MEMORANDUM
OFFICE OF THE CITY ATTORNEY

CONFIDENTIAL ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

DATE: June 12, 2017

TO: Sign Ordinance Review Committee File

FROM: Ariel Pierre Calonne, City Attorney
Megan McMahon, Law Clerk

SUBJECT: Commercial Speech Regulation

ISSUES PRESENTED

1. Does the commercial speech doctrine survive the Supreme Court's decision in *Reed v. Town of Gilbert?*

2. If so, what are the applicable legal standards for regulating commercial speech?

SHORT ANSWERS

1. Probably.

2. Commercial speech -- speech which proposes a commercial transaction -- is protected by the First Amendment as long it is truthful and nonmisleading. Regulations of commercial speech must pass the four-part *Central Hudson* intermediate scrutiny test. However, regulations of commercial speech which distinguish based on the content of the speech or the identity of the speaker are subject to heightened scrutiny under *Sorrell.* In contrast, laws compelling commercial speech, such as laws requiring disclosures, are subject to a lower level of scrutiny. According to *Zauderer*, laws requiring purely factual disclosures will pass scrutiny under the First Amendment as long as the law is "reasonably related" to a substantial government interest.

DISCUSSION

1. The Supreme Court's decision in *Reed v. Town of Gilbert* did not supplant existing commercial speech doctrine.

While the United States Supreme Court has not explicitly ruled on whether its decision in *Reed* applies to commercial speech, the Ninth Circuit touched on the issue in a footnote of a case decided after *Reed*. In *Lone Star Sec. & Video, Inc. v. City of Los Angeles*, the Ninth Circuit noted that "although laws that restrict only commercial speech are content based… such restrictions need only withstand intermediate scrutiny." (*Lone Star Sec. & Video, Inc. v. City of Los Angeles* (9th Cir. 2016) 827 F.3d 1192, 1198, fn.3.) However, a court could interpret that footnote as merely non-binding dicta because the speech at issue was not commercial speech and thus it did not influence the holding.

Although the Ninth Circuit has not addressed the question whether *Reed* overruled *Central Hudson*, the Ninth Circuit has continued to rely on *Central Hudson* since *Reed* was decided. (See *Retail Digital Network, LLC v. Appelsmith* (9th Cir. 2016) 810 F.3d 638; see also *CTIA- The Wireless Association v. City of Berkeley, California* (9th Cir. 2017) 854 F.3d 1105, 1115.) This continued reliance on *Central Hudson* suggests that the commercial speech doctrine is alive and well.

In addition, post-*Reed,* the District Courts for the Northern and Central Districts of California have held that *Reed* does not apply to commercial speech. Therefore, when speech is deemed commercial, intermediate scrutiny as defined by the *Central Hudson* test applies. (See *Contest Promotions, LLC v. City & Cty. Of San Francisco* (N.D. Cal. 2015) 2017 U.S. Dist. LEXIS 63567 at p.11 ["*Reed* does not concern commercial speech, and therefore does not disturb the framework that commercial speech is subject only to intermediate scrutiny as defined by the *Central Hudson* test."]; *California Outdoor Equity Partners v. City of Corona* (C.D. Cal. 2015) 2015 U.S. Dist. LEXIS 89454 at pp. 26-27 ["*Reed* does not concern commercial speech, let alone bans on off-site billboards. The fact that *Reed* has no bearing on this case is abundantly clear from the fact that Reed does not even cite *Central Hudson*, let alone apply it."]; *Citizens for Free Speech v. County of Alameda* (N.D. Cal. 2015) 114 F. Supp. 3d 952 [holding that *Reed* does not alter the analysis for laws regulating off-site commercial speech]; *CTIA- The Wireless Ass'n v. City of Berkeley* (N.D. Cal. 2015) 139 F.Supp. 3d 1048, 1061 ["The Supreme Court has clearly made a distinction between commercial speech and noncommercial speech . . . and nothing in its recent opinions, including *Reed*, even comes close to suggesting that that well-established distinction is no longer valid."]; *San Francisco Apt. Ass'n v. City & Cnty. Of San Francisco* (N.D. Cal. 2015) 142 F. Supp.3d 910, 922 [holding

that *Reed* was inapplicable because it "does not concern commercial speech," which is instead analyzed under *Central Hudson*].)

In conclusion, it is unlikely that *Reed* changed the legal analysis applicable to commercial speech regulations. Thus, the City can regulate noncommercial signs over commercial signs in certain circumstances, i.e., so long as the four-part *Central Hudson* test is satisfied.

2. Overview of the Commercial Speech Doctrine

a. <u>What is commercial speech?</u>

Commercial speech is "expression related solely to the economic interests of the speaker and its audience." (*Cent. Hudson Gas & Elec. Corp. v. Pub. Serv. Comm'n of New York* (1980) 447 U.S. 557, 561.) In other words, speech is commercial if it does "no more than propose a commercial transaction." (*Coyote Publ'g, Inc. v. Miller* (9th Cir. 2010) 598 F.3d 592, 598.) Thus, commercial speech includes any communication that proposes a commercial transaction that is likely to influence consumers in their commercial decisions. (*Ibid.)*

The Supreme Court has recognized the difficulty of determining whether speech is commercial. Accordingly, when it is not clear whether speech is commercial, the Court set out three factors relevant to the determination: (i) whether the speech is an advertisement, (ii) whether the speech refers to a specific product, and (iii) whether the speaker has an economic motive for the speech. *(Bolger v. Youngs Drug Prods. Corp.* (1983) 463 U.S. 60, 66-67.) Although these factors on their own are not determinative, the Court held that the "combination of all these characteristics" provides strong support for the conclusion that the speech in question is commercial. (*Id.* at p. 67.)

b. <u>Regulations of truthful, nonmisleading commercial speech</u>

Commercial speech is protected by First Amendment only if it concerns lawful activity and is not misleading. (See *Cent. Hudson Gas & Elec. Corp. v. Pub. Serv. Comm'n of New York, supra,* 447 U.S at 566.) Regulations applicable to truthful, nonmisleading commercial speech are analyzed under a four-part intermediate scrutiny test set forth by the United States Supreme Court in *Central Hudson Gas & Electric Corp. v. Public Service Commission of New York*. (*Id*. at p. 564-66.) Under the *Central Hudson* test, a court must determine:

(1) Whether the expression is protected by the First Amendment;

(2) whether the asserted governmental interest is substantial;
(3) whether the regulation directly advances the governmental interest asserted; and,
(4) whether it is not more extensive than is necessary to serve that interest. *(Id.* at p. 566.)

The fourth prong of *Central Hudson,* the "narrowly tailoring" prong, requires "a reasonable fit between the legislature's ends and the means chosen to accomplish those ends." *(Lorillard Tobacco Co. v. Reilly* (2001) 533 U.S. 525, 556.) The burden is on the government to show that the elements of the test are satisfied. (*44 Liquormart v. Rhode Island* (1996) 517 U.S. 484, 504-05.)

Despite several members of the Supreme Court expressing doubts about the continued validity of *Central Hudson*, the Court has continued to apply this framework for regulations of commercial speech. (*Lorillard Tobacco Co. v. Reilly* (2001) 533 U.S. 525, 555 ["Admittedly, several Members of the Court have expressed doubts about the Central Hudson…"]; *See, e.g., Greater New Orleans Broad. Ass'n v. United States* (1999) 517 U.S. 173, 197 [conc. opn. of Thomas, J.]; *44 Liquormart, Inc. v. Rhode Island*, *supra*, 517 U.S. at pp. 501, 510-14 [joint opn. of Stevens, Kennedy and Ginsburg, JJ.]; *Id.* at p. 518 [conc. opn. of Thomas, J.])[1] However, subsequent commercial speech cases have applied a more rigorous form of intermediate scrutiny than what *Central Hudson* outlined. (See, e.g., *44 Liquormart v. Rhode Island, supra,* 517 U.S. 484; *Lorillard Tobacco Co. v. Reilly*, *supra,* 533 U.S. 525.)

For example, in *44 Liquormart*, the Court struck down a flat ban on advertising liquor prices. (*44 Liquormart v. Rhode Island, supra,* 517 U.S. 484.) The Court held that the State did not meet its burden to prove that the regulation directly advanced the government's interest because the State presented no evidence to suggest that its speech prohibition would *significantly* reduce marketwide alcohol consumption. (*Id.* at p. 505.) Moreover, the Court held the law was not narrowly tailored. (*Id.* at p. 530.) The Court stated that the "State has other methods at its disposal—methods that would more directly accomplish this stated goal without intruding on seller's ability to provide truthful, nonmisleading information to customers." *(Ibid.)* For example, a tax on alcoholic products "would have a far more certain and direct effect on prices, without any restriction on speech." *(Ibid.)* The Court specified that the "availability of less burdensome alternatives to reach the stated goal signals that the fit between the legislature's ends and the means chosen to accomplish those ends may be too imprecise to withstand First

[1] Justice Thomas has said that he sees no reason for a distinction between commercial and non-commercial speech, and he advocates applying strict scrutiny to regulations of commercial speech.

Amendment scrutiny." *(Ibid.)* This case is significant because it demonstrates that the government must produce evidence that the law directly and significantly advances the substantial government interest. Additionally, the Court has clearly put more teeth into the narrow tailoring prong of *Central Hudson*. Therefore, if a less burdensome alternative exists, the commercial speech regulation is likely to fail intermediate scrutiny.

c. Content-Based and Speaker-Based Regulations of Commercial Speech

Consistent with *Central Hudson*, courts previously applied intermediate scrutiny to content-based and content-neutral regulations of commercial speech alike. (See *Coyote Publ'g, Inc. v. Miller, supra,* 598 F.3d at p. 599 n. 10.) However, in 2011 the Supreme Court in *Sorrell v. IMS Health, Inc.* departed from traditional commercial speech doctrine when it suggested that regulations of commercial speech that are content- or speaker-based are subject to heightened scrutiny. (*Sorrel v. IMS Health, Inc.* (2011) 564 U.S. 552, 565.) At issue in *Sorrell* was a Vermont statute which prohibited drug companies from purchasing prescribing information from pharmacies, insurers, or other entities. (*Id.* at p. 557.) The law also restricted drug companies from using such information "for marketing or promoting a prescription drug, unless the prescriber consents." (*Id.* at p. 558.) The Court, instead of engaging in traditional commercial speech analysis, where the Court would begin its analysis by identifying the commercial character of the communication before analyzing the government's restriction on that communication, began its analysis by stating that the law implemented speech restrictions based on the content of the speech and the identity of the speaker. *(Id.* at pp. 563-64.) The Court declared that heightened scrutiny is required "whenever the government creates 'a regulation on speech because of the disagreement with the message it conveys.'" (*Id.* at p. 565.) This language suggests that content- or speaker-based restrictions on speech, even if they regulations concerning commercial speech, are subject to a heightened level of scrutiny. However, the Court did not actually apply heightened scrutiny, as it found that the law could not withstand intermediate scrutiny under *Central Hudson*. (*Id.* p. at 571.)

Following *Sorrell*, many federal courts of appeals have held that *Sorrell* modifies *Central Hudson* by requiring "heightened judicial scrutiny" for content-based or speaker-based commercial speech regulations. (See *1-800-411-Pain Referral Serv., LLC v. Otto* (8th Cir. 2014) 744 F.3d 1045, 1055; *United States v. Caronia* (2d Cir. 2012) 703 F.3d 149; *Am. Civil Liberties Union of Ill. v. Alvarez* (7th Cir. 2012) 679 F.3d 583; *King v. Governor*

of the State of N.J. (3d Cir. 2014) 767 F.3d 216; *Retail Digital Network, LLC v. Appelsmith* (9th Cir. 2016) 810 F.3d 638, 648.)[2]

Although not binding precedent, the Ninth Circuit's opinion in *Retail Digital Network* provides insight into how *Sorrell* has modified the *Central Hudson* framework, and how a court may apply this more demanding level of intermediate scrutiny. Under the Ninth Circuit's approach, the commercial speech inquiry begins first by asking whether the government regulation restricting speech was content-or speaker-based. (*Retail Digital Network, LLC v. Appelsmith, supra,* 810 F.3d at p. 648.) If the challenged law is content- or speaker-based, then heightened scrutiny is required. (*Ibid.)*

The Ninth Circuit implicitly acknowledged that *Sorrell* did not precisely define what "heightened scrutiny" meant, but the Ninth Circuit indicated that it was something less than strict scrutiny, but more than intermediate scrutiny. *(Retail Digital Network, LLC v. Appelsmith, supra,* 810 F.3d at fn.3.) In essence, the Ninth Circuit suggested that a more exacting form of *Central Hudson* review, using the *Central Hudson* framework, would constitute heightened judicial scrutiny. (*Id.* at p. 648.) The court then went on to discuss the third and fourth prong of *Central Hudson*, as modified by *Sorrell*. (See *Id.* at p. 648.) With respect to the third *Central Hudson* factor, the government bears the burden to show "that the harms it recites are real and that its restriction will in fact alleviate them to a material degree." (*Ibid.)* In order to determine if the law directly advances the government interest, a court will not only look at the asserted justification, but also to the legislature's actual purpose, i.e., "the legislative purposes that the court finds actually animated a challenged law." (*Ibid.)* Moreover, a court will not consider post hoc rationalizations. (*Ibid.)* With respect to the fourth factor, the government bears a "heavier burden" of showing that the challenged law does not reach further than necessary to accomplish the given objective. (*Ibid.)* The court noted that this requirement is "demanding," but is "something short of a least-restrictive means standard" that the government must meet under strict scrutiny. (*Id.* at p. 649.)

d. Compelled Speech Regulations

Laws regulating or prohibiting commercial speech are subject to the *Central Hudson* intermediate scrutiny test. (*CTIA- Wireless Ass'n v. City of Berkeley, supra,* 854 F.3d at p. 1115.) However, laws compelling commercial speech, such as laws requiring

[2] On November 15, 2016, this case was ordered to be heard en banc and it may not be cited as precedent. (*Retail Digital Network, LLC v. Gorsuch* (9th Cir. 2016) 842 F.3d 1092.)

disclosures in advertising and warnings on certain products, are subject to the rule announced in *Zauderer v. Office of Disciplinary Counsel of Supreme Court* (1985) 471 U.S. 626. Under *Zauderer*, compelled disclosure of commercial speech complies with the First Amendment if the information in the disclosure is "reasonably related to a substantial governmental interest" and is purely factual. (*CTIA-Wireless Ass'n v. City of Berkeley*, *supra,* 854 F.3d. at p. 1118.) Preventing public deception and protecting the health, safety, and welfare of consumers are all substantial governmental interests justifying such a regulation. (*Id.* at 1116-17.)

In *Zauderer*, the defendant was disciplined under Ohio state bar professional responsibility rules on the grounds that defendant's advertisement for legal services on a contingent fee basis was "deceptive" within the meaning of the rules. (*Zauderer v. Office of Disciplinary Counsel of Supreme Court, supra,* 471 U.S. at pp. 630-635.) The defendant violated the disciplinary rules by failing to provide information about how the contingent fee would be calculated and by neglecting to disclose the client's potential liability for certain litigation costs. (*Id.* at p. 633-34). The Supreme Court noted that Ohio did not attempt to prevent attorneys from conveying information to the public, but rather had "only required them to provide somewhat more information than they might otherwise be inclined to present." (*Id.* at p. 650.) Therefore, the Court reasoned that mere rational basis review was sufficient in such cases because "disclosure requirements trench much more narrowly on an advertiser's interest than do flat prohibitions on speech." (*Id.* at p. 672.) In addition, such regulations are consistent with the First Amendment because commercial speech protection "is justified principally by the value to consumers of the information such speech provides." (*Ibid.*) The Court held that the disclosure requirements of the state's professional responsibility rule concerning legal advertising was reasonably related to the state's interest in preventing deception of consumers, and upheld defendant's disciplinary sanctions under the rule. (*Id.* at p. 673.)

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