complicated nature of a sale of construction services secured by real property].) In addition to purportedly purchasing merchants’ credit sales contracts, Sezzle provides its merchants marketing services, payment processing services, consumer dispute resolution services, and interest-bearing accounts in which merchants can park the revenue earned from Sezzle. Sezzle’s contracting process with merchants is as follows:

i. To offer Sezzle as a payment option, merchants must create an account with Sezzle through which merchants are asked to provide basic contact information, yearly sales, and average order volume. And, to create an account, merchants must first agree to the Sezzle Merchant Agreement (Merchant Agreement).

ii. The Merchant Agreement is between Sezzle and its merchants. Sezzle’s users are not parties to the Merchant Agreement. The Merchant Agreement is a non-negotiable, clickthrough agreement, subject to unilateral changes post-execution by Sezzle; although Sezzle does promise that, “[i]f Sezzle makes any changes to this Agreement that it deems to be material, Sezzle will make a reasonable effort to inform you of such changes, but it is your responsibility to review the Agreement posted on our website from time to time to see if it has been changed.” The Merchant Agreement is changed by Sezzle often. The currently effective Merchant Agreement is available online at https://legal.sezzle.com/merchant.

iii. Like the User Agreement, the Merchant Agreement describes Sezzle’s product as providing credit to consumers, rather than purchasing credit sales contracts from merchants. The
first sentence of Section 2.1, which purports to describe Sezzle’s service, states that “Sezzle is a
technology that enables Users [to] pay for purchases via an Interest Free Payment Plan.” The
merchant in the Merchant Agreement is the “entity who is using Sezzle Services to process payments
for products or services.” The merchant’s account is defined as “an account created with Sezzle by
the Merchant for the purposes of accepting Sezzle as a payment option . . . .”

39. Consumers using Sezzle are not fully informed of the role of Sezzle or all financing
terms. Sezzle reserves the right to unilaterally impose new fees on consumers subsequent to
execution of the User Agreement. Unlike Boerner, Sezzle’s merchants do not disclose cash and
credit prices, and do not disclose the fees merchants pay to Sezzle. And, unlike Boerner, Sezzle
prohibits merchants from charging a higher credit sale price, thereby ensuring that its merchants
make less from their credit sales than they would from a cash sale in which they would not pay
Sezzle’s fees.

40. Sezzle does not bear the full risk of loss from performance on the credit sales
contracts it purchases. The Merchant Agreement provides Sezzle an opportunity to review and
refuse providing financing for certain consumer purchases, despite the sale having already been
processed by the merchant. Section 4.1 of the Merchant Agreement provides that “[f]unds from
Sezzle transactions typically settle into your external bank account one (1) to seven (7) business
days after the product is shipped. The exact settlement time will depend on explicit agreements and
approval decisions made by Sezzle’s staff. In some cases, due to risk decisions, delayed shipment,
made-to-order products, or excessive Dispute levels, Sezzle may implement a settlement time longer
than this initial range.” Section 12.2 of the Merchant Agreement also provides that merchants
“agree to an extended funds settlement period of 42 days at account closure to ensure funds are
available for returns and refunds.”

Policy considerations do not otherwise justify exempting Sezzle’s transactions.

41. Unlike some of the reported cases in California, there are no countervailing policy
considerations justifying the exemption of Sezzle’s product from the state’s loan laws.

42. Sezzle’s financing product may be worse for consumers than comparable, regulated
options. For example, at least one Sezzle merchant allows consumers to use Sezzle to finance
1. purchase amounts as low as $35.00. If a consumer used Sezzle to finance a $35.00 purchase and was
2. charged all fees provided under the User Agreement, the consumer would have paid an equivalent
3. annual percentage rate (APR) of about 600% on their purchase. In comparison, in Boerner, the
4. consumers were charged slightly more than the state’s usury limit. (Boerner, 21 Cal.3d at 44 n.5
5. [two transactions at issue charged between 11.6-12.5% APR].)
6. 43. Unlike Boerner, there is no direct indication from the Legislature that Sezzle’s
7. underlying credit sales should be exempt from the Unruh Act or other consumer protection laws.
8. And, unlike Boerner, there are no indications that Sezzle provides a unique financing alternative
9. whose absence from the market in its current form would imperil commerce generally. (Id. at 46 n.
10. 11 [“To subject sales-finance companies to the usury acts, however, might constitute a death blow to
11. this vital enterprise. Instalment [sic] credit is so expensive to service that a finance company often
12. cannot operate profitably within the limitations of most usury acts.”]; see also Glaire, 12 Cal.3d at
13. 925.)

IV.

Conclusion and Prayer

Sezzle’s purported purchasing of credit sale contracts between merchants and California
consumers constitutes the making of loans under California law and, thus, requires a CFL license.
“All of the negotiations, circumstances and conduct of the parties surrounding and connected with”
the transactions show that Sezzle did not buy merchants’ credit sale contracts; Sezzle provided
consumers temporary use of money.

WHEREFORE, IT IS PRAYED that:

Pursuant to Financial Code section 22109, subdivision (a), paragraph (3), Sezzle’s
Application is denied due to Sezzle’s prior violations of Financial Code section 22100, subdivision
(a), for engaging in the business of a finance lender without obtaining a license.

Dated: December 30, 2019 MANUEL P. ALVAREZ
Los Angeles, CA Commissioner of Business Oversight

By______________
Adam Wright
Senior Counsel