

**FTC STAKEHOLDER PERSPECTIVES:
REFORM PROPOSALS TO IMPROVE FAIRNESS,
INNOVATION, AND CONSUMER WELFARE**

HEARING

BEFORE THE

SUBCOMMITTEE ON CONSUMER PROTECTION,
PRODUCT SAFETY, INSURANCE,
AND DATA SECURITY

OF THE

COMMITTEE ON COMMERCE,
SCIENCE, AND TRANSPORTATION
UNITED STATES SENATE

ONE HUNDRED FIFTEENTH CONGRESS

FIRST SESSION

SEPTEMBER 26, 2017

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SENATE COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION

ONE HUNDRED FIFTEENTH CONGRESS

FIRST SESSION

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CONTENTS

	Page
Hearing held on September 26, 2017	1
Statement of Senator Moran	1
Prepared statement	2
Statement of Senator Blumenthal	3
Letter dated September 25, 2017 to Hon. Richard Blumenthal from Paul Zurawski, Senior Vice President, External Affairs, Equifax	61
Statement of Senator Inhofe	63
Statement of Senator Capito	64
Statement of Senator Young	66
Statement of Senator Hassan	68
Statement of Senator Klobuchar	70
Statement of Senator Markey	72
Statement of Senator Cortez Masto	74
WITNESSES	
William MacLeod, Partner, Kelley Drye & Warren LLP	5
Prepared statement	7
Lydia Parnes, Esq., Partner, Wilson Sonsini Goodrich & Rosati PC	12
Prepared statement	14
Jessica Rich, Vice President, Consumer Policy and Mobilization, Consumer Reports	18
Prepared statement	19
Berin Szóka, President, TechFreedom	23
Prepared statement	25
APPENDIX	
Joshua D. Wright, Professor, George Mason University School of Law and Director, Global Antitrust Institute, prepared statement	79
Scott Smith, President, Precious Metals Association of North America, pre- pared statement	94
Report dated May 2016 from Berin Szóka and Geoffrey A. Manne entitled, “The FTC Trade Commission: Restoring Congressional Oversight of the Second National Legislature—An Analysis of Proposed Legislation”	96
Presidential Transition Report: The State of Antitrust Enforcement dated January 2017 from the American Bar Association Section of Antitrust Law ..	162
Comments dated September 11, 2017 from Cory L. Andrews and Richard A. Samp of the Washington Legal Foundation to the Federal Trade Com- mission concerning Proposed Consent Agreements and Request for Public Comments in Zero-VOC Paint Claims Cases	205
Letter dated September 26, 2017 to Hon. Jerry Moran and Hon. Richard Blumenthal from Marc Rotenberg, EPIC President; Caitriona Fitzgerald, EPIC Policy Director; and Christine Bannan, EPIC Policy Fellow	213

**FTC STAKEHOLDER PERSPECTIVES:
REFORM PROPOSALS TO IMPROVE FAIRNESS,
INNOVATION, AND CONSUMER WELFARE**

TUESDAY, SEPTEMBER 26, 2017

U.S. SENATE,
SUBCOMMITTEE ON CONSUMER PROTECTION, PRODUCT
SAFETY, INSURANCE, AND DATA SECURITY,
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION,
Washington, DC.

The Subcommittee met, pursuant to notice, at 2:20 p.m. in room SR-253, Russell Senate Office Building, Hon. Jerry Moran, Chairman of the Subcommittee, presiding.

Present: Senators Moran [presiding], Blumenthal, Inhofe, Capito, Young, Hassan, Klobuchar, Markey, Cortez Masto, Booker, and Fischer.

**OPENING STATEMENT OF HON. JERRY MORAN,
U.S. SENATOR FROM KANSAS**

Senator MORAN. The hearing will come to order. Good afternoon, and welcome to today's hearing on FTC Stakeholder Perspectives: Reform Proposals to Improve Fairness, Innovation, and Consumer Welfare.

This is our second attempt at this hearing, and many of our panelists have been polite and kind enough to return. In fact, last September, the full Committee heard testimony from the FTC's three sitting Commissioners at the time: Chairman Ramirez, Commissioner Ohlhausen, and Commissioner McSweeney. We had planned to convene a Subcommittee hearing on that same day, but had to cancel due to scheduling conflicts. The canceled hearing would have consisted of a panel of stakeholders offering their own perspectives about the Commission.

Today we will hear from Berin Szóka, President of TechFreedom, one of the witnesses who was scheduled to testify last September, as well as three former directors of the FTC's Bureau of Consumer Protection: William MacLeod, Lydia Parnes, and Jessica Rich. We thank these former FTC officials for their public service and all the witnesses for appearing today to offer their insights on how we can improve the work of the Commission.

For over a century, the FTC has been protecting competition and consumers by enforcing the Nation's antitrust laws and combating deception and unfairness in a wide variety of industries. Through its efforts, the FTC has often helped to prevent anticompetitive practices that stifle innovation, lower quality, or raise prices. It has

also helped to ensure that consumers can make informed decisions based on accurate advertising and avoid injury from fraud and unfair trade practices, such as unauthorized credit card charges.

Although the FTC's efforts have produced many benefits for consumers and the economy, this Committee and others have questioned the way it sometimes exercises its authority under Section 5 of the FTC Act, which addresses unfair and deceptive acts in commerce. Others have argued that the FTC sometimes conducts investigations and issues orders that impose unnecessary costs, and it does not always provide adequate guidance to businesses seeking to comply with the laws the FTC enforces.

These concerns have sparked numerous proposals for reforming the FTC. For example, last December, the House Energy and Commerce Committee reported H.R. 5510, the FTC Process and Transparency Reform Act of 2016, a bill incorporating eight separate reform bills designed to clarify the FTC's unfairness authority, improve the way the FTC operates, foster greater transparency, and reduce unnecessary costs.

Similarly, in January 2017, earlier this year, the American Bar Association Antitrust Section issued a 60-page Presidential Transition Report. It makes a number of recommendations for improving the FTC's handling of antitrust and consumer protection issues, including repeal of the common carrier exemption and better coordination on privacy between the FTC and other agencies, greater transparency and fairness in the enforcement process, and more judicious use of civil investigative demands, better communication with investigation targets, less burdensome boilerplate order provisions, and monetary relief proportional to the injury caused and the defendant's culpability.

The report also urges the FTC to provide additional guidance on topics relating to unfair practices, data security, monetary remedies, advertising interpretation, and "clear and conspicuous" disclosure requirements. Other private groups, such as TechFreedom, have also proposed various reforms designed to address concerns about the FTC.

The FTC has already taken steps to address some of the concerns addressed by the House bill, by the ABA Report, and other stakeholders. Specifically, this year, the Commission adopted several initiatives to eliminate waste and unnecessary regulation, streamline agency information demands, improve transparency, and promote economic liberty.

As we look ahead to the White House's nominations of candidates to serve as FTC Commissioners, it is especially important for the Committee to provide a forum to address these issues.

We look forward to hearing the testimony of our witnesses and to engaging in a dialogue on the best ways to advance reforms of the Commission.

[The prepared statement of Senator Moran follows:]

PREPARED STATEMENT OF HON. JERRY MORAN, U.S. SENATOR FROM KANSAS

Good afternoon, and welcome to today's hearing on "FTC Stakeholder Perspectives: Reform Proposals to Improve Fairness, Innovation, and Consumer Welfare."

Last September, the full Committee heard testimony from the FTC's three sitting commissioners at the time: Chairman Ramirez, Commissioner Ohlhausen (OL—how—sin), and Commissioner McSweeney. We had planned to convene a Sub-

committee hearing on the same day, but had to cancel it due to scheduling conflicts. The cancelled hearing would have consisted of a panel of stakeholders offering their own perspectives about the Commission.

Today we will hear from Berin Szóka, President of TechFreedom, one of the witnesses who was scheduled to testify last September, as well as three former directors of the FTC's Bureau of Consumer Protection: William MacLeod, Lydia Parnes, and Jessica Rich. We thank these former FTC officials for their public service and all of the witnesses for appearing today to offer their insights on how to improve the Commission.

For over a century, the FTC has been protecting competition and consumers by enforcing the Nation's antitrust laws and combatting deception and unfairness in a wide variety of industries. Through its efforts, the FTC has often helped to prevent anticompetitive practices that stifle innovation, lower quality or raise prices. It has also helped ensure that consumers can make informed choices based on accurate advertising, and avoid injury from fraud and unfair trade practices, such as unauthorized credit card charges.

Although the FTC's efforts have produced many benefits for consumers and the economy, this Committee and others have questioned the way it sometimes exercises its authority under Section 5 of the FTC Act, which addresses unfair and deceptive acts in commerce. Others have argued that the FTC sometimes conducts investigations and issues orders that impose unnecessary costs, and that it does not always provide adequate guidance to businesses seeking to comply with the laws the FTC enforces.

These concerns have sparked numerous proposals regarding how to reform the FTC. For example, last December the House Energy and Commerce Committee favorably reported H.R. 5510, the FTC Process and Transparency Reform Act of 2016, a bill incorporating eight separate reform bills designed to clarify the FTC's unfairness authority, improve the way the FTC operates, foster greater transparency and reduce unnecessary costs.

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As we look ahead to the White House's nominations of candidates to serve as FTC commissioners, it is especially important for this Committee to provide a forum to address these issues.

We look forward to hearing the testimony of our witnesses this afternoon and to engaging in a dialog on the best ways to advance reforms at the Commission.

With that, I will turn to the Ranking Member, Senator Blumenthal, for his opening statement.

Senator MORAN. With that, I turn to the Ranking Member, Senator Blumenthal, for his opening statement.

**STATEMENT OF HON. RICHARD BLUMENTHAL,
U.S. SENATOR FROM CONNECTICUT**

Senator BLUMENTHAL. Thank you, Mr. Chairman. Thank you very much for holding this hearing.

This hearing is critical in reviewing and overseeing the work of the Federal Trade Commission in today's rapidly evolving world

and economy. Congress has long empowered and directed the FTC to protect consumers from unfair, deceptive acts or practices, and unfair methods of competition.

Since the FTC Act was signed into law exactly 103 years ago today, incredibly today, the FTC has proved to be a nimble and agile and sometimes aggressive agency with the experience and expertise necessary to stand up for consumers and promote competitive markets and combat a variety of fraud and other deceptive activity. I know from my personal experience during my service for many years as attorney general of the State of Connecticut how strong and important a partner it can be and should be, even more often than it is, because there are times that the FTC comes down much too softly on industries it oversees, putting the very consumers it is charged with protecting at risk and jeopardy from the harms that it has responsibility to stop.

Last December, to give you one example, the FTC finalized a profoundly flawed consent order that permits used car dealers to advertise that they have rigorously inspected their vehicles for safety, including that they are, quote/unquote, certified, even if the vehicle has unrepaired safety recalls. The settlement had really inadequate and feeble disclosure requirements that failed to fully inform and, worse, create a kind of safe harbor for unscrupulous dealers. Far from protecting consumers, this settlement enables dealers to continue selling dangerous cars with, for example, deadly Takata airbags to unsuspecting buyers. The sale of any car, any car, with an unrepaired safety recall is a threat to public safety, not just the driver, not just the owner, but anybody out there driving alongside or on the road with such a car.

The FTC should have simply prohibited the defendants from advertising the sale of used cars with unrepaired recalls. The courts are clear that the FTC Act empowers the FTC to do more than simply admonish defendants to go sin no more, so to speak, but to proactively prevent defendants from engaging in similar deceptive practices in the future through so-called fencing-in provisions.

I was also dismayed, quite honestly, by the FTC's apparent inaction with respect to Google, even as evidence mounts suggesting Google has repeatedly and consistently abused competition law. This summer, the EU fined Google a record \$2.7 billion for abusing its position as the world's dominant search engine by pushing smaller rivals' results down in search rankings and manipulating the results to promote its own services. The FTC has a duty to investigate and discipline Google or any other company for any illegal actions that may have unfairly disadvantaged competitors and limited consumer choice. Our economy, particularly when it comes to the rapidly growing tech sector, needs robust competition to thrive and ensure consumer protection, and the FTC ought to be an engine and a driver using its muscle to that end.

Equally important are potential limits to the FTC's authority that may constrain its ability to proactively and aggressively protect consumers, and that has been made painfully clear by Equifax's recent disclosure of a massive data breach exposing the personal information of up to 143 million Americans, including their Social Security, birthdates, address histories, and driver license numbers, among other sensitive data.

If the entities that hold our data can't be trusted to protect it, then the government needs to have the right tools to not only go after the hackers and thieves, but also the companies that treat our financial lives with such abandon, negligence, and carelessness.

Let me just say the FTC has brought numerous enforcement actions over the years against companies for lax data security practices, but this piecemeal, after-the-fact, ad-hoc approach would be better served if the Commission had a clear and unlimited civil penalty authority and the ability to prescribe rules requiring reasonable security practices in the first place.

I will push for a measure that I propose that would provide such authority, expanded FTC powers. I also urge that the Justice Department proceed vigorously and promptly with a criminal investigation, and that any other agency with jurisdiction and authority in the Equifax matter seek penalties that protect consumers, deter these kinds of negligent and lax practices in the future, and send a message that data security has to be a number one priority for anybody having our information, and any kinds of negligence or lax practices will not be tolerated.

The FTC has demonstrated time and again it knows how to play this critical role in today's economy, and I hope that it will continue to do so and work with this Committee.

Thank you, Mr. Chairman.

Senator MORAN. Thank you, Senator Blumenthal.

Now, again, we welcome our panel of witnesses. And let me introduce them. Mr. William MacLeod. He is a partner of Kelley Drye and a former Director of the FTC's Bureau of Consumer Protection.

Welcome.

Ms. Lydia Parnes is a partner with Wilson Sonsini Goodrich & Rosati and former Director of the FTC's Bureau of Consumer Protection. Ms. Jessica Rich, Vice President, Policy and Modernization, Consumer Union, and former Director of the FTC's Bureau of Consumer Protection. And Mr. Berin Szóka, President of TechFreedom.

And with that, I will turn to Mr. MacLeod.

**STATEMENT OF WILLIAM MACLEOD, PARTNER,
KELLEY DRYE & WARREN LLP**

Mr. MACLEOD. Thank you, Mr. Chairman, Ranking Member Blumenthal, and members of the Committee. It is a pleasure and a privilege to be here today.

As you mentioned, I am with the law firm of Kelley Drye & Warren, but I am speaking today solely in my own capacity. I am not representing Kelley Drye or any client of Kelley Drye or any other institution for that matter. I'm here today to discuss two institutions that are very dear to me: the first is the Federal Trade Commission, where I spent 8 years, about 4 of which as Director of the Bureau of Consumer Protection; and the second is the Antitrust Section of the American Bar Association. I had the privilege of chairing that section last year, and I was instrumental in assembling the Task Force about which the Chairman spoke, and that was the Task Force to report on the state of antitrust and consumer protection enforcement and make some recommendations. We are here today to talk about some of those recommendations.

But I'd like to start with a story of a case that I handled 19 years ago for a client whose name I won't mention. It was almost exactly 19 years ago when the Federal Trade Commission and eight states, not including the State of Connecticut, brought an action against my client, and the company had just introduced a pesticide product. It was a product that until that time was available only through professionals; you had to subscribe to an expensive exterminator if you wanted to have this product for your home.

The Federal Trade Commission brought an action against the company, not because it alleged anything deceptive in what the company had advertised, but, rather, because it believed the company did not have substantiation in support of its claims. Its claims actually came right off of the label of the product, which the Environmental Protection Agency had approved, but the Federal Trade Commission staff and the Federal Trade Commission ultimately disagreed that the company had enough substantiation for those claims, and even though they did not disagree with any claim the company made, they did think the company should have made more claims, they brought a case, which the company ultimately settled.

That was 19 years ago. That order still exists today. This company is under a regulation of the Federal Trade Commission. Its competitors aren't under this regulation, but this order of about 25 pages, which is now older than some of the voters who will be going to the polls this fall in the elections, still governs the conduct of the company that simply introduced a product to empower consumers. Unless the company mounts an expensive petition or a court motion to modify or terminate this order, it will be around in 2040 when the children of today's new voters are going to the polls the first time.

I never told this story to the Task Force, the ABA Antitrust Section Task Force, but the three lessons I learned in that case and that my client learned the hard way are exactly the highlights that I want to feature in the report. And the first is the age of orders of the Federal Trade Commission. It is a growing body of regulation that is permanent in the case of court orders, is 20 years long in the case of administrative orders, and it is very hard for a company to make those go away.

We propose in our recommendations and report that the FTC impose sunsets in all orders. The Antitrust Division of the Department of Justice does that. Other agencies of the Federal Government do that. They do not have the growing body of regulations.

Second, the story of the disagreement between the Environmental Protection Agency and the Federal Trade Commission is a story that we see today. It is very difficult for a company to organize its affairs and engage in pro-competitive activity if it doesn't know the rules, and, most importantly, if the referees that govern its conduct disagree as to what the rules are.

And the third point is the importance of guidance from the Federal Trade Commission, especially guidance as to the boundaries of advertising: What should be illegal and what should not be illegal? I'm not talking about messages to the con artists; they are not going to pay attention. But the good and honest companies want to know what rules they should abide by, and the Federal Trade

Commission can help them with more guidance on how it interprets ads.

Thank you very much.

[The prepared statement of Mr. MacLeod follows:]

PREPARED STATEMENT OF WILLIAM MACLEOD, PARTNER,
KELLEY DRYE & WARREN LLP

Summary

Thank you for inviting me to testify today. I am William MacLeod, a partner in the law firm Kelley Drye & Warren LLP. I will be speaking solely in my individual capacity today and not as an official representative of any organization.

It was my honor to serve as Chair of the Section of Antitrust Law of the American Bar Association for the 2016–2017 ABA year, and my privilege to join my predecessor, Roxann Henry, in appointing a Task Force to examine the state of antitrust and consumer protection in the United States and to make recommendations to improve enforcement. The Section’s Presidential Transition Task Force issued a comprehensive Report,¹ which was published in the *Antitrust Source*² and is appended to this Statement. The views expressed in that Report are those of the Antitrust Section, and they have not been approved by the House of Delegates or the Board of Governors of the American Bar Association. Therefore, unless otherwise noted, the Section’s views expressed in the Report should not be construed as representing the position of the Association.

The Section of Antitrust law is the leading professional organization for the practice of laws pertaining to antitrust and competition, trade regulation, consumer protection and economics. Its members include attorneys and non-lawyers from private law firms, in-house counsel, non-profit organizations, consulting firms, Federal and state government agencies, as well as judges, professors and law students. The Section’s objectives boil down to four words that appear on its logo: Promoting Competition/Protecting Consumers. These were the objectives that guided the work of the Task Force.

For the composition of the Task Force, we selected attorneys representing defendants and plaintiffs, a member of the Federal judiciary, and law and economics scholars from the Nation’s leading universities. More than half of the members had served in leadership positions in the Antitrust Division of the Department of Justice or the Federal Trade Commission, including several former Assistant Attorneys General and Commissioners as well as officials from every administration over the last four decades.³

At the outset, it should be noted that the Task Force found that the agencies have been in good hands, and that enforcement should remain “firmly tethered” to the statutory basis of enforcement.⁴ Recommending fidelity to the law might seem superfluous, but it was an important response to proposals for radical reorientation of enforcement policy. Prohibiting “unfair” and “deceptive” acts, practices and methods of competition is essential to consumer welfare, but the proscriptions do not have obvious definitions, which makes them tempting tools for tinkering with the outcomes of a competitive market. Clear and transparent enforcement policy is therefore key to distinguishing legal from illegal conduct. By the same token, judicious application of that policy in deciding when and where to prosecute is critical to obtaining the economic benefits of the Commission’s interventions. The Report advises the agency to recognize the enormous impact a prosecution can have on a company, and to focus its “limited enforcement resources on cases involving signifi-

¹American Bar Association, Section of Antitrust Law, Presidential Transition Report: The State of Antitrust Enforcement (January 2017), https://www.americanbar.org/content/dam/aba/publications/antitrust_law/state_of_antitrust_enforcement.authcheckdam.pdf [hereinafter “Report”].

²Available at: https://www.americanbar.org/content/dam/aba/publishing/antitrust_source/jan17_full_source.authcheckdam.pdf

³Report at 1. The Task Force was co-chaired by Theodore Voorhees and Leah Brannon. Samantha Knox served as the Reporter and Organizer. Members included Roxane Busey, Mary Ellen Callahan, Dennis Carlton, Michael A. Carrier, Paul T. Denis, Douglas H. Ginsburg, Louis Kaplow, Donald C. Klawiter, William Kovacic, Jon Leibowitz, Abbott B. Lipsky, Jr., A. Douglas Melamed, Fiona Scott Morton, James H. Mutchnik, Richard Parker, Lydia Parnes, James Rill, and Joel Winston. Megan Browdie served as the ABA Young Lawyer Division’s Representative to the Task Force.

⁴*Id.* at 2.

cant consumer harm.”⁵ This is sound advice. Pursuing minor infractions and challenging economic activity outside its statutory authority not only can distract an agency from its mission, but can be hazardous to an agency itself.⁶

The Report’s recommendations covered both competition and consumer protection, and many of the observations apply to both sides of Commission enforcement, but my testimony today will focus on the consumer side of the agency. For years, consumer protection has consumed more resources, generated more cases, and garnered more public attention than the competition mission.⁷ In 2016, for example, consumer protection actions and orders outnumbered their competition counterparts by more than two to one.⁸ Consumers lodged three million complaints last year with the Commission,⁹ and they have registered over 226 million phone numbers on the Commission’s Do Not Call Registry.¹⁰ From care labels on clothes to disclosures in advertisements to privacy and security of personal information, consumers encounter the effects of FTC regulations, guidelines and enforcement decisions every day.

The Report covered a broad spectrum of consumer protection. Today I will focus on three areas that the Task Force highlighted in its Report. First, I will address a growing body of barnacles on the economy—aging and perpetual regulations in the form of orders and decrees that result from Commission enforcement. Second, I will discuss the need for guidance on Commission interpretations of advertising and the role of disclosures. Third, I will discuss the growing problem of different laws, different agencies and different policies governing the same conduct. Uncoordinated and inconsistent standards make consumer protection compliance more difficult, and can leave gaps in the very protection the rules are intended to provide.

A RISING TIDE OF UNREVIEWED REGULATIONS

[S]ince 1996—the past 20 years—the FTC has required companies signing administrative orders to agree to an order duration of 20 years (longer, if there are subsequent violations) and Federal court orders that last in perpetuity. . . . Especially in areas where technology is rapidly evolving, order provisions that make sense when they are entered may no longer be appropriate in 10 years, let alone 20 years later, and may serve to chill innovative and useful corporate practices.¹¹

The Commission obtains about 150 consumer protection orders a year against corporations and individuals.¹² Some of the orders keep common con artists away from consumers. But many of the defendants and respondents include the largest corporations in the world, and the orders they must observe can impose extensive regulations—obligations that go beyond injunctions against violations of the law. The Commission typically will seek ancillary relief in the form of specific obligations that make it easier for future enforcers to prove that the company violated the terms of the order. For example, a company alleged to have made unsubstantiated claims about the efficacy of a dietary supplement may face an order that requires prescribed levels of substantiation for claims about the health benefits, efficacy, or performance of any food, drug, or dietary supplement.¹³ Once under order, a company faces the peril of civil penalties or a contempt citation for a violation if the FTC alleges that a future advertisement made a covered claim, or that the substantiation

⁵ *Id.* at 27.

⁶ In 1969, and again in 1980, the Commission faced intense criticism for straying from its mission. An ABA Report on the FTC in 1969 was instrumental in refocusing the Commission. AM. BAR ASSN, REPORT OF THE ABA COMMISSION TO STUDY THE FEDERAL TRADE COMMISSION (1969) (commissioned by President Nixon in response to a critique of the FTC by researchers assembled by Ralph Nader, COX, R. FELLMETH & J. SCHULZ, THE CONSUMER AND THE FEDERAL TRADE COMMISSION (1969). A decade later, President Carter intervened to rescue the Commission from Congressional repudiation. See, e.g., MacLeod & Rogowsky, “Consumer Protection under the Reagan Administration,” in Regulation and the Reagan Years, R. Meiners and B. Yandle, eds. (Holmes & Meier, New York, 1989)

⁷ See, e.g., Report at 24; FTC Annual Reports, collected at <https://www.ftc.gov/policy/reports/policy-reports/ftc-annual-reports>.

⁸ FTC, 2016 Annual Highlights, available at <https://www.ftc.gov/node/1205233>.

⁹ *Id.*

¹⁰ FTC, National Do Not Call Registry Data Book for Fiscal Year 2016, available at <https://www.ftc.gov/news-events/press-releases/2016/12/ftc-issues-fy-2016-national-do-not-call-registry-data-book>

¹¹ Report at 29 (footnotes omitted).

¹² FTC, Annual Reports, collected at <https://www.ftc.gov/policy/reports/policy-reports/ftc-annual-reports>.

¹³ Report at 30, n. 94, citing POM Wonderful v. FTC, 777 F.3d 478, 505 (D.C. Cir. 2015).”

did not meet the specific requirements—even if the claim was truthful and substantiated by the standards appropriate at the time it is made.

Recognizing the potential anticompetitive effects and regulatory burdens of perpetual orders, the Commission decided in 1995 to limit administrative orders—those entered in the course of the agency’s internal adjudication—to twenty years duration.¹⁴ But the agency declined to limit Federal court orders, because it said those orders primarily addressed fraudulent activity.¹⁵ To this day, most of those orders are perpetual, and they now account for two-thirds of the orders the FTC enters. Many of them come from cases that do not allege fraud. A failure of a company to produce what the Commission deems to be satisfactory substantiation for a claim can result in an order that stays on the books indefinitely. Every year, in the ordinary course of enforcement, the Commission adds another hundred perpetual regulations to the economy, without the periodic reviews typically applicable to Federal regulations. It is up to the companies struggling with an order provision to do something. The only relief comes in the form of an expensive legal proceeding—a motion in court or a petition to the FTC—that a company under the orders must commence. The burdens to do so are high. Respondents face serious obstacles when they seek to modify or terminate Commission orders.¹⁶ As a result, the typical order will follow the company, and any other company that subsequently acquires it, for twenty years—or forever.

The Commission’s insistence on twenty-year orders and permanent decrees stands in contrast to the practice of other agencies. The Antitrust Division of the Department of Justice traditionally has included ten-year terms in its civil orders, and now sometimes limits them to five years.¹⁷ Indeed, the Commission’s practice is inconsistent with its own application of the Regulatory Flexibility Act (or RFA), in which the agency reviews its guides and regulations every ten years.¹⁸ A bipartisan Congressional mandate, the RFA has been a hallmark of responsible Federal regulation for four decades. The purpose of the statute was stated eloquently by Acting Chairman Maureen Ohlhausen this year, “Regulations can be important tools in protecting consumers, but when they are outdated, excessive, or unnecessary, they can create significant burdens on the U.S. economy, with little benefit.”¹⁹ Unfortunately, regulations that come in the form of FTC orders and decrees are not included in RFA reviews, and these regulations now count in the thousands, amounting to tens of thousands of pages of specific requirements that can handicap a competitor. The mandates continue to accumulate with little or no examination after their temporary reporting obligations are entered. There is no plan to revisit whether the orders’ benefits justify their costs. It is time for the Commission to follow the lead of the Antitrust Division and other agencies that sunset such burdens.

DIVINING THE MEANING OF MESSAGES AND THE NEED FOR DISCLOSURES

The agencies have pursued failure to disclose theories and imposed “clear and conspicuous” disclosure requirements with increasing vigor in recent years. This has created considerable uncertainty for businesses in determining what information is sufficiently important (*e.g.*, material and necessary to prevent unfairness or deception) that it must be disclosed and where the disclosures must appear (*e.g.*, in advertising or at point of sale). The different opinions on claim interpretation and disclosure clarity at the Commission in POM Wonderful were not reconciled in the decision of the D.C. Circuit, leaving additional uncertainty as to whether and what kind of substantiation is needed for a claim, what claims trigger a disclosure, and how much information should be disclosed.²⁰

¹⁴ Report at 30, n. 93.

¹⁵ *Id.*

¹⁶ *Id.* at 31.

¹⁷ *See, e.g.*, U.S. v. Ebay, Case No. 12–CV–05869–EJD–PSG (2014), available at <https://www.justice.gov/atr/case-document/file/494626/download>.

¹⁸ *See, e.g.*, FTC, Regulatory Review Schedule, 82 Fed Reg 29259 (June 28, 2017) (To ensure that its rules and industry guides remain relevant and are not unduly burdensome, the Commission reviews them on a ten-year schedule. Each year the Commission publishes its review schedule, with adjustments made in response to public input, changes in the marketplace, and resource demands.)

¹⁹ FTC, Release, FTC Announces Regulatory Reform Measures Ranging from TVs and Textiles to Energy Labels and E-mail (June 28, 2017), available at <https://www.ftc.gov/news-events/press-releases/2017/06/ftc-announces-regulatory-reform-measures-ranging-tvs-textiles>.

²⁰ Report at 33–34, citing POM Wonderful v. Federal Trade Commission, 777 F.3d 478 (D.C. Cir. 2015).

What does an advertisement communicate? How much information must an advertisement disclose to prevent deception or injury? How should the medium in which an ad appears affect disclosures? These are questions that have preoccupied advertising authorities for decades, and the answers are more elusive today than they were when TV, radio, and print delivered most ads. As long ago as 1992, the Seventh Circuit Court of Appeals encouraged the Commission to explain how it interpreted advertisements.²¹ As recently as *POM Wonderful*, the Commission was divided on which ads were deceptive. When the agency is unsure after years of investigation and adjudication, advertisers are hard-pressed to predict with confidence what they can say without running afoul of the law.

As the Task Force noted, “Especially in the case of short-form broadcast advertising, there simply is not sufficient space to include all of the information the agencies have deemed necessary in forms of advertising.”²² It is important that regulators demonstrate the need for additional or qualifying information, since the cost of the qualification could be the loss of other information or the loss of the advertisement itself. This is not just responsible regulation, but a constitutional mandate. As the courts regularly remind us, the First Amendment recognizes the value of commercial information and requires regulators to strike the right balance between burdens and benefits of communications.²³ Moreover, in any medium, increasing the amount of information that must be disclosed can obscure the most important messages, thus creating a tension with the “clear and conspicuous” objectives of the disclosure.

Not surprisingly, the Task Force also noted uncertainty among advertisers as to how the Commission would apply the “clear and conspicuous” standard in particular fact situations, and recommended that the agency look for additional opportunities to clarify its expectations in guidance and to give businesses an opportunity to come into compliance before the agencies start bringing enforcement actions. Citing cases in which the Commission pursued auto dealers for failure to disclose terms and conditions of their offers, and suggesting the Commission could have offered more warning of the policy it would pursue, the Report recommended an exploration of each element of disclosure policy—from the representation that could trigger a disclosure to the clarity and prominence of the disclosure—and how those factors vary across media.²⁴

A laudable example of the Commission’s efforts to tailor its guidance to the advance of technology can be found in the Online Disclosure Guidelines (often called the Dot Com Disclosures) in which the agency has acknowledged that smaller screens can justify shorter disclosures. Nonetheless, the latest revision of the guidance contained an ominous warning:

If a disclosure is needed to prevent an online ad claim from being deceptive or unfair, it must be clear and conspicuous. Under the new guidance, this means advertisers should ensure that the disclosure is clear and conspicuous on all devices and platforms that consumers may use to view the ad. The new guidance also explains that if an advertisement without a disclosure would be deceptive or unfair, or would otherwise violate a Commission rule, and the disclosure cannot be made clearly and conspicuously on a device or platform, then that device or platform should not be used.

The consequence the Commission contemplates for a disclosure that does not fit—disqualifying a medium for a message—emphasizes the importance of determining whether a disclosure is necessary in the first place (and if so how much is necessary) to cure deception, avoid unfairness, or comply with a rule. If a disclosure mandated for other media would fill an entire screen of a smartphone, it is worth asking whether all the required language is necessary to cure deception. That is what the Commission does when it investigates advertising restraints that trade associations and professional societies adopt. If a restraint is not necessary to cure deception or avoid injury, then the agency may prosecute it as an antitrust violation.²⁵ The Commission has traditionally taken a dim view of private restrictions based on speculative harm. Under Section 5 of the FTC Act, deception depends on a represen-

²¹ *Kraft, Inc. v. Federal Trade Commission*, 970 F.2d 311 (7th Cir. 1992)

²² *Id.*

²³ *See, e.g., AM. BEVERAGE ASS’N V. CITY & CTY. OF SAN FRANCISCO*, No. 16–16073 (9th Cir., Sept. 19, 2017) available at <http://cdn.ca9.uscourts.gov/datastore/opinions/2017/09/19/16-16072.pdf>.

²⁴ Report at 35.

²⁵ *See, e.g., Release, Professional Associations Settle FTC Charges by Eliminating Rules That Restricted Competition Among Their Members*, (December 16, 2013), available at <https://www.ftc.gov/news-events/press-releases/2013/12/professional-associations-settle-ftc-charges-eliminating-rules>.

tation or omission, likely to mislead reasonable consumers, to their detriment,²⁶ and unfairness turns on the threat of substantial injury, not reasonably avoidable by consumers and not outweighed by benefits to consumers or competition.²⁷ Whether imposed by cases, guides or self-regulation, a thorough examination of an advertising restraint advances the mission of the Commission. The same analysis of a regulation or other mandate addresses the requirements in the First Amendment of the Constitution.²⁸

INCONSISTENT RULES UNDERMINE CONSUMER PROTECTION

This Report notes numerous initiatives of the FTC . . . that have enhanced protection of the Nation’s consumers. However, the overlapping jurisdictions of the FTC [and other agencies] give rise to risks of inconsistent regulatory approaches that cause confusion and complicate compliance, particularly with respect to privacy protection. Such inconsistencies could undermine the objectives the Agencies seek to advance.²⁹

It is inevitable in an economy as complex as ours that companies will face multiple regulatory agencies, and that the standards those agencies apply to the same conduct will differ. Those differences can stifle economic activity and diminish consumer protection. The examples cited in the Report deal with approaches to privacy and definitions of unfair and abusive conduct. Inconsistent approaches to privacy have contributed not only to inconsistent standards that companies must try to follow, but also gaps in coverage that could leave loopholes for sectors of the economy without Federal regulation at all. Such a prospect loomed when the Federal Communication Commission adopted its 2015 Open Internet Order and reclassified the provision of Internet broadband access as a “telecommunications service” under Title II of the Telecommunications Act. The Order would have deprived the FTC of jurisdiction over Internet Service Providers, potentially even for conduct that would not have been subject to FCC regulation.³⁰ The discordant policies had international repercussions. As the Task Force observed:

Based in part on its negative perception of the U.S. sectoral approach to privacy, the European Court of Justice issued a decision in 2015 finding that the EU-U.S. Safe Harbor insufficiently protected EU residents’ personal data. . . . Reducing the ability for U.S. companies to transfer personal data effectively and appropriately could impact the U.S.’s competitive posture. Although the Section is not advocating for an umbrella privacy law at this time, it does observe that the inconsistent privacy approaches pose a risk of harm to U.S. companies and competition internationally. More consistency among the regulatory approaches would likely yield reduced compliance costs and promote competitiveness with resulting benefit to consumers.

History provides many examples of unintended consequences of regulations. The lawyers and economists at the FTC have long performed a valuable public service by calling attention to regulatory policies that may be at odds with the interests of consumers and competition. Indeed, the Commission has dedicated a staff, in the Office of Policy Planning, to the advocacy of reasonable regulation in the United States. Over the years, the Commission has brought attention to the value of nutritional claims on labels of foods,³¹ consumer-friendly disclosures on financial docu-

²⁶ Fed. Trade Comm’n, FTC Policy Statement on Deception (Oct. 14, 1983), available at https://www.ftc.gov/system/files/documents/public_statements/410531/831014deceptionstmt.pdf.

²⁷ Fed. Trade Comm’n, FTC Policy Statement on Unfairness (Dec. 17, 1980), available at <https://www.ftc.gov/public-statements/1980/12/ftc-policy-statement-unfairness>, codified at 15 U.S.C. § 45(n).

²⁸ See generally, William MacLeod, Elizabeth Brunins & Anna Kertesz, Three Rules and a Constitution: Consumer Protection Finds Its Limits in Competition Policy, 72 Antitrust L.J. 943 (2005).

²⁹ Report at 3.

³⁰ Report at 25.

³¹ See, e.g., Comments of the Staff of the Bureau of Consumer Protection, the Bureau of Economics and the Office of Policy Planning of the Federal Trade Commission In FDA’s Request for Comments on Nutrient Content Claims (July 27, 2004), available at https://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-staff-comment-food-and-drug-administration-concerning-nutrient-claims/v040020.pdf.

ments,³² and unnecessary restrictions in professions and trades.³³ It is important that the Commission continue this advocacy, and that agencies consider whether their policies conflict with other regulations that impose duties on businesses. A company that answers to multiple authorities, and which cannot satisfy one without offending another, is tempted to abandon the activity rather than risk prosecution. Consumers deprived of the goods and services that the company would have offered under a coordinated regulatory policy could suffer the type of injury that competition and consumer protection agencies try to prevent.

PROGRESS ON TRANSPARENCY

The Section recommends that the FTC adopt a number of reforms to help it deploy its limited enforcement resources in a manner that enhances the impact of its actions while, at the same time, treating target companies in a way that is fair and proportionate to the alleged offenses.³⁴

At the outset of this testimony, I noted a 1969 ABA Report that was credited for sound suggestions on the future of FTC enforcement. The Commission heeded many of those suggestions and improved its protection of consumers as a result. I am gratified to see the current Commission taking the recommendations of our Task Force to heart. This spring, Acting Chairman Ohlhausen announced the formation of internal working groups to implement process reforms at the agency. The Commission revealed the first results of those efforts in July:

The process reforms announced today address CIDs (Civil Investigative Demands) in consumer protection cases, and include:

- Providing plain language descriptions of the CID process and developing business education materials to help small businesses understand how to comply;
- Adding more detailed descriptions of the scope and purpose of investigations to give companies a better understanding of the information the agency seeks;
- Where appropriate, limiting the relevant time periods to minimize undue burden on companies;
- Where appropriate, significantly reducing the length and complexity of CID instructions for providing electronically stored data; and
- Where appropriate, increasing response times for CIDs (for example, often 21 days to 30 days for targets, and 14 days to 21 days for third parties) to improve the quality and timeliness of compliance by recipients.³⁵

I look forward to the FTC building on this progress and adopting more of the recommendations in the Task Force's Report.

And of course, I would be happy to answer any questions the Committee might have.

Senator MORAN. Thank you very much.

Ms. Parnes.

STATEMENT OF LYDIA PARNES, ESQ., PARTNER, WILSON SONSINI GOODRICH & ROSATI PC

Ms. PARNES. Thank you, Chairman Moran, Ranking Member Blumenthal, distinguished members of the Committee.

My name is Lydia Parnes. As you mentioned, I am currently a partner at Wilson Sonsini Goodrich & Rosati. Before that, I had the very clear privilege of working at the FTC for over 27 years, and served as Director of the FTC's Bureau of Consumer Protection for

³² See, e.g., Lacko & Pappalardo, Improving Consumer Mortgage Disclosures/Bureau of Economics Staff Report, June 2007, available at <https://www.ftc.gov/sites/default/files/attachments/educational-materials/p025505mortgagedisclosurereport.pdf>.

³³ See, e.g., Ohlhausen, "Advancing Economic Liberty," Remarks at the George Mason Law Review's 20th Annual Antitrust Symposium, February 23, 2017, available at https://www.ftc.gov/system/files/documents/public_statements/1098513/ohlhausen_-_advancing_economic_liberty_2-23-17.pdf

³⁴ Report at 27.

³⁵ Release, Acting FTC Chairman Ohlhausen Announces Internal Process Reforms: Reducing Burdens and Improving Transparency in Agency Investigations, July 17, 2017, available at <https://www.ftc.gov/news-events/press-releases/2017/07/acting-ftc-chairman-ohlhausen-announces-internal-process-reforms>

my last 5. Thank you so much for inviting me here today to present testimony on FTC reform proposals.

The views that I express in my written and oral testimony reflect recommendations of the ABA Antitrust Section's Presidential Task Force Report as well as my own personal views.

Last year, I was a member of that task force that prepared the report, an impressive bipartisan group of lawyers, professors, economists, and a Federal appellate court judge, all with very deep FTC experience. The report sets out the Section's recommendations on how to enhance consumer protection enforcement efforts, and I want to underscore what the Section recognizes.

The FTC is a highly respected and effective agency, and for decades has engaged in vigorous law enforcement activities to protect consumers and halt unfair or deceptive acts and practices. Of course, there is always room for improvement. And I'd like to focus my remarks on two of the areas where the task force made process improvement recommendations, improving the use of CIDs and clarifying the FTC's legal basis for seeking monetary relief.

CIDs, essentially administrative subpoenas, are an important part of an FTC investigation, but responding to a CID can be exceptionally costly, burdensome, and confusing. Companies also have very limited means to narrow the scope of a CID, which is often overly broad. It is true that the FTC staff will typically negotiate at least some of these terms, but if the staff does not willingly agree to modifications, the company faces a dilemma: It can file a petition to quash or limit the CID, but these petitions are made public, which imposes considerable reputational costs on companies, and for smaller companies, these costs can be existential.

Acting Chairman Ohlhausen recently acknowledged these and other procedural issues, and this summer announced CID reforms responsive to the Section's recommendations. I would urge the Subcommittee and the Commission to consider steps to make these reforms permanent and to address other issues raised in the report, such as by permitting companies to file confidential petitions to challenge overly broad CIDs.

Let me turn next to monetary relief. In recent years, the FTC has sought significant monetary relief in cases that don't involve fraud or other tangible consumer injury. This marks a departure from the agency's prior practices where it sought restitution for injured consumers or disgorgement of ill-gotten gains that were traceable to the violations at issue.

For example, earlier this year, the FTC entered into a settlement agreement with Vizio over claims that the company's smart TVs were collecting television viewing data without the informed consent of customers. The settlement included injunctive provisions that you would expect in an order like this, but on top of the injunctive provisions, Vizio was required to pay \$1.5 million to the Commission with no explanation offered as to the basis for that monetary relief.

Congress gave the FTC broad consumer protection authority, but more limited authority to obtain money. But the FTC's current approach to monetary relief seems to push the limits of this authority. To address this issue, the Section recommends, first, that the FTC tie monetary relief more closely to the nature of the violation,

the extent of consumer injury, and the culpability of the defendant; and, second, that the FTC issue a policy statement setting forth the theories on which it relies to justify its demands for money. These recommendations appropriately reflect the intent of the FTC Act while also providing greater clarity and transparency.

I very much appreciate your time and will be happy to answer questions.

[The prepared statement of Ms. Parnes follows:]

PREPARED STATEMENT OF LYDIA PARNES, ESQ., PARTNER,
WILSON SONSINI GOODRICH & ROSATI PC

Introduction

Mr. Chairman and Members of the Subcommittee: thank you for the opportunity to present testimony on FTC reform proposals. My name is Lydia Parnes and I am currently a Partner at Wilson Sonsini Goodrich & Rosati. Prior to that, I was the Director of the Bureau of Consumer Protection (BCP) at the Federal Trade Commission (FTC or Commission).

Earlier this year, the Section of Antitrust Law of the American Bar Association (the Section) submitted its Presidential Transition Report.¹ I am attaching a copy of this report along with my written testimony.² The Section's Presidential Transition Task Force was responsible for compiling this report and was comprised of a bi-partisan group of lawyers, professors, economists, and a Federal appellate court judge with deep knowledge of, and extensive work with, the relevant issues and agencies. In fact, over half of the task force members have served in a senior leadership position with either the Commission or the Antitrust Division of the Department of Justice. As a member of this task force, I saw firsthand just how significantly the team's diverse backgrounds and experiences contributed to the crafting of this report.

This report presents the Section's views on the current state of Federal consumer protection enforcement, as well as its recommendations regarding how the new administration could enhance that enforcement. As the Section recognizes, the FTC is a highly respected agency and, over the last several decades, its vigorous efforts in the area of consumer protection have been effective in protecting consumers and in halting unfair or deceptive acts or practices. The Section's thoughtful recommendations would build upon the FTC's excellent work to further refine the FTC's practices and processes. These recommendations are based on the task force's comprehensive experience with the agencies—and with subjects of FTC investigations—to pinpoint areas of concern and to identify practical means for improving results. These are important recommendations that deserve serious consideration.

Today I will highlight four specific areas where the task force made recommendations: (1) case selection; (2) civil investigative demands (CIDs); (3) information sharing in investigations; and (4) order provisions.

I. Case Selection

The FTC has broad prosecutorial discretion to select subjects for its enforcement actions—including which subjects to initially investigate and, subsequently, whether to bring a case or to close that investigation. As the Section notes, the FTC also has limited resources to conduct such investigations and litigations. Accordingly, the Section recommends the FTC focus its efforts on cases where significant consumer harm exists. While the Commission does bring many important cases involving serious consumer harm, the Section notes that, at times, the agency has also prosecuted small companies for technical violations where consumer harm was not apparent.³

¹American Bar Association, Section of Antitrust Law, Presidential Transition Report: The State of Antitrust Enforcement (January 2017), https://www.americanbar.org/content/dam/aba/publications/antitrust_law/state_of_antitrust_enforcement.authcheckdam.pdf [hereinafter Section Presidential Transition Report].

²As stated in the report, the views of the task force members were provided in their individual capacities and should not be attributed, in any way, to their law firms, clients or academic institutions, as applicable. See Section Presidential Transition Report, *supra* note 1, at 1 n.1. This written testimony sets out the Task Force recommendations as well as my own personal views.

³The report mentions *In the matter of Nomi Techs., Inc.*, Docket No. C-4538, 2015 WL 5304114 (F.T.C. Aug. 28, 2015), where dissenting Commissioners Ohlhausen and Wright criticized the majority's decision to bring the case given the technical nature of the violations and the absence of evidence of actual consumer harm. See *id.* at *5, *8.

Such cases appear to underutilize the FTC's valuable assets, given the lack of meaningful consumer harm. They can also have extreme negative effects on small businesses that have more limited resources with which to respond to and defend such enforcement actions and may, as a result of such actions, lose the financing, customers, and business relationships they depend upon for their continued viability.

II. Civil Investigative Demands (CIDs)

A typical FTC investigation begins with the issuance of a civil investigative demand (CID), which compels the subject to submit written responses, documents, and other information and materials to the Commission. CIDs are an important component of the FTC's investigative process. Responding to a CID, however, can be exceptionally costly and burdensome to a company under investigation. The Section thus recommends the Commission act more judiciously in crafting and issuing CIDs to companies and individuals to avoid imposing unnecessary costs. Specifically, the Section suggests the Commission issue more narrowly focused initial CIDs, leaving open the option to issue follow up CIDs if needed.

These recommendations are largely a response to the Commission's tendency to issue overly-broad CIDs, which are not tailored to the company or conduct under investigation. While the Commission needs some leeway in composing CIDs to ensure the necessary information and materials are covered—particularly when the Commission is unfamiliar with how the company creates and stores its records—the Commission has tended to issue CIDs that go beyond merely affording the Commission this leeway and leave the subject both confused as to the potential theories being investigated and facing a substantial burden in terms of its response.⁴ In fact, the legal fees alone, which subjects incur to negotiate scope with the Commission and then to make the productions, can be prohibitive. These costs are compounded by strict production requirements the FTC often imposes. These requirements may vary significantly depending on how a subject stores its records in the ordinary course, and thus require the subject to retain an expensive vendor to make the required production.

The trend toward broader CIDs is also problematic because respondents have limited means to narrow the scope. If the Commission does not willingly agree to modifications, the respondent can file a petition to quash or limit a CID. But these petitions are made public, which imposes considerable reputational costs on the investigative targets. For smaller businesses, in particular, these reputational costs can be significant and even life-threatening.

Acting Chairman Maureen K. Ohlhausen recently acknowledged these (and other) procedural issues, and established new internal Working Groups on Agency Reform and Efficiency to investigate the causes of such issues and to identify potential solutions. This summer, the Commission announced process reforms concerning consumer protection CIDs, some of which seem directly to respond to the Section's recommendations.⁵ For instance, the reforms include “[a]dding more detailed descriptions of the scope and purpose of investigations to give companies a better understanding of the information the agency seeks,” and “[w]here appropriate, significantly reducing the length and complexity of CID instructions for providing electronically stored data.” Such procedural changes have the potential to significantly reduce the burden of responding to CIDs without negatively impacting the FTC's ability to obtain the necessary information. I would urge the Subcommittee and the Commission to consider steps to make these reforms permanent and to address other issues raised in the report, such as by permitting companies to file confidential petitions to challenge overly broad CIDs.

III. Information Sharing in Investigations

Information sharing is critical in Commission investigations. The information shared by a company being investigated helps the FTC to discern whether a violation has occurred. At the same time, if the FTC shares its concerns, the company can better understand what is being investigated and what information and defenses are relevant. The extent to which the FTC staff actually reveals its theories and concerns, however, varies significantly from case to case.

In cases where the staff engage in open discussions early on regarding what is investigating, there is more opportunity for both sides to explore the issues and

⁴As the Section explained, some CIDs demand all information that could potentially relate to violations of essentially every consumer protection law that could possibly apply. Section Presidential Transition Report, *supra* note 1, at 29 n.91.

⁵Press Release, U.S. Fed. Trade Comm'n, Acting FTC Chairman Ohlhausen Announces Internal Process Reforms: Reducing Burdens and Improving Transparency in Agency Investigations (July 17, 2017), <https://www.ftc.gov/news-events/press-releases/2017/07/acting-ftc-chairman-ohlhausen-announces-internal-process-reforms>.

test their theories. Open communication leads to sounder outcomes, as both sides have real opportunities to present evidence and see how that evidence does—or does not—align with the Commission’s theories of harm. On the flip side, in cases where the staff does not disclose its theories to the respondent or inform the respondent of what evidence allegedly supports its theories, the respondent is left at a serious disadvantage in defending its conduct. Moreover, this lack of information sharing can undermine the investigative process itself. If the respondent does not know what the Commission’s legal theory is, it cannot subject this theory to its best defenses. Thus, while the goal of the investigative process is to analyze the facts to understand whether a violation has occurred, not sharing the underlying theory and the evidence allegedly supporting it effectively short-circuits a thorough factual and legal analysis.

Creating open lines of communication begins with the CID’s issuance, as noted. The clearer the CID is regarding the Commission’s intent, the more responsive the subject can be from the outset. To this end, the Commission’s recent process reforms are likely to enhance information sharing efforts. But information sharing should not stop here. The FTC’s theories and concerns are likely to evolve as they receive more information. Keeping respondents informed of these changes is key to reaching thoughtful outcomes supported by the full set of evidence.

To improve communication between the Commission and parties in a consistent fashion, the Section recommends that the FTC adopt internal guidelines for staff to follow in communicating with respondents. The Section suggests that, beginning as early as possible, the staff should be as transparent as possible and encourage open dialogue regarding their substantive concerns (absent compelling circumstances suggesting otherwise, such as clear bad faith by the respondent). These recommendations would both improve the fairness of the process and help the Commission reach better supported decisions.

IV. Order Provisions

The terms the Commission includes in its consent orders are of critical importance. Realistically, a company may not have the resources or capacity to litigate, and—to a large extent—the Commission relies on consent orders to resolve investigations. Consent order terms that are unduly restrictive may do more harm than good and, compounding this problem, may gain the mantle of precedent over time, making appropriate modifications increasingly unlikely. As such, consent orders should be carefully crafted. The Section offers some specific proposals to assist in this effort.

First, the Section recommends reducing the burden of “boilerplate” provisions. The Commission has established a number of administrative provisions that it reuses in the same or substantially similar terms in each consent order. While this practice can expedite the negotiation process, inappropriately broad terms can impose unnecessary costs. For instance, since 1996 the Commission has required companies entering consent decrees to agree to administrative orders lasting 20 years and Federal court orders lasting in perpetuity.⁶ This practice does not account for the nature of the underlying market, nor for how quickly that market might be changing. Accordingly, it may unnecessarily constrain the company’s ability to react to competitive changes or consumer demands, particularly when coupled with the “fencing in” provisions and other burdensome affirmative obligations that the Commission routinely includes in consent orders.⁷ The Section therefore recommends the FTC adopt a sunset period of around 5 years for both administrative and district court orders, allowing upward deviation for extenuating circumstances such as fraud or recidivism.

⁶ See Press Release, U.S. Fed. Trade Comm’n, FTC Rule Incorporating Sunset Policy for Existing Administrative Orders in Consumer Protection and Antitrust Cases (Nov. 20, 1995), <https://www.ftc.gov/news-events/press-releases/1995/11/ftc-rule-incorporating-sunset-policy-existing-administrative>. The Commission justified keeping Federal court orders unlimited because “many of these orders are against defendants involved in hard-core fraud.” *Id.*

⁷ The FTC typically includes “fencing-in” relief in its consumer protection orders, which is relief that stretches beyond violations identified in the Commission’s complaint to reach allegedly related practices. For instance, in matters involving unsubstantiated claims regarding health benefits, the Commission typically imposes a term requiring scientific substantiation for any claim about the health benefits, efficacy, or performance of any food, drug, or dietary supplement. See e.g., *POM Wonderful v. FTC*, 777 F.3d 478, 505 (D.C. Cir. 2015). This often leaves the respondent with much confusion and uncertainty regarding which implied claims the Commission might find in future advertising or what substantiation it would find sufficient. Other burdensome affirmative obligations the FTC requires include, for data security matters, expensive biennial security audits. See e.g., *In the Matter of Snapchat, Inc.*, Docket No. C-4501, 2014 WL 1993567, at *14 (F.T.C. May 8, 2014).

Relatedly, the Section recommends the FTC reconsider its standard implementation of “Scofflaw” provisions, to alleviate their burdensome requirements for respondents operating legitimate businesses. Scofflaw provisions include requirements such as distributing the order to various individuals, keeping records, reporting changes (like asset sales, mergers, or bankruptcy), and filing compliance reports, that typically last between 3 and 20 years. Federal court boilerplate Scofflaw provisions often go beyond the Commission’s standard ones, including by providing the FTC the right to gather information from the respondent in various ways that can be very burdensome. Federal court orders, for instance, often allow the Commission to contact the respondent directly—not through counsel—regarding order-related matters, which contradicts longstanding ethical rules prohibiting such conduct.⁸ While such terms were originally intended to permit proper oversight when defendants behaved fraudulently, the FTC has increasingly filed cases in Federal court in non-fraud cases, but continued to incorporate these onerous terms. This practice imposes unnecessary costs on respondents and should be reconsidered.

Second, the Section recommends tying monetary relief more closely to critical issues including the nature of the violation, the extent of consumer injury, and the culpability of the respondent. In recent years, the Commission has increasingly sought significant monetary relief, including civil penalties, restitution, and/or disgorgement, in Section 5 cases that do not involve fraud or tangible consumer injury. This marks a departure from the Commission’s prior practices, in which it sought restitution or disgorgement tethered to injury or unjust enrichment that was traceable to the violation(s). More recently, the staff has sought monetary relief even when violations are marginal, technical, or unintentional and the injury is minimal or nonexistent—and it often seeks the maximum possible amount regardless of the underlying facts or litigation risks.

These changes to FTC practice inappropriately penalize respondents beyond what is necessary to deter the same or similar conduct. They also create unnecessary uncertainty, as the respondents cannot rely on *ex ante* calculations as to the costs of the conduct at issue to estimate likely fines. Consider, for instance, that the public perceives larger fines as indicative of more egregious conduct, and reasonably judges the respondent according to this perceived level of misconduct. By detaching fines from actual wrongdoing, the Commission creates a situation in which the public is judging a respondent more harshly—potentially significantly so—than is warranted. The Section’s recommendations would help realign the costs, both monetary and reputational, to the misconduct and harm identified. These recommendations, moreover, mirror the FTC’s prior statement on monetary relief, including disgorgement and restitution, in competition cases, which was unanimously adopted but is not in effect today.⁹

Conclusion

The Section’s Presidential Transition Report offers numerous recommendations for enhancing the FTC’s consumer protection enforcement processes and outcomes. These recommendations would alleviate unnecessary burdens on businesses while facilitating better FTC decisions and outcomes.

Thank you for your time. I would be happy to answer any questions.

Senator MORAN. Thank you for your testimony.

Ms. Rich.

⁸See AM. BAR ASS’N, MODEL RULES OF PROF’L CONDUCT, R. 4.2 (2014) (“In representing a client, a lawyer shall not communicate about the subject of the representation with a person the lawyer knows to be represented by another lawyer in the matter, unless the lawyer has the consent of the other lawyer or is authorized to do so by law or a court order.”).

⁹U.S. Fed. Trade Comm’n, Policy Statement on Monetary Equitable Remedies—Including in Particular Disgorgement and Restitution—in Federal Trade Commission Competition Cases Addressing Violations of the FTC Act, the Clayton Act, or the Hart-Scott-Rodino Act (July 31, 2003), <https://www.ftc.gov/public-statements/2003/07/policy-statement-monetary-equitable-remedies-including-particular>. This statement established, for instance, that the FTC would seek disgorgement only where (1) the underlying violation was clear, and (2) there was a reasonable basis for calculating the payment amount, and (3) it would take into account the other remedies available, including private actions and criminal proceedings. The FTC withdrew this statement less than 10 years after unanimously adopting it, finding it “overly restrictive.” Press Release, U.S. Fed. Trade Comm’n, FTC Withdraws Agency’s Policy Statement on Monetary Remedies in Competition Cases; Will Rely on Existing Law (July 31, 2012), <https://www.ftc.gov/news-events/press-releases/2012/07/ftc-withdraws-agencys-policy-statement-monetary-remedies>.

**STATEMENT OF JESSICA RICH, VICE PRESIDENT, CONSUMER
POLICY AND MOBILIZATION, CONSUMER REPORTS**

Ms. RICH. Chairman Moran, Ranking Member Blumenthal, and members of the Subcommittee, thank you for the opportunity to be here today on behalf of Consumer Reports and our Policy and Mobilization Division, Consumers Union, to discuss the important work of the Federal Trade Commission.

I arrived at Consumers Union in May of this year following 26, believe me, years in the FTC's Bureau of Consumer Protection, the last four as its Director. My tenure at the agency spanned several Democratic and Republican administrations, and I am equally proud of the work I did under all of them.

Consumers Union has always regarded the FTC as a leader in ensuring consumers are protected in the marketplace and that they have the accurate information needed to make informed choices. Every year, the FTC returns millions of dollars to consumers and saves billions more through its law enforcement efforts. Every year, it halts ongoing fraud and deception and helps legitimate companies that offer consumers valuable products and services compete on a level playing field. Every year, it educates the public through consumer and business education, public workshops, and policy reports, and it does so on a shoestring compared with the budgets of many other Federal agencies, and without many of the tools and remedies that other agencies routinely employ.

Notably, the FTC pursues its work as a bipartisan group of President-appointed and Senate-confirmed Commissioners. All cases, rulemakings, and other significant FTC actions require formal approval by a majority of them, and despite the occasional dissenting or concurring statement, virtually all decisions over the years have been unanimous.

In creating the FTC more than a century ago, Congress vested it with broad jurisdiction so it could address a wide range of unfair or deceptive practices across the marketplace. The breadth and flexibility inherent in the FTC Act has proven to be critical to the FTC's effectiveness. Who could have anticipated when the FTC Act was passed that there would be spyware, spam, massive data breaches, or tech support scams? It was 100 years ago. And who knew that cars would someday be able to drive themselves, or that your refrigerator or your children's toys would connect to a network of computers in your home, creating risk to personal data and documents you reasonably thought were secure?

But despite the breadth of the FTC Act, the agency's effectiveness is limited by certain restrictions on its authority. Notably, for historical reasons that no longer make sense, the FTC can't address unfair and deceptive practices by common carriers, creating an uneven playing field for businesses and consumers alike.

The FTC also has very limited rulemaking authority, and it can only seek penalties for law violations in very specific instances. I'm aware of various proposals that would change the way the FTC operates, some of which may be discussed here today.

Last year, as was mentioned, the House Energy and Commerce Committee considered proposals that would have altered the FTC's investigation and enforcement procedures. For example, one bill would have capped the length of FTC consent decrees to 8 years.

Another would have enacted select portions of the FTC's Unfairness Statement into law, which could limit the FTC's ability to address the wide range of harms in today's marketplace.

Earlier this year, the ABA Section of Antitrust Law also made some proposals, for example, echoing the call for shorter orders and recommending that the FTC lower the monetary relief it obtains in non-fraud cases. All of these recommendations would weaken an agency that already lacks authority and resources in critical areas at a time when consumers need the FTC's help the most.

Today, consumers face enormous challenges navigating the marketplace, making it harder than ever for them to avoid fraud, deception, and other harms. Every day, they encounter 24-hour data collection and advertising, phishing attempts, imposter scams, massive data breaches, highly sophisticated frauds, and confusion about who they can trust. In this environment, the FTC needs more authority to protect consumers, not less, including stronger laws to protect consumers' privacy and security, repeal of the common carrier exemption, strong remedies to hold wrongdoers accountable, and more resources.

My long-time experience at the FTC informs how the proposals under consideration would affect the agency's work, so I'm very pleased to have been invited here today to assist the Subcommittee in its deliberations. Consumers Union stands ready to assist staff in evaluating any recommendations that the Subcommittee believes may have merit.

Thanks again for the opportunity to testify.

[The prepared statement of Ms. Rich follows:]

PREPARED STATEMENT OF JESSICA RICH, VICE PRESIDENT, CONSUMER POLICY AND MOBILIZATION, CONSUMER REPORTS

Chairman Moran, Ranking Member Blumenthal, and Members of the Subcommittee, thank you for the opportunity to be here today on behalf of Consumer Reports and our policy and mobilization division, Consumers Union (hereinafter "Consumers Union"), to discuss the important work of the Federal Trade Commission.¹ Consumers Union has been a strong and longtime supporter of the FTC's work and mission.

I arrived at Consumers Union in May of this year. Before that, I spent 26 years working in the FTC's Bureau of Consumer Protection, the last four as its Director of Consumer Protection. My tenure at the FTC spanned several Democratic and Republican Administrations, and I am equally proud of the work I did under all of them. For me, moving to Consumer Reports, a strong, nonpartisan advocate for U.S. consumers, was a natural continuation of the work I have pursued throughout my professional life.

We—and I mean "we" at Consumers Union—have always regarded the FTC as a leader in ensuring that consumers are protected in the marketplace, and that they have the accurate information needed to make informed decisions. Every year, the FTC returns millions of dollars to consumers and saves billions more through its law enforcement efforts. Every year, it halts ongoing fraud and deception, and helps legitimate companies that offer consumers valuable products and services compete on a level playing field. Every year, it educates the public through consumer and business education, public workshops, and policy reports. And it does so on a shoe-

¹ Consumers Union is the policy and mobilization division of Consumer Reports. Consumers Union is an expert, independent, nonprofit organization whose mission is to work for a fair, just, and safe marketplace for all consumers and to empower consumers to protect themselves. Its work focuses on auto and product safety, financial services, healthcare, food safety, privacy and technology, and many other areas. Consumer Reports is the world's largest independent product-testing organization. Using its more than 50 labs, auto test center, and survey research center, the nonprofit organization rates thousands of products and services annually. Founded in 1936, Consumer Reports has over 7 million subscribers to its magazine, website, and other publications.

string, compared with the budgets of many other Federal agencies, and without many of the tools and remedies that other agencies routinely employ.

So that the FTC can continue to perform these important functions, the agency needs to be strong and independent, and have the resources and authority needed to pursue its vital mission. Indeed, given the enormous challenges that consumers face in today's marketplace, the FTC needs more authority—not less—to fulfill its fundamental consumer protection role.

Our support for the FTC in recent years has included efforts to strengthen its authority in a number of ways. To name just a few:

- We supported the FTC's implementation of the Do Not Call Registry, and its continuing work to protect consumers from the harassment of unwanted telemarketing calls.
- We supported the FTC's implementation of the Children's Online Privacy Protection Act, one of the seminal privacy laws passed in this country.
- We supported the clarification and strengthening of consumer disclosures required under the Used Car Rule.
- We supported the recently enacted Consumer Review Fairness Act, clarifying the FTC's authority to protect consumers against being forced to surrender their right to provide others with honest reviews about shoddy products, services, and treatment in the marketplace.
- We supported enactment of the Contact Lens Rule to ensure that consumers get their own copy of the prescription so they can shop around for their lenses, as well as the recent rulemakings to clarify that rule and its counterpart, the Eyeglass Rule.
- And right now, we are supporting efforts to preserve the FTC's authority to protect consumers from being victimized by deceptive pyramid schemes.

We also commend the FTC for the many law enforcement actions it has successfully pursued to obtain significant benefits for consumers. Some examples from the last few years include:

- *Cancer Fund of America* (halted fraudulent cancer charity that bilked over \$187 million from consumers).²
- *Western Union* (\$586 million to remedy long-standing use of money transfer system to facilitate fraud).³
- *T-Mobile and AT&T* (at least \$178 million for consumers who had unauthorized third party charges "crammed" onto their phone bills).⁴
- *Herbalife* (\$200 million for consumers who lost money in allegedly deceptive multi-level marketing operation, and significant reforms to company operations).⁵
- *Warner Bros.* (barring undisclosed payments to social media "influencers" for supposedly objective, positive product reviews).⁶
- *Craig Brittain* (ban on website operator who posted nude images of women online without their consent and tried to extract payment to remove them).⁷
- *AMG Services* (\$1.3 billion court judgment against fraudulent payday lending scheme that charged consumers multiple undisclosed and inflated fees).⁸
- *Ashley Madison* (\$1.6 million for alleged failure of online dating service to provide reasonable protections for highly sensitive personal data, and for posting fake member profiles to lure in new customers).⁹

² <https://www.ftc.gov/news-events/press-releases/2015/05/ftc-all-50-states-dc-charge-four-cancer-charities-bilking-over> (with State Attorneys General).

³ <https://www.ftc.gov/news-events/press-releases/2017/01/western-union-admits-anti-money-laundering-violations-settles> (with Department of Justice).

⁴ <https://www.ftc.gov/news-events/press-releases/2014/12/t-mobile-pay-least-90-million-including-full-consumer-refunds>; <https://www.ftc.gov/news-events/press-releases/2016/12/ftc-providing-over-88-million-refunds-att-customers-who-were> (with FCC and State Attorneys General).

⁵ <https://www.ftc.gov/news-events/press-releases/2016/07/herbalife-will-restructure-its-multi-level-marketing-operations>.

⁶ <https://www.ftc.gov/news-events/press-releases/2016/07/warner-bros-settles-ftc-charges-it-failed-adequately-disclose-it>.

⁷ <https://www.ftc.gov/news-events/press-releases/2015/01/website-operator-banned-revenge-porn-business-after-ftc-charges>.

⁸ <https://www.ftc.gov/news-events/press-releases/2016/10/us-court-finds-ftcs-favor-imposes-record-13-billion-judgment>.

⁹ <https://www.ftc.gov/news-events/press-releases/2016/12/operators-ashleymadisoncom-settle-ftc-state-charges-resulting> (with State Attorneys General).

- *Volkswagen* (over \$11 billion to consumers to remedy deceptive sales of cars marketed as “clean diesel,” but that contained secret software designed to evade pollution emissions tests).¹⁰

Notably, the FTC brought these actions—which address topics ranging from pyramid schemes and charity fraud, to phony reviews and data breaches—as a bipartisan group of President-appointed and Senate-confirmed Commissioners. These actions, like all significant FTC activity, required formal consideration and approval by a majority of Commissioners. And while concurring and dissenting statements in some FTC cases reveal that the Commissioners disagree on occasion, the vast majority of Commission votes over the years have been unanimous. For example, when Commissioner Joshua Wright ended his tenure at the FTC, he noted that he had dissented on approximately 4 percent of Commission votes, and issued a written dissent in just *half-a-percent* of consumer protection motions—all during a period in which he was in the minority.¹¹

In creating the FTC more than a century ago, Congress vested it with broad jurisdiction under the Federal Trade Commission Act so that it could reach “unfair or deceptive” practices wherever they occur. Congress deliberately provided the FTC with broad and flexible authority to ensure that it could address a wide range of practices across the marketplace,¹² and that has proven to be a wise decision. The FTC is the only “general purpose” consumer protection agency at the Federal level, so it plays a critical role in promoting fairness and truthfulness across many industry sectors. In addition, companies introduce many new products, services, and features into the marketplace every day, but this progress and growth has also created new opportunities for scams and harms that once would have been unimaginable.

Who could have anticipated in 1914, when the FTC Act was passed, that there would be spyware, spam, massive data breaches, or tech support scams? And who knew that cars would someday be able to drive themselves, or that your refrigerator or your children’s toys would connect to a network of computers in your home, creating risks to personal data and documents that consumers reasonably believe they are storing safely?

The flexibility in the FTC Act also enables the agency to protect, not just individual consumers, but also small businesses that have been preyed upon by other companies peddling fraudulent business services.¹³

But despite the breadth of the FTC Act, the agency’s effectiveness is limited by certain restrictions on its authority. Notably, for historical reasons that no longer make sense, the FTC lacks authority to address unfair or deceptive practices by “common carriers” and nonprofit entities. It has very limited rulemaking authority. And it can only seek penalties for law violations in very specific instances.

In my experience, the FTC is very careful about how it pursues its mission and how it treats all affected parties. The FTC’s Commissioners and staff take great pride in being fair and evenhanded and, given the agency’s relatively small size, have no choice but to focus the FTC’s resources strategically and deliberately. The agency also takes appropriate care not to interfere with or disrupt legitimate business activity. This care is taken not only at the Commissioner level, but throughout the decision-making process in the Bureaus.

For example, many companies are given an opportunity to negotiate a consent order prior to the staff recommending an enforcement action to the Commission. If a company chooses not to enter into a consent, it has the opportunity to meet with the Director of the Bureau of Consumer Protection and, subsequently, all of the Commissioners prior to any decision about whether to issue a complaint.

In addition, to assist companies seeking to comply with the law, the Commission provides online business guidance on a wide range of topics, including data secu-

¹⁰ <https://www.ftc.gov/news-events/press-releases/2017/05/federal-judge-approves-ftc-order-owners-certain-volkswagen-audi> (with Department of Justice and State of California).

¹¹ <https://twitter.com/ProfWrightGMU/status/634778695727755264>.

¹² See, e.g., *FTC v. Sperry & Hutchinson Trading Stamp Co.*, 405 U.S. 233, 240 (1972), quoting Senate Report No. 597, 63d Cong., 2d Sess., (1914), p. 13: “The committee gave careful consideration to the question as to whether it would attempt to define the many and variable unfair practices which prevail in commerce and to forbid their continuance or whether it would, by a general declaration condemning unfair practices, leave it to the Commission to determine what practices were unfair. It concluded that the latter course would be the better, for the reason, as stated by one of the representatives of the Illinois Manufacturers’ Association, that there were too many unfair practices to define, and, after writing 20 of them into the law, it would be quite possible to invent others. . . .”).

¹³ See <https://www.ftc.gov/about-ftc/bureaus-offices/bureau-consumer-protection/small-business>.

rity,¹⁴ endorsements and testimonials,¹⁵ environmental claims,¹⁶ jewelry claims,¹⁷ native advertising,¹⁸ and how to make clear and conspicuous online disclosures.¹⁹

The Commission also regularly holds public workshops, enlisting a range of stakeholders from the industry, advocacy, academic, and tech communities to discuss emerging issues and possible solutions.²⁰ And the FTC employs dozens of economists in its Bureau of Economics, whose role is to consider the effects of potential Commission actions on consumers, businesses, and the marketplace as a whole, and to advise the Bureau and the Commission on whether to take such actions.

In addition, the FTC recently created an Office of Technology Research and Investigations, and has appointed a series of Chief Technologists, to ensure that the Commission thoroughly understands new and emerging technologies as it seeks to address consumer protection issues in our increasingly connected world.

Understandably, individuals and companies may not like being the focus of an investigation, even in those instances when the investigation is ultimately closed without Commission action. However, in my experience, the FTC's actions are appropriately measured, well-considered, and grounded in the law and in the FTC's fundamental mission to protect U.S. consumers. Some in the consumer advocacy community, including my organization, have at times wished that the FTC could and would do more.²¹ Nevertheless, we consider the agency one of our champions.

Thanks to the FTC, and to Congress' wisdom in establishing it, consumers enjoy a far more fair, dependable, and consumer-friendly marketplace than otherwise would exist. Moreover, businesses operating fairly and honestly are rewarded with a more level playing field, where bad actors cannot count on getting away with and profiting off of their illegal activity.

We appreciate the interest in the FTC that this Subcommittee is taking as part of its oversight responsibilities. I am aware of a number of proposals that have been put forward to change the way the FTC operates, some of which may be discussed here today.

We wrote letters to the House Energy and Commerce Committee last year expressing concern about a number of proposals being considered there that would have altered, restricted, or encumbered the FTC's investigation and enforcement procedures.²² Those letters were sent before I arrived, but I agree with the concerns they raise. While some of the Committee's proposals would have strengthened the FTC's ability to protect consumers—and indeed, a couple of them were ultimately signed into law²³—some would have severely hampered the FTC's ability to protect consumers in today's exciting, but highly challenging consumer marketplace.²⁴

I am also aware that this Subcommittee is reviewing January 2017 recommendations from the American Bar Association (ABA) Section of Antitrust Law, some of which address processes and practices related to the FTC's consumer protection mission. While we share the goals of the ABA and this Subcommittee to ensure fairness, balance, and transparency in the FTC's operations, we do not support a number of the recommendations as currently framed. Some of them would limit the FTC's effectiveness in protecting consumers, which remains—and should always remain—the paramount mission of the FTC. And some appear to rely on single anecdotes that do not reflect my longtime experience at the FTC.

¹⁴ <https://www.ftc.gov/tips-advice/business-center/guidance/start-security-guide-business>.

¹⁵ <https://www.ftc.gov/news-events/media-resources/truth-advertising/advertisement-endorsements>.

¹⁶ <https://www.ftc.gov/news-events/media-resources/truth-advertising/green-guides>.

¹⁷ <https://www.ftc.gov/news-events/media-resources/tools-consumers/jewelry-guides>.

¹⁸ <https://www.ftc.gov/tips-advice/business-center/guidance/native-advertising-guide-businesses>.

¹⁹ <https://www.ftc.gov/news-events/press-releases/2013/03/ftc-staff-revises-online-advertising-disclosure-guidelines>.

²⁰ <https://www.ftc.gov/news-events/audio-video/ftc-events/workshops>. Recent topics include military consumers, connected cars, identity theft, artificial intelligence and blockchain technologies, drones, ransomware, charity fraud, and new technologies and research affecting privacy ("PrivacyCon").

²¹ <https://consumersunion.org/research/joint-comments-to-the-ftc-on-proposed-settlements-with-used-car-dealers-under-the-carmax-asbury-and-west-herr-brands-about-recalled-cars-advertised-as-safe/> (FTC should do more to stop dealer deception regarding cars with open recalls).

²² <https://consumersunion.org/research/consumers-union-and-partners-urge-u-s-house-committee-in-letter-to-protect-the-ftc/>.

²³ See Consumer Review Fairness Act of 2016, <https://www.congress.gov/bill/114th-congress/house-bill/5111>; BOTS Act of 2016, <https://www.congress.gov/bill/114th-congress/senate-bill/3183>.

²⁴ For example, we opposed the proposal to cap the length of FTC consent decrees to eight years, and to require the FTC to justify continuing non-fraud decrees for more than five years, because such requirements would undermine the FTC's ability to prevent repeat offenses.

Consumers face enormous challenges navigating today's marketplace, making it harder than ever to avoid fraud, deception, and other harms. Every day, they face 24-hour data collection and advertising, phishing attempts, imposter scams, massive data breaches, highly sophisticated frauds, and confusion about who they can trust. In this environment, the FTC needs more authority to protect consumers, not less, including stronger tools to protect consumers from privacy and security threats; broader jurisdiction over common carriers and other entities currently shielded from liability; stronger remedies to hold wrongdoers accountable; and greater resources to address consumer harms across the entire marketplace.

Because my first-hand experience at the FTC informs how the many proposals under consideration would affect the FTC's work, I am pleased to have been invited here today to assist the Subcommittee in its deliberations. Although the FTC is not perfect, my experience is that it employs procedures appropriate to its responsibilities, that it uses them fairly and evenhandedly, and that it pursues its mission with dedication, even as it observes the limits of its authority. I and my colleagues at Consumers Union stand ready to assist this Subcommittee in evaluating these proposals, and to take a careful look at any other recommendations that the Subcommittee believes may have merit.

Thank you again for the opportunity to testify.

Senator MORAN. Thank you very much.
Mr. Szóka.

STATEMENT OF BERIN SZÓKA, PRESIDENT, TECHFREEDOM

Mr. SZÓKA. Chairman Moran, Ranking Member Blumenthal, thank you for inviting me here today. As the only person sitting at this table who has not been a Director of the Bureau of Consumer Protection, I hope I can at least offer an outside perspective.

I have been studying how the FTC works for nearly a decade, since leaving the private practice of law, and have co-chaired the FTC Technology and Reform Project, an independent and scholarly effort launched in 2013 to study how the Federal Trade Commission operates. And I've been referring to the FTC for years now as the "Federal Technology Commission." The name seems to have stuck; even the former chairwoman has embraced it. It's not necessarily good or bad, it's just a convenient shorthand for an important truth, which is that more than any other government agency in the world, the FTC wrestles with a wide range of questions about how to protect consumers as technology changes without strangling or stifling innovation.

But as I said in my testimony to this Committee in 2012, what the FTC calls its common law of settlements in privacy and data security lacks the two key elements of real common law. First is the analytical rigor that comes with adversarial litigation. Two sides argue their case before a neutral, independent judge, and then that judge delivers a written and binding decision premised on carefully reasoned analysis of the law. Second is that that decision, those decisions over time, provide clear and authoritative precedent. Antitrust law offers a fine example of how the FTC can be effective, indeed, often very aggressive, in protecting consumers without also being the judge, jury, and executioner, as it effectively is today.

There is no reason that consumer protection laws should be inconsistent with the fundamentals of the rule of law. I think the FTC's Bureau of Consumer Protection can and should work more like its Bureau of Competition. I summarize reforms I think Congress should consider in my written testimony and provide more

detail in the attached testimony I coauthored for last year's hearing in the House on FTC reform.

I would break down FTC reform into seven broad categories. First, ensuring the FTC has the jurisdiction it needs, especially over the non-common carrier services provided by common carriers. Second, further codifying the Unfairness Policy Statement to ensure that the FTC's assessment of unreasonableness, including data security, satisfies the cost-benefit test that Congress codified in 1994. Third, codifying and further clarifying the 1983 Deception Policy Statement, especially to ensure that the FTC uses that power to focus on claims that are actually material to consumers. Fourth, to increase the role of economists in investigations, complaints, settlements, reports, and rulemaking. Fifth, to increase the role of Commissioners in overseeing what the Chairman and the staff do. Sixth, to remove disincentives against litigation so that courts will play more of a role in shaping consumer protection law. And, finally, encouraging or requiring the FTC to provide clearer and more empirically grounded guidance as to what the law means. And these last two reforms are really the crucial parts.

Perhaps the greatest reason that companies have settled essentially all data security and privacy cases is, as Lydia notes, reputational cost. Consider Equifax's recent data breach. Its stock dropped 30 percent, and just today its CEO has resigned. That is the reputational market at work. And that's a good thing, but it's also something the FTC has effectively leveraged. It has used that fact to essentially coerce settlements with companies by strong-arming them through the very, very burdensome and costly investigative process, threatening to go public, or through the administrative enforcement process that they have to endure before getting into a Federal court.

I think Congress can modify both of these without hampering the FTC's ability to protect consumers, but that would mean requiring greater Commissioner oversight of investigations, as Lydia notes, keeping investigations confidential until a complaint is filed, filing most complaints in Federal court, and explaining charges with greater specificity.

So in the end, consumer protection law probably won't ever work quite like antitrust law. Courts will probably always play less of a role, but they should play some role. And regardless of what Congress does, the FTC itself must provide more and better guidance on how companies can comply with the law. This will avoid both arbitrary enforcement and also ensure that consumers are protected by good data security and fair privacy practices.

Since 2010, the FTC has issued a flurry of reports asserting what companies should do, but without really substantially analyzing why or how to strike the right balance. Acting Commissioner Ohlhausen should be commended for convening a workshop this December on how to define informational injuries. This is a golden opportunity for the FTC to take a more empirically grounded approach to data security and privacy, just as it did with environmental marketing claims through the Green Guides that the FTC has updated regularly since 1992.

Not since 1994 has Congress made significant reforms. Such course corrections should happen every 2 years, but that has not

happened since 1996. It's time for the FTC to be reauthorized and for this Committee to start looking into these procedural matters. And I suspect that how the Committee handles them, how the FTC handle them, will prove even more important in determining what consumer protection looks like in 2117 than any major enactments between now and then.

So I look forward to helping this Committee ensure the Federal Technology Commission remains focused on serving consumers in the century to come.

[The prepared statement of Mr. Szóka follows:]

PREPARED STATEMENT OF BERIN SZÓKA¹ AND GRAHAM OWENS,² TECHFREEDOM

TABLE OF CONTENTS

I. Introduction

Background of FTC Enforcement in the Digital Economy

II. Summary of Proposed Legislative Reforms

- A. The Common Carrier Exception
- B. More Economic Analysis
- C. Clarification of the FTC's Substantive Standards
- D. Clarifying the FTC's Pleading Standards
- E. Encouraging More Litigation to Engage the Courts in the Development of Section 5 Doctrine and Provide More Authoritative Guidance
- F. The Civil Investigative Demand Process
- G. Fencing-In Relief
- H. Closing Letters
- I. Re-opening Past Settlements

III. Reasonable Siblings: Background on Section 5 and Negligence

IV. Informational Injuries In Practice: Data Security & Privacy Enforcement to Date

V. The Green Guides as Model for Empirically Driven Guidance

- A. The Green Guides (1992–2012)
- B. What the Commission Said in 2012 about Modifying the Guides

VI. Eroding the Green Guides and their Empirical Approach

- A. Modification of the Green Guides by Policy Statement (2013)
- B. Modification of the Green Guides by Re-Opening Consent Decree (2017)
- C. Remember Concerns over Revocation of the Disgorgement Policy?
- D. What Re-Opening FTC Settlements Could Mean for Tech Companies

VII. Better Empirical Research & Investigations

- A. What the FTC Does Now
- B. The Paperwork Reduction Act

VIII. Pleading, Settlement and Merits Standards under Section 5

- A. Pleading & Complaint Standards
 - 1. Deception Cases
 - 2. Unfairness Cases
- B. Preponderance of the Evidence Standard

IX. Conclusion

¹ Berin Szóka is President of TechFreedom, a nonprofit, *nonpartisan* technology policy think tank. J.D. University of Virginia School of Law; B.A. Duke University. He can be reached at bszoka@techfreedom.org. With thanks to my dedicated legal staff at TechFreedom, and in particular Vinny Sidhu and Sunny Seon Kang.

² I. Graham Owens is a Legal Fellow with TechFreedom. J.D. George Washington University School of Law; B.A. University of Virginia. He can be reached at gowens@techfreedom.org.

I. Introduction

Over the last two decades, use of, and access to, the Internet has grown exponentially, connecting people and businesses and improving the human condition in ways never before imagined. In 2011, 71.7 percent of households reported accessing the Internet, a sharp increase from 18 percent in 1997 and 54.7 percent in 2003.³ This digital growth—from a network of computers that only a few consumers could reach, to a seemingly infinite marketplace of ideas accessible by almost all Americans—has benefited society beyond measure, affording consumers the ability to access information, purchase goods and services, and interact with each other almost instantaneously without having to leave the home.⁴

However, as use and benefits of the Internet has grown, so too has the collection of personal data and, consequently, cyber-attacks endeavoring to steal that data. Since 2013, the number of companies facing data breaches has steadily increased.⁵ In 2016, 52 percent of companies reported experiencing a breach—an increase from 49 percent in 2015—with 66 percent of those who experienced a breach reporting multiple breaches.⁶ Perhaps not surprisingly, not much has changed since 2000, where one report revealed that system penetration by outsiders grew by 30 percent from 1998 to 1999.⁷ Interestingly, despite immense improvements in companies' ability to anticipate and prevent cyber-attacks, some of the largest and most sophisticated companies in the world, including Sony, Target, eBay, and JPMorgan, continue to experience data breaches today,⁸ just as they did in 2000.⁹ In spite of these statistics, the United States currently has no comprehensive legal framework in which to inform companies of the best practices to both prevent or respond to cyber-attacks, as well as to ensure that they're acting responsibly in the eyes of the Government.¹⁰

Absent a comprehensive statutory framework, the Federal Trade Commission ("FTC" or "Commission") happily stepped in to police the vast number of data security and privacy practices not covered by the few Internet privacy and cyber security statutes enacted at the time. For two decades, the FTC has grappled with the consumer protection issues raised by the Digital Revolution. Armed with vast jurisdiction and broad discretion to decide what is unfair and deceptive, the agency has dealt with everything from privacy to data security, from online purchases to child protection, and much more. The FTC has become the Federal *Technology* Commission—a term we coined,¹¹ but which the FTC and others have em-braced.¹²

³THOM FILE, U.S. CENSUS BUREAU, COMPUTER AND INTERNET USE IN THE UNITED STATES 1 (May 2013), <https://www.census.gov/prod/2013pubs/p20-569.pdf>; see also Steve Case, The Complete History of the Internet's Boom, Bust, Boom Cycle, Business Insider (Jan. 14, 2011), available at <http://www.businessinsider.com/what-factors-led-to-the-bursting-of-the-internet-bubble-of-the-late-90s-2011-1>.

⁴See FED. TRADE COMM'N, PRIVACY ONLINE: FAIR INFORMATION PRACTICES IN THE ELECTRONIC MARKETPLACE: A REPORT TO CONGRESS 1 (2000), <https://www.ftc.gov/sites/default/files/documents/reports/privacy-online-fair-information-practices-electronic-marketplace-federal-trade-commission-report/privacy2000.pdf>.

⁵PONEMON INST. LLC, FOURTH ANNUAL STUDY: IS YOUR COMPANY READY FOR A BIG DATA BREACH? 1 (2016), <http://www.experian.com/assets/data-breach/white-papers/2016-experian-data-breach-preparedness-study.pdf> [hereinafter PONEMON, DATA BREACH].

⁶*Id.*

⁷Hope Hamashige, *Cybercrime can kill venture*, CNN (March 10, 2000), http://cnnfn.cnn.com/2000/03/10/electronic/q_crime/index.htm (reporting the findings of the Computer Security Institute at Carnegie Mellon University).

⁸PONEMON INST. LLC, 2014: A YEAR OF MEGA BREACHES 1 (2015), <http://www.ponemon.org/local/upload/file/2014%20The%20Year%20of%20the%20Mega%20Breach%20FINAL3.pdf>.

⁹Hamashige, *Cybercrime* (noting that, just as today, in 2000, "[e]ven the biggest Internet companies with the most sophisticated technology are vulnerable to hackers, a trend highlighted last month when hackers stopped traffic on several popular Internet sites including Yahoo!, Amazon.com and eBay.").

¹⁰See, e.g., ALAN CHARLES RAUL, TASHA D MANORANJAN & VIVEK MOHAN, THE PRIVACY, DATA PROTECTION AND CYBERSECURITY LAW REVIEW 268 (Alan Charles Raul, 1st ed. 2014) ("With certain notable exceptions, the U.S. system does not apply a 'precautionary principle' to protect privacy, but rather, allows injured parties (and government agencies) to bring legal action to recover damages for, or enjoin, 'unfair or deceptive' business practices.").

¹¹Berin Szóka & Geoffrey Manne, The Second Century of the Federal Trade Commission, TECHDIRT (Sept. 26, 2013), available at <https://www.techdirt.com/blog/innovation/articles/20130926/16542624670/secondcentury-federal-trade-commission.shtml>; see also Consumer Protection & Competition Regulation in a High-Tech World: Discussing the Future of the Federal Trade Commission, Report 1.0 of the FTC: Technology & Reform Project, 3 (Dec. 2013), available at http://docs.techfreedom.org/FTC_Tech_Reform_Report.pdf.

¹²Kai Ryssdal, The FTC is Dealing with More High Tech Issues, MARKETPLACE (Mar. 7, 2016) (quoting then-Chairman Edith Ramirez), available at <http://www.marketplace.org/2016/03/07/tech/ftc-dealing-more-high-tech-issues>.

This was inevitable, given the nature of the FTC’s authority. Enforcing the promises made by tech companies to consumers forms a natural baseline for digital consumer protection. On top of that deception power, the FTC has broad power to police other practices, without waiting for Congress to catch up. As the FTC said in its 1980 Unfairness Policy statement:

The present understanding of the unfairness standard is the result of an evolutionary process. The statute was deliberately framed in general terms since Congress recognized the impossibility of drafting a complete list of unfair trade practices that would not quickly become outdated or leave loopholes for easy evasion.¹³

The question is not whether the FTC *should* be the Federal Technology Commission, but *how* it wields its powers. For all that academics like to talk about creating a Federal Search Commission¹⁴ or a Federal Robotics Commission,¹⁵ and for all the talk in Washington of passing “comprehensive baseline privacy legislation” or data security legislation, the most important questions turn on the FTC’s processes, standards, and institutional structure. How the FTC and Congress handle these seemingly banal matters could be even more important in determining how consumer protection works in 2117 than will any major legislative lurches over the next century. Indeed, with the costs of cybercrimes expected to reach \$2 trillion by 2019,¹⁶ the business community can ill afford to have to anticipate the approaches of both hackers and Federal regulators simultaneously, and it would seem more practical for the agency to help guide businesses by providing best practices to better protect their consumers. Yet, rather than promulgate rules or provide any clear guidance, the FTC has instead chosen to approach the issue through case-by-case enforcement actions, almost always ending in consent decrees, which do not admit liability and only focus on prospective requirements of the specific defendant in that case.¹⁷

This approach, and the resulting ambiguity, has left companies facing uncertainty in terms of whether their data security and privacy practices are not only sufficient to safeguard against an FTC enforcement action, but more importantly, whether they’re utilizing the best practices available to protect their consumers’ data and privacy.

Understandably, this ambiguity has frustrated judges and legal commentators alike, even resulting in one company’s demise. Such frustration was made abundantly clear by the Third Circuit when, despite affirming the FTC’s authority to regulate cyber security practices under the “unfair practices” prong of Section 5, the court nonetheless questioned the Commission’s assertion that its consent decrees and “guidance” somehow create standards against which companies’ cyber practices

¹³ See, e.g., Omer Tene, *With Ramirez, FTC became the Federal Technology Commission*, IAPP (Jan. 18, 2017), <https://iapp.org/news/a/with-ramirez-ftc-became-the-federal-technology-commission/>.

¹⁴ Fed. Trade Comm’n, *FTC Policy Statement on Unfairness* (1980), available at <https://www.ftc.gov/public-statements/1980/12/ftc-policy-statement-unfairness> (hereinafter 1980 Unfairness Policy Statement).

¹⁵ See, e.g., Oren Bracha & Frank Pasquale, *Federal Search Commission? Access, Fairness, and Accountability in the Law of Search*, 93 CORNELL L. REV. 1149 (2008), available at <http://www.lawschool.cornell.edu/research/cornell-law-review/upload/Bracha-Pasquale-Final.pdf>.

¹⁶ See, e.g., Ryan Calo, *The case for a Federal robotics commission*, Brookings Institute (Sept. 15, 2014), available at <https://www.brookings.edu/research/the-case-for-a-federal-robotics-commission/>; Nancy Scola, *Why the U.S. might just need a Federal Commission on Robotics*, Washington Post (Sept. 15, 2014), available at https://www.washingtonpost.com/news/the-switch/wp/2014/09/15/why-the-u-s-might-just-need-a-federal-commission-on-robots/?utm_term=.38dfc4bec72e.

¹⁷ Steve Morgan, *Cyber Crime Costs Projected to Reach \$2 Trillion by 2019*, Forbes (Jan. 17, 2016), available at <https://www.forbes.com/sites/stevemorgan/2016/01/17/cyber-crime-costs-projected-to-reach-2-trillion-by-2019/#6e10063a3a91>.

¹⁸ See *F.T.C. v. Wyndham Worldwide Corp.*, 799 F.3d 236, 257, n.22. (3d Cir. 2015). Notably, this practice is not entirely limited to data security and privacy enforcement—though for reasons later discussed, the effects on companies are arguably more severe in this context—by the Commission, with one study finding that 1,524 of the 2,092 enforcement action brought by the FTC in either Federal or administrative courts have ended in consent decrees without any adjudication. This means that almost 73 percent of the FTC’s enforcement actions have ended in legally enforceable orders, despite no impartial judicial guidance as to the factual and legal legitimacy of the FTC’s claims. See Daniel A. Crane, *Debunking Humphrey’s Executor*, 83 GEO. WASH. L. REV. 1835, 1867 (2015). But in tech-related cases its almost 100 percent, meaning the courts have played essentially no role at all in disciplining the FTC’s use of unfairness in “informational injury” cases. See *infra* note 122 (providing list of a few cases that did not result in settlement).

can be tested for “unfairness.”¹⁸ In fact, the Third Circuit emphatically agreed with the defendant’s claim that “consent orders, which admit no liability and which focus on prospective requirements on the defendant, were of little use to it in trying to understand the specific requirements imposed by § 45(a).”¹⁹ The court continued:

We recognize it may be unfair to expect private parties back in 2008 to have examined FTC complaints or consent decrees. Indeed, these may not be the kinds of legal documents they typically consulted. At oral argument we asked how private parties in 2008 would have known to consult them. The FTC’s only answer was that “if you’re a careful general counsel you do pay attention to what the FTC is doing, and you do look at these things.” Oral Arg. Tr. at 51. We also asked whether the FTC has “informed the public that it needs to look at complaints and consent decrees for guidance,” and the Commission could offer no examples. *Id.* at 52.²⁰

The court’s frustration did not end with the Commission’s use of consent decrees either, making sure to also address issues with the FTC’s 2007 guidebook, *Protecting Personal Information, A Guide for Businesses*, which, according to the FCC, “describes a ‘checklist[]’ of practices that form a ‘sound data security plan.’”²¹ Ultimately, the court recognized that “[t]he guidebook does not state that any particular practice is required by [Section 5],” and “[f]or this reason, we agree . . . that the guidebook could not, on its own, provide ‘ascertainable certainty’ of the FTC’s interpretation of what specific cybersecurity practices fail [Section 5].”²²

Despite being rebuked by practitioners and courts alike, the FTC has brushed aside this frustration and continued to rely on consent decrees, conclusory guidebooks/reports, and “blog posts” to inform businesses as to what constitutes reasonable data security and privacy practices. By contrast, the FTC has pursued a radically different course, providing significantly more thorough guidance in an area not considered to be the FTC’s primary jurisdiction—environmental regulations through “Green Guides.” As explained below, these Green Guides reflect a sincere and thoughtful effort by the FTC to gather relevant data as the basis for analyzing not only “what” is required, but more significantly “why” is it essential and “how much” of a certain practice is necessary.

On privacy and data security, the Commission has refused to do such empirical work or to issue clear guidance, relying instead on consent decrees and conclusory reports and guidebooks that lack any evident empirical foundation. This has deprived businesses of the regulatory certainty and clarity they need to comply with the law—and deprived consumers of better, more consistent data security and privacy practices. The Commission has flaunted the warning given it by the D.C. Circuit over forty years ago, that “courts have stressed the advantages of efficiency and expedition which inhere in reliance on rulemaking instead of adjudication alone,” including in providing businesses with greater certainty as to what business practices are not permissible.²³ Ironically, the D.C. Circuit made that statement in a case where the FTC fought vehemently—and the court agreed—for the authority to provide the very guidance they refuse to provide to the digital economy today. Congress *did* provide that rulemaking authority a year later, with the Magnuson-Moss Act of 1975,²⁴ but also found it necessary to institute new procedural safeguards in 1980, after the FTC’s gross abuse of its rulemaking powers in the intervening five years,²⁵ which culminated in the agency being denounced as the “National Nanny.”²⁶

With this backdrop in mind, I come before this Committee today with two goals. First, to inform this body—through a historical lens—of the FTC’s ongoing procedural issues, particularly as they pertain to data security and privacy practices. Sec-

¹⁸ *F.T.C. v. Wyndham Worldwide Corp.*, 799 F.3d 236, 252–253, 255 (3d Cir. 2015).

¹⁹ *Id.* at 257 n.22.

²⁰ *Id.* at 257 n.23.

²¹ *Id.* at 257.

²² *Id.* at 257 n.21.

²³ *Nat’l Petroleum Refiners Ass’n v. F.T.C.*, 482 F.2d 672, 675–76 (D.C. Cir. 1973), cert. denied, 415 U.S. 951 (1974).

²⁴ The Magnuson-Moss Warranty Federal Trade Commission Improvement (Magnuson-Moss) Act, Pub.L. No. 93–637, § 202(a), 88 Stat. 2193 (1975).

²⁵ The Federal Trade Commission Improvements Act of 1980 (Improvements Act), Pub.L. No. 96–252, 94 Stat. 374 (1980).

²⁶ Editorial, WASH. POST (Mar. 1, 1978), reprinted in MICHAEL PERTSCHUK, REVOLT AGAINST REGULATION, 69–70 (1982); see also J. Howard Beales III, *Advertising to Kids and the FTC: A Regulatory Retrospective that Advises the Present*, 8 n.37 (2004), available at https://www.ftc.gov/sites/default/files/documents/public_statements/advertising-kidsand-ftc-regulatory-retrospective-advises-present/040802adstokids.pdf. (“Former FTC Chairman Pertschuk characterizes the Post editorial as a turning point in the Federal Trade Commission’s fortunes.”).

ond, to use that historical analysis as a framework with which to propose practical process reforms that will ensure American businesses and the FTC work together as partners, not enemies, to make certain that consumers’—including Americans as well as foreign consumers who patronize U.S. businesses—data and privacy are afforded the greatest respect and protection possible.

To that end, we herein provide a more indepth historical analysis of the FTC’s enforcement authority, including an examination of the problems that have arisen due to the FTC’s current procedural issues. We detail how the FTC has utilized data-driven guidance in other contexts—namely the aforementioned Green Guides—to guide businesses through empirical analysis of available data. Finally, we use that historical context to frame ways that Congress can help urge the FTC to provide the same types of empirical guidance to the tech industry. Finally, I will discuss the underlying issues with the FTC’s *very* low pleading standard and examine ways that Congress can address this problem.

Background of FTC Enforcement in the Digital Economy

While the FTC began studying online privacy issues as early as 1995,²⁷ the FTC truly started dealing with consumer protection issues related to the Internet in 1997—settling a series of assorted cases before, in 2001, it brought its first data security enforcement action premised on deception, settled against Eli Lilly in 2002.²⁸ In 2005, the FTC brought its first data security action premised on unfairness against BJ’s Wholesale Club.²⁹ According to the FTC’s most recent Privacy & Data Security Update, the Commission has brought over 60 data security cases since 2002, over 40 general privacy cases, and over 130 spam and spyware cases.³⁰ Yet, as discussed, rather than promulgate rules or provide any clear guidance, the FTC has instead chosen to approach the issue through case-by-case enforcement actions, almost always ending in consent decrees, which only focus on prospective requirements of the specific defendant in that case.³¹ the FTC truly started dealing with consumer protection issues related to the Internet in 1997—settling a series of assorted cases before, in 2001, it brought its first data security enforcement action premised on deception, settled against Eli Lilly in 2002.³² In 2005, the FTC brought its first data security action premised on unfairness against BJ’s Wholesale Club.³³ According to the FTC’s most recent Privacy & Data Security Update, the Commission has brought over 60 data security cases since 2002, over 40 general privacy cases, and over 130 spam and spyware cases.³⁴ Yet, as discussed, rather than promulgate rules or provide any clear guidance, the FTC has instead chosen to approach the issue through case-by-case enforcement actions, almost always ending in

²⁷ See FED. TRADE COMM’N, PRIVACY ONLINE: A REPORT TO CONGRESS 2 (June 1998), available at <https://www.ftc.gov/sites/default/files/documents/reports/privacy-online-report-congress/priv-23a.pdf> [hereinafter 1998 FTC Privacy Report] (“In April 1995, staff held its first public workshop on Privacy on the Internet, and in November of that year, the Commission held hearings on online privacy as part of its extensive hearings on the implications of globalization and technological innovation for competition and consumer protection issues.”); see also FED. TRADE COMM’N, A REPORT FROM THE FEDERAL TRADE COMMISSION STAFF: THE FTC’S FIRST FIVE YEARS PROTECTING CONSUMERS ONLINE (Dec. 1999), available at <https://www.ftc.gov/sites/default/files/documents/reports/protecting-consumers-online/fiveyearreport.pdf>.

²⁸ See Press Release, Fed. Trade Comm’n, Eli Lilly Settles FTC Charges Concerning Security Breach (Jan. 18, 2002), available at <https://www.ftc.gov/news-events/press-releases/2002/01/eli-lilly-settles-ftc-charges-concerning-security-breach>.

²⁹ See Complaint, In re BJ’s Wholesale Club, Inc. (F.T.C. Sept. 20, 2005) (No. C–4–4148), available at <https://www.ftc.gov/sites/default/files/documents/cases/2005/09/092305comp0423160.pdf>; see also Michael D. Scott, The FTC, the Unfairness Doctrine, and Data Security Breach Litigation: Has the Commission Gone Too Far?, 60 Admin. L. Rev. 127, 146 (2008) (discussing BJ’s Wholesale Club enforcement action and use of unfairness prong).

³⁰ See Fed. Trade Comm’n, 2016 Privacy & Data Security Update (Jan. 2017), <https://www.ftc.gov/reports/privacy-data-security-update-2016> (providing overview of various enforcement actions).

³¹ *F.T.C. v. Wyndham Worldwide Corp.*, 799 F.3d 236, 257 n.22 (3d Cir. 2015).

³² See Press Release, Fed. Trade Comm’n, Eli Lilly Settles FTC Charges Concerning Security Breach (Jan. 18, 2002), available at <https://www.ftc.gov/news-events/press-releases/2002/01/eli-lilly-settles-ftc-charges-concerning-security-breach>.

³³ See Complaint, In re BJ’s Wholesale Club, Inc. (F.T.C. Sept. 20, 2005) (No. C–4–4148), available at <https://www.ftc.gov/sites/default/files/documents/cases/2005/09/092305comp0423160.pdf>; see also Michael D. Scott, The FTC, the Unfairness Doctrine, and Data Security Breach Litigation: Has the Commission Gone Too Far?, 60 Admin. L. Rev. 127, 146 (2008) (discussing BJ’s Wholesale Club enforcement action and use of unfairness prong).

³⁴ See Fed. Trade Comm’n, 2016 Privacy & Data Security Update (Jan. 2017), <https://www.ftc.gov/reports/privacy-data-security-update-2016> (providing overview of various enforcement actions).

consent decrees, which only focus on prospective requirements of the specific defendant in that case.³⁵

In a speech last week, Acting Chairman Ohlhausen broadly summarized the “various types of consumer injury addressed in our privacy and data security cases” as “informational injury.”³⁶ It’s a useful shorthand: one term to describe a cluster of consumer protection problems behind a wide range of cases. But for the same reason, it’s also a dangerous term—one that could, like “net neutrality,” take on a life its own, and serve to obscure and frustrate analysis rather than inform it.³⁷ Of course, Chairman Ohlhausen chose her words carefully:

[L]et me also emphasize that this is not a discussion of the legal question of what constitutes a “substantial injury” under our unfairness standard. My topic today may inform the substantial injury question, but I am speaking more broadly. Indeed, many of the cases I will mention are deception cases, or allege both deception and unfairness.

In my review of our privacy and data security cases, I have identified at least five different types of consumer informational injury. Certain of these types are more common. Many of our cases involve multiple types of injury. Courts and FTC cases often emphasize *measurable* injuries from privacy and data security incidents, although other injuries may be present. And to be clear, not all of these types of injury, standing alone, would be sufficient to trigger liability under the FTC Act.³⁸

It is fitting that she should emphasize the word “measurable”—and also caveat it with the word “often”—because both speak to the central question facing the Federal Technology Commission as it grapples with an endless, and accelerating, parade of novel consumer protection issues: *how* does the agency determine what the right answer is in any particular case and what should be done about it? Ohlhausen defended the FTC’s approach to privacy and data security enforcement:

Case-by-case enforcement focuses on real-world facts and specifically alleged behaviors and injuries. As such, each case integrates feedback on earlier cases from advocates, the marketplace and, importantly, the courts. This ongoing process preserves companies’ freedom to innovate with data use. And it can adapt to new technologies and new causes of injury.³⁹

Yes, the courts’ “feedback” is “important.” Indeed, in a reply brief the FTC expressly agreed with TechFreedom on this importance of courts’ guidance when it said it “agrees that the field would be aided by a body of law that includes ‘Article III court decisions.’”⁴⁰ Yet, such assertions of the importance of courts’ “feedback” by the FTC seem empty given there has been precious little of it. Since 1997, not counting a handful of cases where the FTC sought injunctive relief against absent defendants (generally foreign scammers), the FTC has litigated, even partially, only

³⁵ *F.T.C. v. Wyndham Worldwide Corp.*, 799 F.3d 236, 257 n.22 (3d Cir. 2015).

³⁶ Maureen K. Ohlhausen, Acting Chairman, Fed. Trade Comm’n, *Painting the Privacy Landscape: Information Injury in FTC Privacy and Data Security Cases*, Address Before the Federal Communications Bar Association (Sept. 19, 2017), https://www.ftc.gov/system/files/documents/public_statements/1255113/privacy_speech_mkohlhausen.pdf [hereinafter Ohlhausen, *Informational Injury Speech*].

³⁷ Larry Downes, *The Tangled Web of Net Neutrality and Regulation*, Harvard Business Review (March 31, 2017), available at <https://hbr.org/2017/03/the-tangled-web-of-net-neutrality-and-regulation> (“Despite being a simple idea, net neutrality has proven difficult to translate into U.S. policy. It sits uncomfortably at the intersection of highly technical Internet architecture and equally complex principles of administrative law. Even the term “net neutrality” was coined not by an engineer but by a legal academic, in 2003.”). Gerard Stegmaier, a veteran attorney in the field of data security and privacy, explained it as such: “Words matter. Net Neutrality. Deep Packet Inspection. #Privacy. Businesses beware. There’s a new label in town from the gov’t and repeating it could have significant unintended consequences. From a speech yesterday the @FTC acting chair declared “informational injuries” exist. Let that sink in.” Posting of Gerard Stegmaier on LinkedIn.com (Sept. 20, 2017), available at <https://www.linkedin.com/feed/update/urn:li:activity:6316291846356115456> (also on file with author).

³⁸ Ohlhausen, *Informational Injury Speech*, *supra* note 36, at 2–3.

³⁹ Ohlhausen, *Informational Injury Speech*, *supra* note 36, at 2.

⁴⁰ Plaintiff’s Response In Opposition to the Motion to Dismiss, *F.T.C. v. Wyndham Worldwide Corp.*, 10 F. Supp. 3d 602 (D.N.J. 2014), *aff’d*, 799 F.3d 236 (3d Cir. 2015) (No. 2:13–CV–01887–ES–SCM) at 22, n. 8.

a handful of cases: *LabMD*,⁴¹ *Wyndham Worldwide Corp.*,⁴² *Amazon.com, Inc.*,⁴³ and *D-Link Systems, Inc.*⁴⁴ Thus, the way the FTC works today is a far cry from what the FTC said about how it would operate back in 1980:

The statute was deliberately framed in general terms since Congress recognized the impossibility of drafting a complete list of unfair trade practices that would not quickly become outdated or leave loopholes for easy evasion. The task of identifying unfair trade practices was therefore assigned to the Commission, subject to judicial review, in the expectation that the underlying criteria would evolve and develop over time. As the Supreme Court observed as early as 1931, the ban on unfairness “belongs to that class of phrases which do not admit of precise definition, but the meaning and application of which must be arrived at by what this court elsewhere has called ‘the gradual process of judicial inclusion and exclusion.’”⁴⁵

What former FTC Chairman Tim Muris said of the Commission in 1981 remains true today: “Within very broad limits, the agency determines what shall be legal. Indeed, the agency has been ‘lawless’ in the sense that it has traditionally been beyond judicial control.”⁴⁶ As he noted in his 2010 testimony before a Senate Subcommittee, “the Commission’s authority remains extremely broad.”⁴⁷ What Commissioner Wright said of the FTC’s competition enforcement—where the Commission differs from the DOJ in enforcing (in theory, anyway) the same substantive laws—is even more true of consumer protection:

The combination of institutional and procedural advantages with the vague nature of the Commission’s Section 5 authority gives the agency the ability, in some cases, to elicit a settlement even though the conduct in question very likely may not [violate any law or regulation]. This is because firms typically prefer to settle a Section 5 claim rather than going through lengthy and costly administrative litigation in which they are both shooting at a moving target and have the chips stacked against them. Significantly, such settlements also perpetuate the uncertainty that exists as a result of the ambiguity associated with the Commission’s [Section 5] authority by encouraging a process by which the contours of Section 5 are drawn without any meaningful adversarial proceeding or substantive analysis of the Commission’s authority.⁴⁸

Without the courts to demand rigor from the FTC in defining “measurable” harm, what should the Commission do? And what should Congress do?

Chairman Ohlhausen’s speech represents a major step in the right direction—precisely because it promises to give more analytical rigor to the term “informational injury” than such generalizations generally have. She concludes:

This analysis raises several important questions. Is this list of injuries representative? When do these or other informational injuries require government intervention? Perhaps most importantly, how does this list map to our statutory deception and unfairness authorities?

These are critical and challenging questions. That’s why I am announcing today that the FTC will host a workshop on informational injury on December 12 of this year. This workshop will bring stakeholders together to discuss these issues in depth. I have three goals for this workshop: First, better identify the quali-

⁴¹*LabMD, Inc. v. F.T.C.*, No. 1:14-CV-00810-WSD, 2014 WL 1908716, at *1 (N.D. Ga. May 12, 2014), *aff’d*, 776 F.3d 1275 (11th Cir. 2015).

⁴²*F.T.C. v. Wyndham Worldwide Corp.*, 799 F.3d 236, 257 n.22 (3d Cir. 2015).

⁴³*F.T.C. v. Amazon.com, Inc.*, 71 F. Supp. 3d 1158 (W.D. Wash. 2014).

⁴⁴*Fed. Trade Comm’n v. D-Link Sys., Inc.*, No. 3:17-CV-00039-JD, 2017 WL 4150873, at *1 (N.D. Cal. Sept. 19, 2017).

⁴⁵1980 Unfairness Policy Statement, *supra* note 12 (quoting *FTC v. Raladam Co.*, 283 U.S. 643, 648 (1931)).

⁴⁶Timothy J. Muris, *Judicial Constraints*, in *THE FEDERAL TRADE COMMISSION SINCE 1970: ECONOMIC REGULATION AND BUREAUCRATIC BEHAVIOR*, 35, 49 (Kenneth W. Clarkson & Timothy J. Muris, eds., 1981).

⁴⁷*Hearing on Financial Services and Products: The Role of the Fed. Trade Commission in Protecting Customers, before the Subcomm. on Consumer Protection, Product Safety, and Insurance of the S. Comm. on Commerce, Science, and Transportation*, 111th Cong. 2 (2010) (statement of Timothy J. Muris, Former Chairman, Fed. Trade Comm’n) available at http://lawproffessors.typepad.com/files/muris_senate_testimony_ftc_role_protecting_consumers_3-17-101.pdf.

⁴⁸Joshua D. Wright, *Revisiting Antitrust Institutions: The Case for Guidelines to Recalibrate the Federal Trade Commission’s Section 5 Unfair Methods of Competition Authority*, 4 CONCURRENTS: COMPETITION L.J. 1 at 3 (2013), available at https://www.ftc.gov/sites/default/files/documents/public_statements/siting-antitrust-institutions-case-guidelines-recalibrate-federal-trade-commissions-section-5-unfair/concurrences-4-2013.pdf.

tatively different types of injury to consumers and businesses from privacy and data security incidents. Second, explore frameworks for how we might approach quantitatively measuring such injuries and estimate the risk of their occurrence. And third, better understand how consumers and businesses weigh these injuries and risks when evaluating the tradeoffs to sharing, collecting, storing, and using information. Ultimately, the goal is to inform our case selection and enforcement choices going forward.⁴⁹

Amen. This is the kind of workshop the FTC should have held two decades ago—and several more times since. The FTC has, in fact, conducted such workshops, collected empirical data, and issued corresponding guidance based upon rigorous empirical analysis in another context: the Green Guides first issued for environmental marketing in 1992, and updated three times since then.⁵⁰ As discussed below, these offer an excellent model for how the Commission could begin to take a more substantive approach to defining informational injury, while also providing clearer guidance to industry.

Congress should support and encourage this effort—by holding the FTC to the high standards set by its work on the Green Guides. If this effort represents a significant departure with the analytically flimsy, “know-it-when-we-see-it” approach the FTC has generally taken to “informational injury” cases thus far, both consumers and companies would benefit from clearer, better substantiated guidance. But this will not be an easy change to make; it will require a new degree of rigor in how the Bureau of Consumer Protection operates, and a new closeness in BCP’s engagement with the Bureau of Economics.

At best, this could be the beginnings of a “law and economics” revolution in consumer protection law—of the sort that transformed competition law in decades past, has guided the Bureau of Competition since, and has informed the courts in their development of antitrust case law.

But at worst, this process could result in blessing the FTC’s current approach with a veneer of analytical rigor that merely validates the status quo. The report that comes out of this process *could* resemble the reports the FTC has produced since the 2012 Privacy Report, which make broad recommendations as to what industry best practices should be, without any real analysis behind those recommendations or how they relate to the Commission’s powers under Section 5.⁵¹

Chairman Ohlhausen’s initial thoughtful framing suggests reason for optimism, but everything will depend on how she and whoever becomes permanent Chairman (if it is not her) execute on the plan. In any event, the Commission’s own more recent experience with the Green Guides—to say nothing of the last 15 years of experience with data security and privacy—suggests that self-restraint is unlikely to prove sustainable, on its own, in disciplining the agency. Ultimately, the kind of analytical quality that has defined antitrust law, and has sustained the law and economics approach there, requires *external* constraints—namely, regular engagement with the courts and oversight by Congress.

To that end, a careful reassessment of the Commission’s processes is long overdue. The last time Congress seriously reconsidered, and revised, the FTC’s processes was in 1994.⁵² The agency has not been reauthorized since 1996.⁵³ Congress should return to its habit—the default assumption prior to Ken Starr, Monica Lewinsky, and impeachment—of reauthorizing the FTC every two years and, each time, re-examining how well the agency is working. Modifications to the statute should not be made lightly, but they should also happen more often than once in a generation.

Last year, the House Committee on Energy and Commerce considered no fewer than seventeen bills regarding the FTC. The attached white paper, co-authored with Geoffrey Manne, Executive Director of the International Center for Law & Econom-

⁴⁹ Ohlhausen, *Informational Injury Speech*, *supra* note 36, at 9.

⁵⁰ See Fed. Trade Comm’n, *Environmental Friendly Products: FTC’s Green Guides* (last visited Sept. 24, 2017), available at <https://www.ftc.gov/news-events/media-resources/truth-advertising/green-guides> (“The Green Guides were first issued in 1992 and were revised in 1996, 1998, and 2012. The guidance they provide includes: (1) general principles that apply to all environmental marketing claims; (2) how consumers are likely to interpret particular claims and how marketers can substantiate these claims; and (3) how marketers can qualify their claims to avoid deceiving consumers.”).

⁵¹ See BERIN SZÓKA & GEOFFREY A. MANNE, *THE FEDERAL TRADE COMMISSION: RESTORING CONGRESSIONAL OVERSIGHT OF THE SECOND NATIONAL LEGISLATURE 57–60* (2016), available at <http://docs.house.gov/meetings/IF/IF17/20160524/104976/HHRG-114-IF17-Wstate-ManneG-20160524-SD004.pdf> [hereinafter White Paper].

⁵² Federal Trade Commission Act Amendments of 1994, Pub. L. 103–312, 108 Stat. 1691 (Aug. 26, 1994) available at <http://uscode.house.gov/statutes/pl/103/312.pdf>.

⁵³ Federal Trade Commission Reauthorization Act of 1996, Pub. L. 104–216, 110 Stat. 3019 (Oct. 1, 1996), available at <http://uscode.house.gov/statutes/pl/104/216.pdf>.

ics, surveys those bills and provides recommendations to Congress on how to approach them.⁵⁴ Together, they form a starting point for the Senate Commerce Committee to begin its work, but they do not cover many of the most important aspects of how the agency works. Given this Committee's extensive knowledge and expertise, we hope that this Committee, along with the broader Senate, should start its own work on FTC reform legislation afresh.

II. Summary of Proposed Legislative Reforms

Rather than repeat the full analysis provided in the aforementioned white paper we presented to the House Energy & Commerce Committee last year, we have instead provided a short overview of how to consider thinking about the main issues we believe need to be addressed through legislation.

A. *The Common Carrier Exception*

The FTC Act excludes “common carriers subject to the Acts to regulate commerce.”⁵⁵ What this provision means will be crucial—especially for technology cases in the coming years—and merits clarification from Congress.

The Federal Communications Commission has proposed to undo its 2015 reclassification of broadband providers as common carriers.⁵⁶ Doing so will return the controversial issue of “net neutrality” to the Federal Trade Commission by restoring the FTC’s jurisdiction over broadband providers—or rather, there *should* be a seamless transition to ensure that consumers remain protected. But a Ninth Circuit panel decision last year calls into question whether the FTC’s jurisdiction will be fully restored,⁵⁷ creating the possibility that a company providing broadband service, once that service is no longer considered a common carrier service by the FCC, might still remain outside the jurisdiction of the FTC either because (1) that particular corporate entity also provides a common carrier service such as voice (which will remain subject to Title II of the Communications Act even after the FCC’s proposes re-reclassification of broadband) or (2) another corporate entity under common ownership provides such a common carrier service. In short, the panel decision rejected the FTC’s longstanding “activity-based” interpretation of the statute in favor of an “entity-based” interpretation. The Ninth Circuit granted rehearing of that decision earlier this year, effectively vacating the panel decision.⁵⁸

At oral arguments last week, AT&T stuck by its general arguments for an entity-bases interpretation, but clarified two things.⁵⁹ First, it read the statute to turn on the common carrier or non-common carrier status of each specific corporate entity, so that the FTC’s jurisdiction over Oath, for example, the company formed by the Verizon parent company after it acquired AOL and Yahoo! and merged them together, would not be affected by the fact that Verizon Wireless provides a common carrier voice service. Second, AT&T argued that the FCC has plenary jurisdiction to, as it did in the *Computer Inquiries*, mandate such structural separation to ensure that there is no gap in consumer protection between the FTC and FCC.⁶⁰

It is impossible to predict how the Ninth Circuit might resolve this case, but it is safe to say that if the FCC issues its Third Open Internet Order this year, or even early next year, that decision might well come out before the Ninth Circuit’s decision.

Congress should not assume that the Ninth Circuit will fully restore the FTC’s activity-based interpretation of its jurisdiction, even though appears to be the most likely result of the case. Congress should, instead, consider quickly moving legislation that would codify that interpretation. Even if the Ninth Circuit en banc panel accepts AT&T’s argument and simply narrows the panel decision, that would only solve part of the problem raised by the panel decision. Requiring structural separation between “edge” companies like Oath and broadband companies like Verizon *might* make business sense anyway, but it might not—especially given the ongoing push to restrict the sharing of consumer data *even among corporate affiliates under common ownership*. Furthermore, AT&T’s argument would still raise serious questions about which agency will deal with net neutrality and other consumer protec-

⁵⁴ See generally White Paper, *supra* note 51.

⁵⁵ 15 U.S.C. § 45(a).

⁵⁶ Notice of Proposed Rulemaking, Restoring Internet Freedom, WC Docket No. 17–108, 32 FCC Rcd 4434 (2017), https://apps.fcc.gov/edocs_public/attachmatch/FCC-17-60A1_Red.pdf.

⁵⁷ *Fed. Trade Comm’n v. AT & T Mobility LLC*, 835 F.3d 993 (9th Cir. 2016), *reh’g en banc granted sub nom.*, *Fed. Trade Comm’n v. AT&T Mobility LLC*, 864 F.3d 995 (9th Cir. 2017).

⁵⁸ *Fed. Trade Comm’n v. AT&T Mobility LLC*, 864 F.3d 995 (9th Cir. 2017).

⁵⁹ United States Court of Appeals for the Ninth Circuit, *Fed. Trade Comm’n v. AT&T Mobility LLC*, 864 F.3d 995 (2017), Oral Arguments, available at <https://www.youtube.com/watch?v=Rs8EQU-KIEw>.

⁶⁰ *Id.* at 13:50.

tion concerns about broadband services once they are returned to Title I: it is difficult to see how the common carrier services provided by these companies, if only telephony, could be functionally separated from the broadband service. Would consumers have to deal with, and subscribe to, two separate services, each offered by a separate corporate entity?

The Ninth Circuit may, of course, reject AT&T's arguments completely, fully reverse the panel decision, and restore the FTC's activity-based interpretation completely. But it would be far better for Congress to resolve this question before the FCC revises the regulatory classification of broadband. It could do so in a one-sentence bill.

Of course, many have argued that the common carrier exception should be abolished, and the Protecting Consumers in Commerce Act of 2016 (H.R. 5239) would have done just that.⁶¹ Simply restoring the activity-based exemption need not be permanent; it could be stop-gap measure that allows Congress time to consider whether to maintain the exemption.

B. More Economic Analysis

As many commentators have noted, the FTC has frequently failed to employ sufficient economic analysis in both its enforcement work and policymaking. Former Commissioner Josh Wright summarized the problem pointedly in a speech entitled "The FTC and Privacy Regulation: The Missing Role of Economics," explaining:

An economic approach to privacy regulation is guided by the tradeoff between the consumer welfare benefits of these new and enhanced products and services against the potential harm to consumers, both of which arise from the same free flow and exchange of data. Unfortunately, government regulators have instead been slow, and at times outright reluctant, to embrace the flow of data. What I saw during my time at the FTC is what appears to be a generalized apprehension about the collection and use of data—whether or not the data is actually personally identifiable or sensitive—along with a corresponding, and arguably crippling, fear about the possible misuse of such data.⁶²

As Wright further noted, such an approach would take into account the risk of abuses that will cause consumer harm, weighed with as much precision as possible. Failing to do so can lead to significant problems, including creating disincentives for companies to innovate and create benefits for consumers.

Specifically, Congress or the FTC should require the Bureau of Economics to have a role in commenting on consent decrees⁶³ and proposed rulemaking,⁶⁴ and a greater role in the CID process. But the most effective ways to engage economists in the FTC's decisionmaking would be to raise the FTC's pleading standards and make reforms to the CID process designed to make litigation more likely: in both cases, the FTC will have to engage its economists more closely, either in order to ensure that its complaints are well-plead or to prevail on the merits in Federal court.

C. Clarification of the FTC's Substantive Standards

The FTC has departed in significant ways from both the letter and spirit of the 1980 Unfairness Policy Statement and the 1983 Deception Policy Statement. This is mainly due to the FTC essentially having complete, unchecked, discretion to interpret these policy statements as it sees fit—including the discretion to change course regularly without notice. The courts simply have not had the opportunity to effectively implement Section 5(n), nor has the FTC ever really chosen to constrain its own discretion in meaningful ways (as it has done with the Green Guides). Making substantive clarifications to Section 5 will not be adequate without *process* reforms to ensure that these clarifications are given effect over time. But that does not mean they would be without value.

In order to clarify the FTC's substantive standards under Section 5, we would suggest the following key changes:

1. Codifying other key aspects of the 1980 Unfairness Policy Statement into Section 5 that were not already added by the addition of Section 5(n) in 1994;

⁶¹Protecting Consumers in Commerce Act of 2016, H.R. 5239, 114th Cong. (2016), available at <https://www.congress.gov/bills/114/congress/house-bill/5239/text>.

⁶²Remarks of Joshua D. Wright, *The FTC and Privacy Regulation: The Missing Role of Economics*, George Mason University Law and Economics Center (Nov. 12, 2015), available at http://masonlec.org/site/rte_uploads/files/Wright_PRIVACYSPEECH_FINALv2_PRINT.pdf.

⁶³See White Paper, *supra* note 51, at 42–43.

⁶⁴See *id.* at 98–100.

2. Codifying the Deception Policy Statement, just as Congress codified the Unfairness Policy Statement in a new Section 5(n).⁶⁵ This issue is explored in greater depth in my 2015 joint comments with Geoffrey Manne on the FTC’s settlement of its enforcement action with Nomi Technologies, Inc.⁶⁶ Specifically, in codifying the Deception Policy Statement, Congress should:
 - a. Clarify—or require the FTC to propose clarifications of—when and how the FTC must establish the materiality of statements about products: it made sense to presume that all express statements were material in the context of traditional advertising: because each such statement was calculated to persuade users to buy a product. But the same cannot *necessarily* be said of the myriad other ways that companies communicate with users today, such as through online help pages or privacy policies (which companies are required to post online, if only by California law).
 - b. Require the FTC to meet the requirements of Section 5(n) when bringing enforcement actions based on the “reasonableness” of a company’s practices, such as data security.⁶⁷
3. Codify the FTC’s 2015 Unfair Methods of Competition Policy Statement, with one small modification: the FTC should be barred from going beyond antitrust doctrine.⁶⁸

D. Clarifying the FTC’s Pleading Standards

Several courts have already concluded that the FTC’s deception enforcement actions must satisfy the heightened pleading standards of Section 9(b) of the Federal Rules of Civil Procedure, which applies to claims filed in Federal court that “sound in fraud.”⁶⁹ As explained below, this requirement would not be difficult for the FTC to meet, since the agency has broad Civil Investigative powers that are not available to normal plaintiffs before filing a complaint.⁷⁰ There is no reason the FTC should not have to plead its deception claims with specificity.

The same can be said for unfairness claims, even though they do not “sound in fraud.” In both cases, getting the FTC to file more particularized complaints is critical, given that the FTC’s complaint is, in essentially all cases, the FTC’s last word on the matter, supplemented by little more than a press release, and an aid for public comment.

Indeed, the bar should likely be *higher*, not lower for unfairness cases. The attached white paper recommends a preponderance of objective standard for unfairness cases.⁷¹ The critical thing to note is that there is no statutory standard for settling FTC enforcement actions—so the standard by which the FTC really operates is the very low bar set by Section 5(b): “reason to believe that [a violation may have occurred]” and that “it shall appear to the Commission that [an enforcement action] would be to the interest of the public.”⁷² In addition to the substantive clarifications to the FTC’s substantive standards, Congress must clarify either the settlement standard or the pleading standard, if not both.

E. Encouraging More Litigation to Engage the Courts in the Development of Section 5 Doctrine and Provide More Authoritative Guidance

Litigation is important for two reasons. First, having to prove its case before a neutral tribunal forces analytical rigor upon the FTC and thus forces it to make better, more informed decisions. Second, court decisions will provide guidance to regulated companies on how to comply with the law that is necessarily more authoritative (since the FTC cannot simply overrule a court decision the way it can change its mind about its own enforcement actions or guidance) and also likely (but not necessarily) more detailed and better grounded in the FTC’s doctrines.

⁶⁵ See White Paper, *supra* note 51, at 21–28.

⁶⁶ In the *Matter of Nomi Technologies, Inc.*, Comments of the International Center for Law & Economics & TechFreedom, File No. 1323251 (May 26, 2015), https://www.ftc.gov/system/files/documents/public_comments/2015/05/00011-96185.pdf.

⁶⁷ See *infra* 69.

⁶⁸ See White Paper, *supra* note 51, at 28–30; Fed. Trade Comm’n, Statement of Enforcement Principles Regarding “Unfair Methods of Competition” Under Section 5 of the FTC Act (Aug. 13, 2015), available at https://www.ftc.gov/system/files/documents/public_statements/735201/150813section5enforcement.pdf.

⁶⁹ *Rombach v. Chang*, 355 F.3d 164, 170 (2d Cir. 2004) (“In deciding this issue, several circuits have distinguished between allegations of fraud and allegations of negligence, applying Rule 9(b) only to claims pleaded under Section 11 and Section 12(a)(2) that sound in fraud.”).

⁷⁰ See *infra* at 19.

⁷¹ See White Paper, *supra* note 51, at 18–21.

⁷² 15 U.S.C. § 45(b).

One major reason companies settle so often across the board is that the FTC staff has the discretion to force companies to endure the process of litigating through the FTC's own administrative process, first before an administrative law judge and then before the Commission itself, before ever having the opportunity to go before an independent, neutral tribunal. The attached white paper explore three options:⁷³

1. "[E]mpower one or two Commissioners to insist that the Commission bring a particular complaint in Federal court. This would allow them to steer cases out of Part III either because they are doctrinally significant or because the Commissioners fear that, unless the case goes to Federal court, the defendant will simply settle, thus denying the entire legal system the benefits of litigation in building the FTC's doctrines. In particular, it would be a way for Commissioners to act on the dissenting recommendations of staff, particularly the Bureau of Economics, about cases that are problematic from either a legal or policy perspective."⁷⁴
2. Abolish Part III completely, as former Commissioner Calvani has proposed.⁷⁵
3. Require the FTC to litigate in Federal court while potentially still preserving Part III for the supervision of the settlement process and discovery.⁷⁶ Requiring the FTC to litigate all cases in Federal court (as the SMARTER Act would do for competition cases⁷⁷) might, in principle, prove problematic for the Bureau of Consumer Protection, which handles many smaller cases. Retaining Part III but allowing Commissioners to object to its use might strike the best balance.

F. The Civil Investigative Demand Process

There are many reasons why companies do not litigate privacy and data security cases. Some of them are beyond the control of FTC or Congress—for example, the extreme sensitivity of these issues for companies. Studies by the Ponemon Institute found that “[d]ata breaches are more concerning than product recalls and lawsuits,”⁷⁸ with a company's stock price falling an average of 5 percent after a data breach is disclosed.⁷⁹ Witness the 30 percent hit Equifax took to its stock price upon revelation of its data breach.⁸⁰ Perhaps most illustrative of the sensitivity of these issues was the case of LabMD—a medical testing company and one of the handful of companies who dared litigate against the FTC—which ultimately went out of business due to litigation costs and reputational damage, even though the judge ultimately found that no consumer was injured.⁸¹ But a very significant, if not the biggest, reason why companies reflexively, almost invariably settle their cases is that the process of the FTC's investigation can be punishment enough to make settlement seem more attractive. After enduring a burdensome investigative process, companies (especially start-ups) frequently lack additional resources to defend themselves and face an informational asymmetry given the intrusiveness inherent in the FTC's current process. Even Chris Hoofnagle, who has long advocated that the FTC be far more aggressive on privacy and data security, warns, in his new treatise on privacy regulation at the agency, that

⁷³ See White Paper, *supra* note 51, at 82–85.

⁷⁴ *Id.*

⁷⁵ See *id.* at 84–85.

⁷⁶ *Id.*

⁷⁷ Standard Merger and Acquisition Reviews Through Equal Rules Act of 2015, H.R. 2745, 114th Cong. (2015).

⁷⁸ PONEMON, DATA BREACH, *supra* note 5, at 6.

⁷⁹ See Help Net Security, *After a data breach is disclosed, stock prices fall an average of 5 percent* (May 16, 2017), <https://www.helpnetsecurity.com/2017/05/16/data-breach-stock-price/> (detailing a study by Ponemon).

⁸⁰ Paul R. La Monica, *After Equifax apologizes, stock falls another 15 percent* (Sept. 13, 2017), available at <http://money.cnn.com/2017/09/13/investing/equifax-stock-mark-warner-ftc-probe/index.html>.

⁸¹ See, e.g., Cheryl Conner, *When The Government Closes Your Business*, *Forbes* (Feb. 1, 2014), <https://www.forbes.com/sites/cherylnsnapconner/2014/02/01/when-the-government-closes-your-business/#6e7c78971435>; Dune Lawrence, *A Leak Wounded This Company. Fighting the Feds Finished It Off*, *Bloomberg* (April 25, 2016), <https://www.bloomberg.com/features/2016-labmd-ftc-tiversa/> (“The one company that didn't settle with the FTC is LabMD. Daugherty hoped, at first, that if he were as cooperative as possible, the FTC would go away. He now calls that phase ‘the stupid zone.’”).

[T]he FTC’s investigatory power is very broad and is akin to an inquisitorial body. On its own initiative, it can investigate a broad range of businesses without any indication of a predicate offense having occurred.⁸²

This onerous the process inevitably leads to more false-positives as FTC staff becomes invested in fishing expeditions and force such consent decrees regardless of the actual harms on consumers.⁸³ Other systemic costs of this process include increased discovery burdens on (even blameless) potential defendants, inefficiently large compliance expenditures throughout the economy, under experimentation and innovation by firms, doctrinally questionable consent orders, and a relative scarcity of judicial review of Commission enforcement decisions. Ultimately, this phenomena distorts the FTC’s consumer protection mission because the agency can self-select cases that are likely to settle and further its policy goals, rather than choosing cases on the basis of stopping the most nefarious actors and truly protecting consumers. As even former FTC Commissioner Joshua Wright noted, such self-serving personal and agency goals may push agencies to pursue cases “with the best prospect for settlement, cases that will consume few investigative resources, settle quickly, and are more likely to result in a consent decree that provides a continuing role for the agency.”⁸⁴ Thus, more than any other aspect of the FTC Act or the FTC’s operations, it is here that reinvigorated congressional oversight is needed.

The attached white paper explores this topic in great depth. Specifically, we recommend:

1. Reporting on how the agency uses CIDs⁸⁵
2. Making CIDs confidential by default and allowing companies to move to quash them confidentially.⁸⁶ Today, fighting an FTC subpoena means the FTC can make the fight public, which may have serious consequences for a company’s brand and stock price.
3. Requiring a greater role for Commissioners and economists in supervising the discovery process.⁸⁷

Ultimately, any examination of the FTC’s processes should start with arguably the most sacred principle in the American judicial system: innocent until proven guilty. As the Supreme Court made clear in 1895, “[t]he principle that there is a presumption of innocence in favor of the accused is the undoubted law, axiomatic and elementary, and its enforcement lies at the foundation of the administration of our criminal law.”⁸⁸ While it is inarguably true that these cases are very clearly not criminal, it is also true that these companies and their employees face the threat of losing their “life, liberty, and property” as a result of these actions, as evidenced by LabMD. Despite the Administrative Law Judge finding that “the evidence fails to show any computer hack for purpose of committing identity fraud,” the employees of LabMD were nonetheless left without employment simply due to “speculation” by the FTC—a word that appeared seventeen times in the ALJ’s decision.⁸⁹

Given the sensitive nature of both the type of information involved in these cases, including financial and health information, as well as consumers’ sensitivity to reports that their data may be in jeopardy, it is of the utmost importance that Congress ensure that innocent businesses’ reputations aren’t irreparably damaged simply due to “speculation.” To be clear: this is not to say that parties who are guilty of implementing nefarious practices should be protected from the court of public opinion. Indeed, as former Commissioner Wright alluded to, implementing processes that would, at the very least, require the FTC to plead its claims with specificity—and, ideally, subsequently prove it on the basis of data-driven standards—prior to dragging a companies’ name through the mud would actually ensure the FTC was

⁸² Darren Bush, *The Incentive and Ability of the Federal Trade Commission to Investigate Real Estate Markets: An Exercise in Political Economy*, 20–21, available at <http://www.antitrustinstitute.org/files/517c.pdf>.

⁸³ See Geoffrey A. Manne, R. Ben Sperry & Berin Szóka, *In the Matter of Nomi Technologies, Inc.: The Dark Side of the FTC’s Latest Feel-Good Case*, ICLE Antitrust & Consumer Protection Research Program White Paper 2015–1 (2015).

⁸⁴ D.H. Ginsburg & J.D. Wright, *Antitrust Settlements: The Culture of Consent*, in I. William E. Kovacic: *An Antitrust Tribute—Liber Amicorum* (Charbit *et al.*, eds., February 2013), https://www.ftc.gov/sites/default/files/documents/public_statements/antitrust-settlements-culture-consent/130228antitrustslmt.pdf.

⁸⁵ See White Paper, *supra* note 51, at 37–40.

⁸⁶ *Id.* at 46–48.

⁸⁷ *Id.* at 48–53.

⁸⁸ *Coffin v. United States*, 156 U.S. 432, 453 (1895).

⁸⁹ LabMD, Inc., No. 9357, 2015 WL 7575033, at *48 (MSNET Nov. 13, 2015), <https://causeofaction.org/wp-content/uploads/2015/11/Docket-9357-LabMD-Initial-Decison-electronic-version-pursuant-to-FTC-Rule-3-51c21.pdf>.

using its limited resources to *only* go after the worst actors, rather than merely those most likely to settle.

Requiring the FTC to first make a showing beyond “speculation” of harm it alleges before invoking its immensely broad investigatory power, would at least provide businesses and its employees with some level of protection before being labeled as having unsecure data practices and being forced to face the repercussions that inevitably come with such a label. In doing so, Congress would ensure one of the oldest maxims of law in democratic civilizations continues. As Roman Emperor Julian eloquently quipped in response to his fiercest adversary’s statement that “Oh, illustrious Caesar! if it is sufficient to deny, what hereafter will become of the guilty?”: “If it suffices to accuse, what will become of the innocent?”⁹⁰

G. Fencing-In Relief

The FTC has broad powers under Section 13(b) to include in consent decrees extraordinarily broad behavioral requirements that “fence in” the company in the future.⁹¹ The courts have been exceedingly deferential to the FTC in applying these requirements, though at least one circuit court has rebuked the FTC’s broad approach, as explained in the attached white paper.⁹² Rather than attempting to limit how the FTC uses its 13(b) powers, Congress should focus on when Section 13(b) applies. As Howard Beales, former director of the Bureau of Consumer Protection, has argued, regarding deception:

the Commission’s use of Section 13(b) remedies should be reevaluated in light of the law’s original purpose: [O]ne class of cases clearly improper for awarding redress under Section 13(b): traditional substantiation cases, which typically involve established businesses selling products with substantial value beyond the claims at issue and disputes over scientific details with well-regarded experts on both sides of the issue. In such cases, the defendant would not have known *ex ante* that its conduct was “dishonest or fraudulent.” Limiting the availability of consumer redress under Section 13(b) to cases consistent with the Section 19 standard strikes the balance Congress thought necessary and ensures that the FTC’s actions benefit those that it is their mission to protect: the general public.⁹³

The same logic goes for the kind of unfairness cases the FTC is bringing against high-tech companies, as Josh Wright noted in his dissent in the *Apple* product design case:

The economic consequences of the allegedly unfair act or practice in this case—a product design decision that benefits some consumers and harms others—also differ significantly from those in the Commission’s previous unfairness cases. The Commission commonly brings unfairness cases alleging failure to obtain express informed consent. These cases invariably involve conduct where the defendant has intentionally obscured the fact that consumers would be billed. Many of these cases involve unauthorized billing or cramming—the outright fraudulent use of payment information. Other cases involve conduct just shy of complete fraud—the consumer may have agreed to one transaction but the defendant charges the consumer for additional, improperly disclosed items. Under this scenario, the allegedly unfair act or practice injures consumers and does not provide economic value to consumers or competition. In such cases, the requirement to provide adequate disclosure itself does not cause significant harmful effects and can be satisfied at low cost. However, the particular facts of this case differ in several respects from the above scenario.⁹⁴

The key point, as Wright argued, is that the Commission is increasingly using unfairness not to punish obviously bad actors or to proscribe conduct that merits *per se* illegality because it is inherently bad, but rather, conduct that presents difficult tradeoffs: How long should consumers remain logged in to an apps store to balance the convenience of the vast majority of users with the possibility that some users with children may find that their children make unauthorized purchases on

⁹⁰ *Coffin v. United States*, 156 U.S. 432, 455 (1895).

⁹¹ See, e.g., *Kraft, Inc. v. F.T.C.*, 970 F.2d 311, 326 (7th Cir. 1992) (“The F.T.C. has discretion to issue multi-product orders, so called ‘fencing-in’ orders, that extend beyond violations of the Act to prevent violators from engaging in similar deceptive practices in the future.”) (citing *F.T.C. v. Colgate-Palmolive Co.*, 380 U.S. 374, 395 (1965)).

⁹² See White Paper, *supra* note 51, at 73–75.

⁹³ J. Howard Beales III & Timothy J. Muris, *Striking the Proper Balance: Redress Under Section 13(b) of the FTC Act*, 79 ANTITRUST L. J. 1, 6–7 (2013).

⁹⁴ Dissenting Statement of Commissioner Joshua D. Wright, In the Matter of Apple, Inc., FTC File No. 1123108, at 3 (Jan. 15, 2014), available at <https://goo.gl/ORCC9E>.

the device immediately after the parent has logged in? How much, and what kind of, data security is “reasonable?” And so on. These reflect business decisions that are inevitable in the modern economy. The Commission might well be justified in declaring that a company has struck the wrong balance, but it should not treat them exactly as it would obvious fraudsters, who set out to defraud consumers.

In order to deter the Commission from taking advantage of this frequent judicial deference by imposing such disconnected “fencing-in” remedies in non-fraud cases—which, of course, is compounded by the fact that most cases are never reviewed by courts at all—Congress should consider imposing some sort of minimal requirement that provisions in proposed orders and consent decrees be (i) reasonably related to challenged behavior, and (ii) no more onerous than necessary to correct or prevent the challenged violation.

H. Closing Letters

While consent decrees might help companies understand what the FTC will deem illegal on a case-by-case basis, in unique fact patterns, closing letters could do the inverse, telling companies what the FTC will deem *not* to be illegal, which is potentially far more useful in helping companies plan their conduct. In the past, the FTC issued at least a few closing letters with a meaningful degree of analysis of the practices at issue under the doctrinal framework of Section 5(n).⁹⁵ But in recent years, the FTC has markedly changes its approach, issuing fewer letters and writing those it did issue at a level of abstraction that offers little real guidance and even less analysis.⁹⁶

Rep. Brett Guthrie’s (R-KY) proposed CLEAR Act (H.R. 5109) would require the FTC to report annually to Congress on the status of its investigations, including the legal analysis supporting the FTC’s decision to close some investigations without action. This requirement would not require the Commission to identify its targets, thus preserving the anonymity of the firms in question.⁹⁷ Most importantly, the bill requires:

- (1) IN GENERAL.—The Commission shall, on an annual basis, submit a report to Congress on investigations with respect to unfair or deceptive acts or practices in or affecting commerce (within the meaning of subsection (a)(1)), detailing—
 - (A) the number of such investigations the Commission has commenced;
 - (B) the number of such investigations the Commission has closed with no official agency action;
 - (C) the disposition of such investigations, if such investigations have concluded and resulted in official agency action; and
 - (D) for each such investigation that was closed with no official agency action, a description sufficient to indicate the legal *and economic* analysis supporting the Commission’s decision not to continue such investigation, and the industry sectors of the entities subject to each such investigation.

This bill, with our proposed addition noted, would go a long way to improving the value of the FTC’s guidance. Indeed, such annual reporting could form annual addenda to guidance that the FTC issues in the guidance it provides on informational injury modeled on the Green Guides. Although the Green Guides themselves do not involve such reporting, it would make sense in this context, where the FTC is regularly confronted with far more novel fact patterns each year.

I. Re-opening Past Settlements

The FTC may, under its current rules, re-open past settlements at any time—subject only to the Commission’s assertion about what the “public interest” requires and after giving companies an opportunity to “show cause” why their settlements should *not* be modified.⁹⁸ By contrast, courts require far more for re-opening their

⁹⁵ *Id.* at 40–43. See, e.g., Letter from Joel Winston, Associate Director of Fed. Trade Comm’n to Michael E. Burke, Esq., Counsel to Dollar Tree Stores, Inc. (June 5, 2001) available at http://www.ftc.gov/sites/default/files/documents/closing_letters/dollar-tree-stores-inc./070605doltree.pdf.

⁹⁶ See, e.g., Letter from Maneesha Mithal, Associate Director of Fed. Trade Comm’n to Lisa J. Sotto, Counsel to Michael’s Stores, Inc. (June 5, 2001) available at http://www.ftc.gov/sites/default/files/documents/closing_letters/michaels-storesinc./120706michaelsstorescltr.pdf.

⁹⁷ The Clarifying Legality and Enforcement Action Reasoning Act, H.R. 5109, 114th Cong. (2016) [hereinafter CLEAR Act] available at <https://www.congress.gov/bill/114th-congress/house-bill/5109/text>.

⁹⁸ 16 C.F.R. 3.72(b).

orders. The FTC has, in fact, proposed to re-open four settlements entered into in 2013 under the Green Guides. Congress should write a meaningful standard by which the FTC should have to justify re-opening past settlements. If the Commission continues on its current course, it will be able to use its settlements to bypass the procedural safeguards of notice-and-comment rulemaking.

III. Reasonable Siblings: Background on Section 5 and Negligence

The FTC's enforcement authority is derived from Section 5 of the Federal Trade Commission Act (FTC Act), which declares unlawful "[u]nfair methods of competition in or affecting commerce" and "unfair or deceptive acts or practices in or affecting commerce."⁹⁹ Under the broad terms of Section 5, the FTC challenges "unfair methods of competition" through their antitrust division and "unfair or deceptive practices" through their consumer protection division.¹⁰⁰ In pursuing its consumer protection mission there are different standards for "unfair" and "deceptive" practices, with its unfairness authority being "the broadest portion of the Commission's statutory authority."¹⁰¹ Indeed, this "unfairness" authority was initially unrestrained by any statutory definition,¹⁰² and remained so until Congress added Section 5(n) in 1994. In addition to Section 5 authority, however, the FTC has also asserted violations of other statutes in its data security enforcement, most notably the Gramm-Leach-Bliley Act ("GLBA"),¹⁰³ Children's Online Privacy Protection Act ("COPPA"),¹⁰⁴ as well as regulations promulgated under those statutes.¹⁰⁵

Congress intentionally framed the FTC's authority under Section 5 in the general terms "unfair" and "deceptive" to ensure that the agency could protect consumers and competition throughout all trade and under changing circumstances.¹⁰⁶ To be sure, this broad authority has not been lost on the FTC, who readily acknowledges that "Congress intentionally framed the statute in general terms," which the agency interprets to mean "[t]he task of identifying unfair methods of competition" as being "assigned to the Commission."¹⁰⁷ Despite the addition of Section 5(n) to the Act in 1994 to *require* cost-benefit analysis, this lack of clear statutory guidance as to what constitutes "unfair" proved to be problematic, with at least one Commissioner recently recognizing that "nearly one hundred years after the agency's creation, the Commission has still not articulated what constitutes . . . unfair . . . leaving many wondering whether the Commission's Section 5 authority actually has any meaningful limits."¹⁰⁸ Commissioner Wright was referring to a lack of clarity around the meaning of unfairness in competition cases, but his point holds more generally.

Given the broad nature of Section 5, few industries are beyond the FTC's reach and the FTC has met the broad statutory language with an equally broad exercise

⁹⁹ 15 U.S.C.A. § 45 (West 2017).

¹⁰⁰ See generally Justin (Gus) Hurwitz, *Data Security and the FTC's Uncommon Law*, 101 Iowa L. Rev. 955, 964 (2016) (discussing in great lengths the FTC's "common law" approach) [hereinafter Hurwitz, *Uncommon Law*].

¹⁰¹ *Id.*

¹⁰² See *Id.*; see also Statement of Basis and Purpose of Trade Regulation Rule 408, Unfair or Deceptive Advertising and Labeling of Cigarettes in Relation to the Health Hazards of Smoking, 29 Fed. Reg. 8324, 8355 (July 2, 1964) (setting the three-factor contours of the "unfairness" prong for the first time through application of Section 5 to cigarette advertisements).

¹⁰³ See Gramm-Leach-Bliley Act, 15 U.S.C. § 6801 *et seq.* (2012) ("It is the policy of the Congress that each financial institution has an affirmative and continuing obligation to . . . protect the security and confidentiality of . . . customers' nonpublic personal information.").

¹⁰⁴ The Child Online Privacy Protection Act of 1998, 15 U.S.C. § 6501, *et seq.* (1994 & Supp. IV 1998) (making it unlawful under § 6502(a)(1) "for an operator of a website or online service directed to children . . . to collect personal information from a child in a manner that violates the regulations prescribed under subsection (b) of this section."); see also Melanie L. Hersh, *Is COPPA A Cop Out? The Child Online Privacy Protection Act As Proof That Parents, Not Government, Should Be Protecting Children's Interests on the Internet*, 28 Fordham Urb. L.J. 1831, 1878 (2001) (detailing how the FTC uses COPPA to regulate data security for children).

¹⁰⁵ See, e.g., FTC Final Rule, 16 C.F.R. §§ 313.10–313.12 (2000); *Individual Reference Servs. Grp., Inc. v. F.T.C.*, 145 F. Supp. 2d 6, 20 (D.D.C. 2001), *aff'd sub nom. Trans Union LLC v. F.T.C.*, 295 F.3d 42 (D.C. Cir. 2002) (holding that the FTC's final rule, promulgated under the GLBA "did not contravene plain meaning of Act and were permissible construction of that legislation" and "agencies' action in promulgating final rules was not arbitrary and capricious").

¹⁰⁶ See H.R. REP. NO. 63–1142, at 19 (1914) (Conf. Rep.) (observing if Congress "were to adopt the method of definition, it would undertake an endless task").

¹⁰⁷ Joshua D. Wright, Commissioner, Federal Trade Comm'n, Section 5 Recast: Defining the Federal Trade Commission's Unfair Methods of Competition Authority at the Executive Committee Meeting of the New York State Bar Association's Antitrust Section, 2 (June 19, 2013), available at https://www.ftc.gov/sites/default/files/documents/public_statements/section-5-recast-defining-federal-trade-commissions-unfair-methods-competition-authority/130619section5recast.pdf.

¹⁰⁸ *Id.*

of its authority to enforce Section 5.¹⁰⁹ The FTC has brought data security and privacy actions against advertising companies, financial institutions, health care companies, and, perhaps most significantly, companies engaged in providing data security products and services.¹¹⁰ Further, not only are companies responsible for safeguarding their own data, but the FTC has also alleged that companies are responsible for any data security failings of their third-party clients and vendors, too.¹¹¹

Companies who are the victims of such cyber-attacks are victims themselves. They suffer immense financial losses, stemming largely from reputational damage as customers are fearful of remaining loyal to companies who can't protect their personal and financial information.¹¹² According to one study, 76 percent of customers surveyed said they "would move away from companies with a high record of data breaches," with 90 percent responding that "there are apps and websites that pose risks to the protection and security of their personal information."¹¹³ Unquestionably, data security is the cornerstone of the digital economy and digitization of the physical economy. As Naveen Menon, President of Cisco Systems for Southeast Asia, put it "[s]ecurity is what protects businesses, allowing them to innovate, build new products and services."¹¹⁴

The recent Equifax breach illustrates just how strongly reputational forces encourage companies to invest in data security. As of the time this testimony was being written, Equifax's post-hack stock had plummeted 30 percent.¹¹⁵ Given the enormous stakes for companies' brands, it is not difficult to understand why—with no clear guidance from Congress or the FTC—companies have opted to settle and enter into consent decrees rather than risk further reputational damage and customer loss through embarrassing and costly litigation.¹¹⁶ Out of approximately 60 data security enforcement actions, only two defendants dared face an FTC armed with near absolute discretion as to the interpretation of "reasonable" data security practices. This hesitation to challenge the FTC in order to gain clarity from the courts about what actually constitutes unreasonable practices—in addition to the more obvious reason of escaping liability—was only reinforced by the *LabMD* case, where the company's decision to litigate against the FTC rather than enter into a consent decree led to its demise.¹¹⁷

Data security poses a unique challenge: unlike other unfairness cases, the company at issue is both the victim (of data breaches) and the culprit (for allegedly having inadequate data security). In such circumstances, the FTC should apply unfairness as more of a negligence standard than strict liability. Consider both a company that has been hacked and a business owner whose business has burned down. In both situations, it is very likely that employees and customers lost items they consider to be precious—perhaps even irreplaceable. Additionally, it is equally likely that neither *wanted* this unfortunate event to occur. Finally, in both situations, prosecutors would investigate the accident to determine the cause and assess the damage and costs. However, under the FTC's current approach to Section 5 enforcement, how each business owner would be judged for liability purposes would vary greatly despite these similarities.

¹⁰⁹ See Cho & Caplan, *Cybersecurity Lessons*; Stuart L. Pardo & Blake Edwards, The FTC, the Unfairness Doctrine, and Privacy by Design: New Legal Frontiers in Cybersecurity 12 J. Bus. & Tech. L. 227, 232 (2017) (discussing the FTC's enforcement of "everything from funeral homes, vending machine companies, telemarketing and mail marketing schemes, credit reporting, and the healthcare industry.") [hereinafter Pardo & Edwards, *New Legal Frontiers*].

¹¹⁰ See Fed. Trade Comm'n, 2016 Privacy & Data Security Update (Jan. 2017), <https://www.ftc.gov/reports/privacy-data-security-update-2016> (providing overview of various enforcement actions).

¹¹¹ See *id.* (For example, the consent decree agreed to in the FTC's enforcement action against Ashley Madison required the defendants to implement a comprehensive data-security program, including third-party assessments).

¹¹² See generally PONEMON, DATA BREACH; see also *Data breaches cost U.S. businesses an average of \$7 million—here's the breakdown*, Business Insider (April 27, 2017), <http://www.businessinsider.com/sc/data-breaches-cost-us-businesses-7-million-2017-4> (providing that the average cost of a data security breach is \$7 million, with 76 percent of customers saying they would move away from companies with a high record of data breaches).

¹¹³ See VANSONBOURNE, DATA BREACHES AND CUSTOMER LOYALTY REPORT (2015), <http://www.vanson-bourne.com/client-research/18091501JD>.

¹¹⁴ Naveen Menon, *There can be no digital economy without security*, World Economic Forum (May 8, 2017), <https://www.weforum.org/agenda/2017/05/there-can-be-no-digital-economy-without-security/>.

¹¹⁵ See, e.g., *Equifax Plummets After Huge Data Breach, Kroger Sinks on Profit drop, American Outdoor Brand Falls*, Yahoo Finance, Sept. 8, 2017, <https://finance.yahoo.com/news/equifax-plummets-huge-data-breach-kroger-sinks-profit-drop-american-outdoor-brands-falls-144654294.html>.

¹¹⁶ *Id.*

¹¹⁷ *Id.*

Under the common law of torts, absent some criminal intent (*e.g.*, insurance fraud) the businessman whose office burned down would only be held liable if he acted negligent in some way. At common law, negligence involves either an act that a *reasonable* person would know creates an unreasonable risk of harm to others.¹¹⁸ Should a prosecutor or third party bring a lawsuit against the business owner, they would be required to put forth expert testimony and a detailed analysis showing exactly *how* and *why* the owner's negligence caused the fire.

Conversely, despite all of the FTC's rhetoric about "reasonableness"—which, as one might "reasonably" expect, should theoretically resemble a negligence-like framework—the FTC's approach to assessing whether a data security practice is unfair under Section 5 actually more closely resembles a rule of strict liability.¹¹⁹ Indeed, rather than conduct any analysis showing that (1) the company owed a duty to consumers and (2) *how* that the company's breach of that duty was the cause of the breach—either directly or proximately—which injured the consumer, instead, as one judge noted, the FTC "kind of take them as they come and decide whether somebody's practices were or were not within what's permissible from your eyes."¹²⁰

There is no level of prudence that can avert *every* foreseeable harm. A crucial underpinning of calculating liability in civil suits is that some accidents are unforeseeable, some damages fall out of the chain of causation, and mitigation does not always equal complete prevention. Thus our civil jurisprudence acknowledges that no amount of care can prevent *all* accidents (fires, car crashes, *etc.*), or at least the standard of care required to achieve an accident rate near zero would be wildly disproportionate, paternalistic, and unrealistic to real-world applications (*e.g.*, setting the speed limit at 5 mph).

The chaos theory also applies to the unpredictability of data breaches. Thus, if the FTC wants to regulate data security using a "common law" approach, then it must be willing to accept that certain breaches are inevitable and liability should only arise where the company was truly negligent. This is not simply a policy argument; it is the weighing of costs and benefits that Section 5(n) requires—at least in theory. Companies do not want to be hacked any more than homeowners want their houses to burn down. The FTC should begin its analysis of data security cases with that incentive in mind, and ask whether the company has acted as a "reasonably prudent person" would.

This, then, presents the key question: what constitutes "reasonably prudent" data security and privacy practices for purposes of avoiding liability under Section 5? To help inform Congress—and, in turn, the FTC—on how to go about answering this question, the remainder of this testimony will focus on determining three key elements of this question: (1) the types of injuries that should merit the FTC's attention, (2) the analytical framework, built upon empirical research and investigations, which should determine what constitutes "reasonable," and (3) the pleading requirements to determine the specificity with which the FTC must state its claim in the first instance.

IV. Informational Injuries In Practice: Data Security & Privacy Enforcement to Date

In 2005, the FTC brought its first data security case premised solely on unfairness—against a company (BJ's Warehouse) not for violating the promises it had made to consumers, but for the underlying adequacy of its data security practices.¹²¹ Whether this was a proper use of Section 5 is not the important question—although it is essential to note that *BJ's Warehouse* was the consent decree that launched the FTC's use of unfairness for data security a thousand² more (or closer to "hundreds" in the context of privacy and data security). Even if one stipulates that the FTC could have, and likely *would* have, prevailed on the merits, had the case gone to trial, the important question is this: how might the Commission have changed its approach to data security? That question becomes even more salient if one tries to project back, asking what the Commission should have done then if it had known what we know today: that twelve years later, we would still not have

¹¹⁸ See Restatement (Second) of Torts §284 (1965).

¹¹⁹ See Geoffrey A. Manne & Kristian Stout, *When "Reasonable" Isn't: The FTC's Standard-Less Data Security Standard*, Journal of Law, Economics and Policy, Forthcoming (Aug. 31, 2017), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3041533.

¹²⁰ Transcript of Proceedings at 91, 94–95, LabMD, Inc. v. Fed. Trade Comm'n, No. 1:14-CV-810-WSD, 2014 WL 1908716 (N.D. Ga. May 7, 2014).

¹²¹ Fed. Trade Comm'n, *BJ's Wholesale Club Settles FTC Charges* (June 16, 2005), available at <https://www.ftc.gov/news-events/press-releases/2005/06/bjs-wholesale-club-settles-ftc-charges>.

a single tech-related unfairness case resolved on the merits (and only four that had made it to Federal court).¹²²

The Commission had, of course, asked Congress for comprehensive privacy legislation in 2000.¹²³ Besides asking again, what else could the Commission have done? It could have begun a rulemaking under the Magnusson-Moss Act of 1975, subject to the procedural safeguards imposed by Congress in 1980 (after the FTC's abuse of its rulemaking powers in the intervening five years). But, as many have noted, it would be difficult to craft prescriptive rules for data security or privacy in any rulemaking, and the process would have taken several years.

There *was* a third way: the FTC could have sought public comment on the issues of data security and privacy, issued a guidance document, then repeated the process every few years to update the agency's guidance to reflect current risks, technologies, and trade-offs. In short, the Commission could have followed the model established by its Green Guides.

V. The Green Guides as Model for Empirically Driven Guidance

As the FTC proceeds with Chairman Ohlhausen's plans for a workshop on "informational injuries," it should consider its own experience with the Green Guides as a model. The parallel is not exact: the Guides focus entirely on deception, and primarily on consumer expectations, while the FTC's proposed "informational injuries" would involve both deception and unfairness. However, the Guides do still delve into substantiation of environmental marketing claims, and, thus, the underlying merits of what companies were promising their customers. FTC guidance on the meaning of "informational injuries" in the context of data security and privacy would necessarily cover wider ground, ultimately attempting to understand harms as well as "reasonable" industry practices under both deception and unfairness prongs. Still, the Guides emphasis on empirical substantiation would serve the FTC well in attempting to provide a clearer analytical basis for *why* a practice or action is deemed to have caused "informational injury" in certain cases, rather than merely stating *what* practices the FTC has determined likely to cause such harm.

Though court guidance in this context may seem rarer than the birth of a giant panda, the Third Circuit nonetheless provided some insight into the value of previous FTC guidance—namely the FTC's 2007 guidebook titled "Protecting Personal Information: A Guide for Business,"—in understanding harms and "reasonable" practices that constitute violations of Section 5.¹²⁴ Discussing this guidebook, which "describes a 'checklist[]' of practices that form a 'sound data security plan,'" the court notably found that, because "[t]he guidebook does not state that any particular practice is required by [Section 5]," it, therefore, "could not, on its own, provide 'ascertainable' certainty" of the FTC's interpretation of what specific cybersecurity practices fail [Section 5].¹²⁵ Despite this recognition, the court still noted that the guidebook did "counsel against many of the specific practices" alleged in that specific case, and thus, provided sufficient guidance in that very narrow holding to inform the defendant of "what" conduct was not considered reasonable.¹²⁶ Specifically, the court noted that the guidebook recommended:

[T]hat companies "consider encrypting sensitive information that is stored on [a] computer network . . . [, c]heck . . . software vendors' websites regularly for alerts about new vulnerabilities, and implement policies for installing vendor-approved patches." It recommends using "a firewall to protect [a] computer from hacker attacks while it is connected to the Internet," deciding "whether [to] install a 'border' firewall where [a] network connects to the Internet," and setting access controls that "determine who gets through the firewall and what they will be allowed to see . . . to allow only trusted employees with a legitimate business need to access the network." It recommends "requiring that employees use 'strong' passwords" and cautions that "[h]ackers will first try words like . . . the software's default password[] and other easy-to-guess choices." And it recommends implementing a "breach response plan," *id.* at 16, which includes

¹²² See *Fed. Trade Comm'n v. D-Link Sys., Inc.*, No. 3:17-CV-00039-JD, 2017 WL 4150873, at *1 (N.D. Cal. Sept. 19, 2017); *Fed. Trade Comm'n v. Wyndham Worldwide Corp.*, 799 F.3d 236, 253 (3d Cir. 2015); *LabMD, Inc. v. F.T.C.*, No. 1:14-CV-00810-WSD, 2014 WL 1908716, at *1 (N.D. Ga. May 12, 2014), *aff'd*, 776 F.3d 1275 (11th Cir. 2015); *F.T.C. v. Amazon.com, Inc.*, 71 F. Supp. 3d 1158 (W.D. Wash. 2014).

¹²³ Fed. Trade Comm'n, *Privacy Online: Fair Information Practices in the Electronic Market Place—A Report to Congress* (2000) [hereinafter Privacy Report].

¹²⁴ *Wyndham*, 799 F.3d at 256.

¹²⁵ *Id.* at 256 n.21.

¹²⁶ *Id.* at 256–57.

“[i]nvestigat[ing] security incidents immediately and tak[ing] steps to close off existing vulnerabilities or threats to personal information.”¹²⁷

Most notably, nowhere in the court’s discussion did it identify a single instance of the FTC explaining *why* a certain practice is necessary or reasonable; instead the FTC had merely asserted that companies should just accept the FTC’s suggestions, without any consideration or analysis as to whether the immense costs that might be associated with implementing many of these practices are in the consumers’ best interest. This is far from the weighing of costs and benefits that Section 5(n) requires. By comparison, the Green Guides, while focused on deception, reflect a deep empiricism about substantiation of environmental marketing claims, informed by a notice and comment process and distilled into clear guidance accompanied by detailed analysis.

While multi-national corporations such as Wyndham *might* (arguably) possess the resources to blindly implement any and all suggestions the FTC makes, and to follow the FTC’s pronouncements in each consent decree, the economic principle of scarcity will inevitably require smaller businesses with vastly fewer resources to make difficult decisions as to which practices they should utilize to provide the greatest security possible with its limited resources. For example, using the list above, would a company with limited resources be acting “reasonable” if it implemented a “breach response plan,” but failed to check *every* software vendors’ website regularly for alerts? Further, would a company be engaging in “deceptive” practices if it failed to notify customers that, due to limited resources, it could only implement half of the FTC’s recommended practices? The answer to these questions matter and will undoubtedly have significant consequences on how competitive small businesses remain in this country. As mentioned earlier, one study suggests that 76 percent of customers “would move away from companies with a high record of data breaches,” with 90 percent responding that “there are apps and websites that pose risks to the protection and security of their personal information.”¹²⁸ This shows that consumers are understandably concerned about how well a company protects their data. If a company is essentially required to choose between admitting that it lacks the resources to implement advanced security practices on par with large, established businesses, or risk an FTC action for “deception,” how can any startup or small business expect to compete and grow in these polarizing circumstances?

Under the FTC’s current enforcement standards, this all shows how easily small businesses may find themselves in a catch-22. On the one hand, if the business wishes to pretend it has the resources to implement the same data security standards as multi-national corporations in order to attract and maintain customers weary of their data being hacked, the business will be acting “deceptively” in the eyes of the FTC, and will be open to the costly litigation, reputational damage, and massive fines that come with it. On the other hand, if the small business wishes to be open and readily admit that, due to resource constraints, its data security practices are anemic when compared to multi-national corporations, it will be open to the loss of customers and businesses invariably linked to such claims. As this illustrates, how can any startup or small business expect to compete without the FTC providing guidance as to best practices based on empirical research—including economies of scale?

Thus, to ensure the ability of businesses to compete and make sound decisions as to the allocation of their finite resources, it is imperative that the FTC not only endeavor to provide guidance as to *what* practices are sound, but also explain *why* such practices are necessary, as well as “how much” is necessary, especially in relation to a business’s size and available resources.

A. *The Green Guides (1992–2012)*

First published in 1992, the Guides represented the Commission’s attempt to better understand a novel issue before jumping in to case-by-case enforcement. By 1991, it was becoming increasingly common for companies to tout the environmental benefits of their products. In some ways, these claims were no different from traditional marketing claims: the FTC’s job was to make sure consumers “got the benefit of the bargain.” But in other ways, it was less clear exactly what that “benefit” was—such as regarding recycling content, recyclability, compostability, biodegradability, refillability, sourcing of products, etc. Rather than asserting how much of each of these consumers *should* get, the Commission sought to ground its understanding of these concepts in empirical data about what consumers actually ex-

¹²⁷ *Id.* (internal citations omitted).

¹²⁸ See VANSONBOURNE, DATA BREACHES AND CUSTOMER LOYALTY REPORT (2015), <http://www.vanson-bourne.com/client-research/18091501JD>.

pected. As the Commission summarized its approach in the Statement of Basis and Purpose for the 2012 update:

The Commission issued the Guides to help marketers avoid making deceptive claims under Section 5 of the FTC Act. Under Section 5, a claim is deceptive if it likely misleads reasonable consumers. Because the Guides are based on how consumers reasonably interpret claims, consumer perception data provides the best evidence upon which to formulate guidance. As EPA observed, however, perceptions can change over time. The Guides, as administrative interpretations of Section 5, are inherently flexible and can accommodate evolving consumer perceptions. Thus, if a marketer can substantiate that consumers purchasing its product interpret a claim differently than what the Guides provide, its claims comply with the law.¹²⁹

Of course, as the Deception Policy Statement notes, “If the representation or practice affects or is directed primarily to a particular group, the Commission examines reasonableness from the perspective of that group.”¹³⁰ Thus, the Commission immediately added the following:

the Green Guides are based on marketing to a general audience. However, when a marketer targets a particular segment of consumers, such as those who are particularly knowledgeable about the environment, the Commission will examine how reasonable members of that group interpret the advertisement. The Commission adds language in Section 260.1(d) of the Guides to emphasize this point. Marketers, nevertheless, should be aware that more sophisticated consumers may not view claims differently than less sophisticated consumers. In fact, the Commission’s study yielded comparable results for both groups.¹³¹

This bears emphasis because many speak of privacy-sensitive consumers as a separate market segment, and argue that we should apply deception in privacy cases based upon their expectations. But here, unlike in privacy, the Commission actually undertook empirical research—which turned not to support an idea that probably seemed intuitively obvious: that more environmentally knowledgeable or “conscious” consumers had different interpretation of environmental marketing claims.

The Commission issued the first Green Guides in August 1992, thirteen months after two days of public hearings, including a 90-day public comment period in between. The Commission followed this process in issuing revised Green Guides in 1996, 1998, and 2012. So detailed was the Commission’s analysis, across so many different fact patterns, that, while the 2012 Guides ran a mere 12 pages in the Federal Register,¹³² the Statement of Basis and Purpose for them ran a staggering 314 pages.¹³³ In each update, the FTC explored how the previous version of the Guides addresses each, the FTC’s proposal, comments received on the proposal and justification for the final rule. In short, the FTC was doing something a lot like rule-making. Except, of course, the Guides are not themselves legally binding.

The FTC has never done anything even resembling this type of comprehensive guide for data security or privacy. Indeed, just this year, the FTC touted “a series of blog posts” as a grand accomplishment in the FTC’s “ongoing efforts to help businesses ensure they are taking reasonable steps to protect and secure consumer data.”¹³⁴ The FTC has regularly trumpeted its 2012 Privacy Report, but that document does something very different. Most notably, the Report calls on industry actors to self-police in the most general of terms, making statements like “to the extent that strong privacy codes are developed, the Commission will view adherence to such codes favorably in connection with its law enforcement work.”¹³⁵ Unlike the

¹²⁹ Fed Trade Comm’n, Statement of Basis and Purpose (2012 Update), at 24–25, <https://www.ftc.gov/sites/default/files/attachments/press-releases/ftc-issues-revised-green-guides/green-guidesstatement.pdf> [hereinafter “Statement of Basis and Purpose”].

¹³⁰ Fed. Trade Comm’n, FTC Policy Statement on Deception (Oct. 14, 1983), at 1, https://www.ftc.gov/system/files/documents/public_statements/410531/831014deceptionstmt.pdf.

¹³¹ See Statement of Basis and Purpose, at 25.

¹³² 16 C.F.R. 260 (2012).

¹³³ See generally note 129.

¹³⁴ Press Release, Fed. Trade Comm’n, Stick with Security: FTC to Provide Additional Insights on Reasonable Data Security Practices (July 21, 2017), <https://www.ftc.gov/news-events/press-releases/2017/07/stick-security-ftc-provide-additional-insights-reasonable-data>.

¹³⁵ Fed. Trade Comm’n, *Protecting Consumer Privacy in an Era of Rapid Change: Recommendations for Businesses and Policymakers* (March 2012), at 73, <https://www.ftc.gov/sites/default/files/documents/reports/federal-trade-commission-report-protecting-consumer-privacy->

focus on substance and comprehensiveness of the Green Guides, the 2012 Privacy Report speaks in generalities, dictating “areas where the FTC will be active,” such as in monitoring Do Not Track implementation or promoting enforceable self-regulatory codes.¹³⁶ The lack of a Statement of Basis and Purpose akin to that issued in updating the Green Guides (the 2012 Statement totaled a whopping 314 pages) introduces unpredictability into the enforcement process, and chills industry action on data security and privacy.

In all, the Green Guides offer a clear, workable model for how the FTC could provide empirically grounded guidance on data security and privacy—even without any action by Congress. The key steps in issuing such guidance would be:

1. Study current industry practices across a wide range of businesses;
2. Gather data on consumer *expectations*, rather than making assumptions about consumer preferences;
3. Engage the Bureau of Economics and the FTC’s growing team of in-house technologists in analysis of the costs and benefits of practice; and
4. Issue (at least) biennial or triennial guidance to reflect the changing nature, degree, and applicability of data security and privacy regulations.

Short of rulemaking, this rulemaking-like approach offers the most clarity, comprehensibility, and predictability for both FTC enforcement staff and industry actors.

B. What the Commission Said in 2012 about Modifying the Guides

There is an obvious tension between conducting thorough empirical assessments to inform updating Commission guidance and how often that guidance can be updated: the more regular the update, the more difficult it will be for the Commission to maintain methodological rigor in justifying that update. The 2012 Statement of Basis and Purpose noted requests that the Commission review and update the Guides every two or three years, but concluded:

Given the comprehensive scope of the review process, the Commission cannot commit to conducting a full-scale review of the Guides more frequently than every ten years. The Commission, however, need not wait ten years to review particular sections of the Guides if it has reason to believe changes are appropriate. For example, the Commission can accelerate the scheduled review to address significant changes in the marketplace, such as a substantial change in consumer perception or emerging environmental claims. When that happens, interested parties may contact the Commission or file petitions to modify the Guides pursuant to the Commission’s general procedures.¹³⁷

This strikes a sensible balance. Unfortunately, this is not at all how the Commission has handled modification of the 2012 Green Guides. Within a year, the FTC would modify the Green guides substantially with no such process for empirical substantiation to justify the new change. And this year, not five years after the issuance of the Guides, it modified the Guides yet again.

VI. Eroding the Green Guides and their Empirical Approach

While the Green Guides offer a model for empirically grounded consumer protection, the Commission has gradually moved away from that approach since issuing its last update to the Green Guides in 2012—following an approach that more closely resembles its approach to data security and privacy.

A. Modification of the Green Guides by Policy Statement (2013)

In 2013, FTC issued an enforcement policy statement clarifying how it would apply the Green Guides,¹³⁸ updated just the year after taking notice-and-comment, to architectural coatings such as paint. The Commission appended this Policy Statement onto its settlement with PPG Architectural Finishes, Inc. (“PPG”) and The Sherwin-Williams Company (“Sherwin-Williams”) to settle alleged violations of Section 5 for marketing paints as being “Free” of Volatile Organic Compounds

era-rapid-change-recommendations/120326privacyreport.pdf. [hereinafter “2012 Privacy Report”].

¹³⁶ *Id.* at 72.

¹³⁷ See Statement of Basis and Purpose, at 26–27.

¹³⁸ Fed. Trade Comm’n, Enforcement Policy Statement Regarding VOC-Free Claims for Architectural Coatings (Mar. 6, 2013), <https://www.ftc.gov/sites/default/files/documents/cases/2013/03/130306ppgpolicystatement.pdf>.

(VOCs).¹³⁹ Specifically, the Policy Statement focused on application of the 2012 Green Guides’ trace-amount test, which provided:

Depending on the context, a free-of or does-not-contain claim is appropriate even for a product, package, or service that contains or uses a trace amount of a substance if: (1) the level of the specified substance is no more than that which would be found as an acknowledged trace contaminant or background level; (2) the substance’s presence does not cause material harm that consumers typically associate with that substance; and (3) the substance has not been added intentionally to the product.¹⁴⁰

The Policy Statement made two clarifications specific to architectural coatings:

First, the “material harm” prong specifically includes harm to the environment and human health. This refinement acknowledges that consumers find both the environmental and health effects of VOCs material in evaluating VOC-free claims for architectural coatings.

Second, the orders define “trace level” as the background level of VOCs in the ambient air, as opposed to the level at which the VOCs in the paint would be considered “an acknowledged trace contaminant.” The harm consumers associate with VOCs in coatings is caused by emissions following application. Thus measuring the impact on background levels of VOCs in the ambient air aligns with consumer expectations about VOC-free claims for coatings.¹⁴¹

In both respects, the Policy Statement amended the Green Guides—while purporting merely to mirror the Guides. Most notably, the Guides had always been grounded in claims about environmental harms. For example, the Statement of Basis and Purpose for the 2012 Update had said:

In this context [the “free of” section of the Guides], the Commission reminds marketers that although *the Guides provide information on making truthful environmental claims*, marketers should be cognizant that consumers may seek out free-of claims for non-environmental reasons. For example, as multiple commenters stated, chemically sensitive consumers may be particularly likely to seek out products with free-of claims, and risk the most grievous injury from deceptive claims.¹⁴²

But now the FTC’s enforcement framework would, for the first time, focus on “human health” as well. In principle, this is perfectly appropriate: after all, “Unjustified consumer injury is the primary focus of the FTC Act,” as the Unfairness Policy Statement reminds us.¹⁴³ But note that the Commission was *not* bringing an unfairness claim—which would have required satisfying the cost-benefit analysis of Section 5(n). Instead, the Commission was bringing a pure deception claim, as with any Green Guides claim. But unlike deception cases brought under the Green Guides, the Commission provided none of the kind of empirical evidence about how consumers understood green marketing claims that had informed the Green Guides. The Commission did not seek public comment on this proposed enforcement policy statement, nor did it supply any such evidence of its own.

In short, the 2013 Policy Statement represented not merely a *de facto* amendment of the Green Guides, undermining the precedential value of the Guides and of all other FTC guidance documents, but a break with the empirical approach by which the FTC had developed the Guides since 1992. This alone should call into question the FTC’s willingness, in recent years, to ground consumer protection work in empirical analysis. But worse was yet to come.

B. Modification of the Green Guides by Re-Opening Consent Decree (2017)

This July, Ohlhausen, now Acting Chairwoman, effectively proposed amending the FTC’s Green Guides—first issued in 1992 and updated in 1996, 1998 and 2012—via proposed consent orders issued to four paint companies accused of deceptively promoting emission-free or zero volatile organic compounds in violation of Section

¹³⁹ Press Release, Fed. Trade Comm’n, FTC Approves Final Orders Settling Charges Against The Sherwin-Williams Co. and PPG Architectural Finishes, Inc.; Issues Enforcement Policy Statement on “Zero VOC” Paint Claims (Mar. 6, 2013), <https://www.ftc.gov/news-events/press-releases/2013/03/ftc-approves-final-orders-settling-charges-against-sherwin>.

¹⁴⁰ 16 C.F.R. § 260.9(c) (2012).

¹⁴¹ Fed. Trade Comm’n, Enforcement Policy Statement Regarding VOC-Free Claims for Architectural Coatings, at 2, https://www.ftc.gov/sites/default/files/documents/public_statements/voc-free-claims-architectural-coatings/130306ppgpolicystatement.pdf.

¹⁴² See Statement of Basis and Purpose, at 138 n. 469.

¹⁴³ 1980 Unfairness Policy Statement.

5 of the FTC Act.¹⁴⁴ In the corresponding press release, the Commission said it plans to “propose harmonizing changes to two earlier consent orders issued in the similar PPG Architectural Finishes, Inc. (Docket No. C-4385) and the Sherwin Williams Company (Docket No. C-4386) matters,” and plans to “issue orders to show cause why those matters should not be modified pursuant to Section 3.72(b) of the Commission Rules of Practice, 16 C.F.R. 3.72(b),” if the consent orders are finalized.¹⁴⁵

This repeated, and compounded, the two sins committed by the FTC in 2013: (1) undermining the value of Commission guidance (here, both the 2012 Guides and the 2013 Enforcement Policy Statement) by reminding all affected parties that guidance provided one day can be changed or revoked the next and (2) failing to provide empirical substantiation for its new approach. To these sins, the Commission added two more: (3) revoking guidance that had been treated as authoritative, and relied upon, by regulated parties for the previous four years through a consent decree and (4) re-opening the two consent decrees to which the 2013 Enforcement policy was attached to “harmonize” them with the FTC’s new approach. Revoking guidance treated as authoritative raises fundamental constitutional concerns about “fair notice.” Re-opening consent decrees raises even more serious concerns about the FTC’s process.

These concerns are reflected in recently proposed FTC settlements. In the 2013 PPG and Sherwin-Williams consent orders, the Commission specified the scope of its jurisdiction in Article II of the orders, stating:

IT IS FURTHER ORDERED that respondent, directly or through any corporation, subsidiary, division, trade name, or other device, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of any covered product in or affecting commerce, shall not make any representation, in any manner, expressly or by implication, regarding:

A. The VOC level of such product; or

B. Any other *environmental* benefit or attribute of such product,

unless the representation is true, not misleading, and, at the time it is made, respondent possesses and relies upon competent and reliable scientific evidence that substantiates the representation.¹⁴⁶

In the same orders, the Commission defined “trace” levels of VOCs as including a “human health” component, stating:

7. “Trace” level of VOCs shall mean:

A. VOCs have not been intentionally added to the product;

B. The presence of VOCs at that level does not cause material harm that consumers typically associate with VOCs, including but not limited to, harm to the environment or *human health*; and

C. The presence of VOCs at that level does not result in concentrations higher than would be found at background levels in the ambient air.¹⁴⁷

of language that specified health as a VOC-related hazard created no immediate substantive changes, it laid the groundwork for a broadening of what constitutes a legitimate claim under the definition of VOC. Specifically, this would mean that the FTC would only have to take one additional step to claim a VOC-related violation if a company did not meet some broad, amorphous standard of “human health” conceived by the FTC. In fact, the 2017 Benjamin & Moore Co., Inc., ICP Construction Inc., YOLO Colorhouse LLC, and Imperial Paints, LLC consent orders took this additional step in an updated Article II, stating:

IT IS FURTHER ORDERED that Respondent . . . must not make any representation, expressly or by implication . . . regarding:

A. The emission of the covered product;

¹⁴⁴Press Release, Fed. Trade Comm’n, Paint Companies Settle FTC Charges That They Misled Consumers; Claimed Products Are Emission- and VOC-free and Safe for Babies and other Sensitive Populations, (July 11, 2017), available at <https://www.ftc.gov/news-events/press-releases/2017/07/paint-companies-settle-ftc-charges-they-misled-consumers-claimed>.

¹⁴⁵*Id.* at ¶ 13.

¹⁴⁶Fed. Trade Comm’n, *In the Matter of PPG Architectural Finishes, Inc.*, Agreement Containing Consent Order (Oct. 25, 2012), at 4, <https://www.ftc.gov/sites/default/files/documents/cases/2012/10/121025ppgagree.pdf>; see also Fed. Trade Comm’n, *In the Matter of Sherwin-Williams Company*, Agreement Containing Consent Order (Oct. 25, 2012), at 4, <https://www.ftc.gov/sites/default/files/documents/cases/2012/10/121025sherwinwilliamsagree.pdf>.

¹⁴⁷*Id.* at 3.

- B. The VOC level of the covered product;
- C. The odor of the covered product;
- D. Any other health benefit or attribute of, or risk associated with exposure to, the covered product, including those related to VOC, emission, or chemical composition; or
- E. Any other environmental benefit or attribute of the covered product, including those related to VOC, emission, or chemical composition, unless the representation is non-misleading, including that, at the time such representation is made, Respondent possesses and relies upon competent and reliable scientific evidence that is sufficient in quality and quantity based on standards generally accepted in the relevant scientific fields, when considered in light of the entire body of relevant and reliable scientific evidence, to substantiate that the representation is true.

Given the nature and type of these products, it is possible that health-related hazards should have been included in these particular consent orders. This would imply that it is the specific context of these cases that serves as a justification for the inclusion of the health-related language. However, the harmonization of these new orders with the 2013 PPG and Sherwin-Williams orders would create new, broader obligations on those two companies. More generally, this would imply that the basis of the FTC's authority emanates not from the context in which the claim is brought, but instead from the very nature of VOCs, *i.e.*, as newly-deemed health hazards.

As a general principle, this means that, under its deception authority, the FTC could create *ex post facto* justifications for expanding its enforcement powers arbitrarily and with no forward guidance. For example, although the voluminous 2012 Green Guides Statement of Basis and Purpose made no mention of health risks,¹⁴⁸ the Commission found a way to add it on to previous consent agreements in a unilateral, non-deliberative way. This places industry actors at the mercy of the FTC, which can alter previous consent orders based on present or future interpretations of "deception."

C. Remember Concerns over Revocation of the Disgorgement Policy?

It is ironic that it should be this particular FTC that would modify a Policy Statement, which was treated as authoritative by regulated parties for four years and which was itself a surreptitious modification of a Guide issued through public notice and comment (and resulting in a 314-page Statement of Basis and Purpose), through such summary means—given that Acting Chairman Ohlhausen had previously urged greater deliberation and public input in withdrawing a policy statement.

In July 2012, the FTC summarily revoked its 2003 Policy Statement on Monetary Equitable Remedies in Competition Cases (commonly called the "Disgorgement Policy Statement")¹⁴⁹ on a 2–1 vote.¹⁵⁰ Commissioner Ohlhausen, the sole Republican on the Commission at the time, objected: "we are moving from clear guidance on disgorgement to virtually no guidance on this important policy issue."¹⁵¹ She also objected to the cursory, non-deliberative nature of the underlying process:

I am troubled by the seeming lack of deliberation that has accompanied the withdrawal of the Policy Statement. Notably, the Commission sought public comment on a draft of the Policy Statement before it was adopted. That public comment process was not pursued in connection with the withdrawal of the statement. I believe there should have been more internal deliberation and likely public input before the Commission withdrew a policy statement that appears to have served this agency well over the past nine years.¹⁵²

What then-Commissioner Ohlhausen said then about revocation of a policy statement remains true now about substantial modification of a policy statement (which is effectively a partial withdrawal of previous guidance): both internal debate and

¹⁴⁸ See generally Statement of Basis and Purpose.

¹⁴⁹ Fed. Trade Comm'n, Policy Statement on Monetary Equitable Remedies in Competition Cases, 68 Fed. Reg. 45,820 (Aug. 4, 2003).

¹⁵⁰ Press Release, Fed. Trade Comm'n, FTC Issues Policy Statement on Use of Monetary Remedies in Competition Cases (July 31, 2003), available at <http://www.ftc.gov/opa/2003/07/d disgorgement.shtm>.

¹⁵¹ See Statement of Commissioner Maureen K. Ohlhausen Dissenting from the Commission's Decision to Withdraw its Policy Statement on Monetary Equitable Remedies in Competition Cases, at 2 (July 31, 2012), <https://www.ftc.gov/public-statements/2012/07/statement-commissioner-maureen-k-ohlhausen-dissenting-commissions-decision>.

¹⁵² *Id.* at 2.

public input are essential. Burying the request for public comment in a press release about new settlements hardly counts as an adequate basis for reconsidering the 2013 Policy Statement—let alone modifying the 2012 Green Guides.

D. What Re-Opening FTC Settlements Could Mean for Tech Companies

The Commission could have, at any time over the last twenty years, undertaken the kind of empirical analysis that led to the Green Guides, and published guidance about interpretation of Section 5, but never did so. Instead, the Commission issued only a series of reports making broad, general recommendations. In fact, in one of the only two data security cases not to end in a consent decree, a Federal district judge blasted the FTC's decision not provide *any* data security standards:

No wonder you can't get this resolved, because if [a 20-year consent order is] the opening salvo, even I would be outraged, or at least I wouldn't be very receptive to it if that's the opening bid. . . . You have been completely unreasonable about this. And even today you are not willing to accept any responsibility. . . . *I think that you will admit that there are no security standards from the FTC.* You kind of take them as they come and decide whether somebody's practices were or were not within what's permissible from your eyes. . . . [H]ow does any company in the United States operate when. . . [it] says, well, tell me exactly what we are supposed to do, and you say, well, all we can say is you are not supposed to do what you did. . . . *[Y]ou ought to give them some guidance as to what you do and do not expect, what is or is not required.* You are a regulatory agency. I suspect you can do that.¹⁵³

In recent years, the Commission has proudly trumpeted its “common law of consent decrees” as providing guidance to regulated entities.¹⁵⁴ Now, everyone must understand that those consent decrees may be modified at any time, particularly those consent decrees that are ordered by the Commission (as opposed to a Federal court). As the Supreme Court made clear, “[t]he Commission has statutory power to reopen and modify its orders at all times.”¹⁵⁵ In order to reopen and modify an order, the Commission faces an incredibly low bar, having to merely show that it has “reasonable grounds to believe that public interest at the present time would be served by reopening.”¹⁵⁶ Meanwhile, the FTC's consent decrees often stipulate that the defendant “waives . . . all rights to seek judicial review or otherwise challenge or contest the validity of the order entered pursuant to this agreement.”¹⁵⁷

But in cases where the FTC needs a court to issue a consent decree (*e.g.*, to obtain an injunction or restitution), if the FTC wishes to modify the decree, it must at least meet the requirements imposed by Federal Rule of Civil Procedure 60:¹⁵⁸ the FTC must meet a heightened pleading standard through a showing of, for example, “fraud,” “mistake,” or “newly discovered evidence” necessitating such a modification.¹⁵⁹ Furthermore, the FTC does not have the freedom to modify court ordered consent decrees “at any time,” as with settlements, but must file a motion “within a reasonable time”—the same standard that applies to all litigants in Federal court.¹⁶⁰

Why should there be such radically different standards? It is true that violating court-ordered consent decrees can result in criminal liability penalties, while violating Commission-ordered consent decrees means only civil penalties—but those penalties may be significant. For example, in 2015, the FTC imposed a \$100 million fine against Lifelock for violating a 2010 consent decree by failing to provide “reasonable” data security¹⁶¹—over eight times the amount of the company's 2010 settlement and two thirds of the company's entire revenue that quarter (\$156.2 mil-

¹⁵³ Transcript of Proceedings at 91, 94–95, *LabMD, Inc. v. Fed. Trade Comm'n*, No. 1:14-CV-810-WSD, 2014 WL 1908716 (N.D. Ga. May 7, 2014)) (emphasis added).

¹⁵⁴ Julie Brill, Comm'r, Fed. Trade Comm'n, “Privacy, Consumer Protection, and Competition,” Address at the 12th Annual Loyola Antitrust Colloquium (Apr. 27, 2012), http://www.ftc.gov/sites/default/files/documents/public_statements/privacy-consumer-protection-and-competition/120427loyolasymposium.pdf (stating the FTC consent decrees have “created a ‘common law of consent decrees,’ producing a set of data protection rules for businesses to follow”).

¹⁵⁵ *Atl. Ref. Co. v. F.T.C.*, 381 U.S. 357, 377 (1965).

¹⁵⁶ *Elmo Co. v. F.T.C.*, 389 F.2d 550, 552 (D.C. Cir. 1967), *cert. denied*, 392 U.S. 905 (1968).

¹⁵⁷ *See, e.g.*, Agreement Containing Consent Order at 3(C), *In re Oracle*, No. 132 3115 (F.T.C. Dec. 21, 2015), <https://www.ftc.gov/system/files/documents/cases/151221oracleorder.pdf>.

¹⁵⁸ Fed. R. Civ. P. 60 (stating that “the court may relieve a party or its legal representative from a final judgment, order, or proceeding” for certain reasons, including “mistake,” “newly discovered evidence,” “fraud,” and “any other reason that justifies relief.”).

¹⁵⁹ Fed. R. Civ. P. 60(b).

¹⁶⁰ Fed. R. Civ. P. 60(c).

¹⁶¹ Fed. Trade Comm'n, *LifeLock to Pay \$100 Million to Consumers to Settle FTC Charges it Violated 2010 Order* (Dec. 17, 2015), available at <https://www.ftc.gov/news-events/press-releases/2015/12/lifelock-pay-100-million-consumers-settle-ftc-charges-it-violated>.

lion).¹⁶² In general, arbitrarily-imposed, post-hoc civil liability carries the risk of causing significant economic loss, reputational harm, and even business closure. For example, the Commission could re-open *all* its past data security and privacy cases to modify the meaning of the term “covered information.” To the extent that companies are found to be in non-compliance with the new standard, they would be liable for prosecution to the full extent of the FTC’s powers. Besides compromising the ability of existing industry actors to comply, invest, and grow, this would have the effect of deterring new actors from entering a data-based industry for fear of uncertainty and retroactive prosecution.

Congress should reassess the standard by which the FTC may reopen and modify its own orders. In doing so, it should begin with the question articulated long ago by the Supreme Court: “whether any thing has happened that will justify . . . changing a decree.”¹⁶³ In answering this question, the Court made clear that “[n]othing less than a clear showing of grievous wrong evoked by new and unforeseen conditions should lead us to change what was decreed . . . with the consent of all concerned.”¹⁶⁴ The reason for the Court’s hesitation to modify consent decrees should be obvious: despite retaining the force of a court order, consent decrees are, at their core, stipulated terms *mutually* agreed to by the parties to the litigation, similar to traditional settlements of civil litigation. Thus, by choosing to settle and enter into consent decrees, “[t]he parties waive their right to litigate the issues involved in the case and thus save themselves the time, expense, and inevitable risk of litigation.”¹⁶⁵

In Federal court, Rule 60 forces parties to show that circumstances have indeed changed enough to justify modification of a court order. However, having to only show that it believes the “public interest” would be served, the FTC essentially is not required to make *any* showing of necessity that would counterbalance the value of preserving the terms of the settlement. Given the enormous weight the FTC itself has placed upon its “common law of consent decrees,” as a substitute both for judicial decisions and clearer guidance from the agency, Congress should find it alarming that the FTC is now undermining the value of that pseudo-common law.

Ultimately, allowing the FTC to modify such agreements without showing any real cause not only negates the value of such agreements to each company (in efficiently resolving the enforcement action and allowing the company to move on), but more systemically and perhaps more importantly, it diminishes the public’s trust in the government to be true to its word. Procedure matters. When agencies fail to utilize fair procedures in developing laws, the public’s faith in both the laws and underlying institutions is diminished. This, in turn, undermines their effectiveness and further erodes the public’s trust in the legal institutions upon which our democracy rests.¹⁶⁶ Thus, even in instances where the policy behind the rule may be sound, a failure by the implementing agency to follow basic due process will undermine the public’s faith and deprive businesses of the certainty they need to thrive.¹⁶⁷

VII. Better Empirical Research & Investigations

Why *doesn’t* the FTC do more empirical research—the kind that went into the Green Guides? What should the process around, and following, its forthcoming workshop on “informational injuries” look like?

¹⁶² LifeLock, Inc., *LifeLock Announces 2015 Fourth Quarter Results* (Feb. 10, 2016), available at <https://www.lifelock.com/pr/2016/02/10/lifelock-announces-2015-fourth-quarter-results-2/>

¹⁶³ *United States v. Swift & Co.*, 286 U.S. 106, 119 (1932).

¹⁶⁴ *Id.*

¹⁶⁵ *Local No. 93, Int’l Asso. of Firefighters, etc. v. Cleveland*, 478 U.S. 501, 522 (1986) (quoting *United States v. Armour & Co.*, 402 U.S. 673, 681–682 (1971)).

¹⁶⁶ *See, e.g.*, Pew Research Center, *Beyond Distrust: How Americans View Their Government* (2015) (“Only 19 percent of Americans today say they can trust the government in Washington to do what is right “just about always” (3 percent) or “most of the time” (16 percent).”).

¹⁶⁷ *See, e.g.*, *Nat’l Petroleum Refiners Ass’n v. F.T.C.*, 482 F.2d 672, 675–76 (D.C. Cir. 1973), cert. denied, 415 U.S. 951 (1974) (recognizing that “courts have stressed the advantages of efficiency and expedition which inhere in reliance on rulemaking instead of adjudication alone,” including in providing businesses with greater certainty as to what business practices are not permissible).

A. *What the FTC Does Now*

Since 2013, the FTC has published each January an annual report titled the “Privacy & Data Security Update.”¹⁶⁸ The 2016 Report¹⁶⁹ boasts the FTC’s “unparalleled experience in consumer privacy enforcement”¹⁷⁰ and the wide spectrum of off-line, online, and mobile privacy practices that the Commission has addressed with enforcement actions:

[The FTC] has brought enforcement actions against well-known companies, such as Google, Facebook, Twitter, and Microsoft, as well as lesser-known companies. The FTC’s consumer privacy enforcement orders do not just protect American consumers; rather, they protect consumers worldwide from unfair or deceptive practices by businesses within the FTC’s jurisdiction.¹⁷¹

Given the far-reaching scope of the FTC’s jurisdiction on Section 5 enforcement and the wide range of companies that have settled “informational injury” cases, one might expect the these annual “Updates” to do more than merely summarize the previous year’s activities, and instead provide empirical research into the privacy and data threats facing consumers. By failing to do so, the Commission not only leaves businesses in the dark as to what constitutes “reasonable” practices in the Government’s eyes, but fails to inform them of the best practices available to ensure that Americans’ data and privacy is adequately protected.

For example, if the Commission is to proudly report that consumer protection was achieved from settling charges with a mobile ad network on the grounds that “[the company] deceived consumers by falsely leading them to believe they could reduce the extent to which the company tracked them online and on their mobile phones,”¹⁷² that Commission’s work should not have ended there as a single bullet-point of the Commission’s many highlights. As an enforcement agency with vast interpretive powers on deceptive practices, and an investigative body with considerable analytical resources, the Commission has a further duty to clearly explain the empirical rationale that substantiates the settlement: Just how do consumers understand privacy in the use of advertising cookies? How might companies use Do Not Track signals, given those consumer expectations, to provide an effective opt-out mechanism? How should the standard differ based on the sizes of companies and the services they provide? What “informational injuries” occur when consumers unknowingly receiving tailored advertisements through the use of unique device identifiers? It is one thing to say that the Commission should not have to answer all these questions in its pleadings, or even in order to prevail in a deception case. It is quite another to say that the Commission should not be expected to perform any research even after the fact, especially on matters that recur across a larger arc of enforcement actions.

Unforeseen vulnerabilities are the inevitable side-effect of rapid technological advancements; in the area of data privacy and security, new consumer risks will arise continually, raising questions that *should* merit careful quantitative and qualitative analyses. However, in its “Privacy & Data Security Update,” the FTC essentially asserts an answer without “showing its work.”

This is in stark comparison to the FTC’s approach on the Green Guides, where “the Commission sought comment on a number of general issues, including the continuing need for, and economic impact of, the Guides, as well as the Guides’ effect on environmental claims”.¹⁷³

[B]ecause the Guides are based on consumer understanding of environmental claims, consumer perception research provides the best evidence upon which to formulate guidance. The Commission therefore conducted its own study in July and August of 2009. The study presented 3,777 participants with questions calculated to determine how they understood certain environmental claims. The first portion of the study examined general environmental benefit claims (“green” and “eco-friendly”), as well as “sustainable,” “made with renewable materials,” “made with renewable energy,” and “made with recycled materials” claims. To examine whether consumers’ understanding of these claims differed depending on the product being advertised, the study tested the claims as they

¹⁶⁸FED. TRADE COMM’N, PRIVACY AND DATA SECURITY UPDATE: 2013 (June 2012), available at https://www.ftc.gov/policy/reports/policy-reports/commission-and-staff-reports?title=data+security&items_per_page=20.

¹⁶⁹FED. TRADE COMM’N, PRIVACY AND DATA SECURITY UPDATE: 2016 (Jan 2017), available at <https://www.ftc.gov/reports/privacy-data-security-update-2016>.

¹⁷⁰*Id.* at 2.

¹⁷¹*Id.*

¹⁷²*Id.*

¹⁷³Statement of Basis and Purpose, at 8.

appeared on three different products: wrapping paper, a laundry basket, and kitchen flooring. The second portion of the study tested carbon offset and carbon neutral claims.¹⁷⁴

Here is an excellent example of the FTC's use of consumer perception data to study the effect of environmental labels, with variables on consumer behavioral segments and changes on perception over time, to substantiate deception claims. Even with the empirical research grounded in a large sample size, the Commission continued to reanalyze "claims appearing in marketing on a case-by-case basis because [the Commission] lacked information about how consumers interpret these claims."¹⁷⁵ The "Green Guides: Statement of Basis and Purpose"¹⁷⁶ is a 314 page document that comprehensively reviews the Commission's economic and consumer perception studies and weighs different empirical methodologies on the appropriate model of risk assessment. It meaningfully fleshes out the Green Guides' core guidance on the "(1) general principles that apply to all environmental marketing claims; (2) how consumers are likely to interpret particular claims and how marketers can substantiate these claims; and (3) how marketers can qualify their claims to avoid deceiving consumers," with self-awareness of the economic impact of regulations and a robust metric on consumer expectations to materialize the Commission's enforcement policies.

It is deeply troubling that this level of thoroughness evades the Commission's privacy enforcement, where the toolbox of economics remains unopened in managing the information flows of commercial data in boundless technology sectors pervading everyday life. The FTC's history of consent decrees provides nothing more than anecdotal evidence that *some* guiding principle is present, within the vague conceptual frameworks of "privacy by design," "data minimization", or "notice and choice."¹⁷⁷ Data privacy and security regulations do not exist in a silo, abstracted and harbored from real-life economic consequences for the consumers, firms, and stakeholders—whose interests intersect at the axis of the costs and benefits of implementing privacy systems, the need for working data in nascent industries, and the market's right to make informed decisions. Consumer protection through privacy regulation is undoubtedly a matter of economic significance parallel to antitrust policies or the label marketing in the Green Guides. Personally identifiable information ("PII") is a valuable corporate asset like any other,¹⁷⁸ with competitive market forces affecting how it is processed, shared, and retained. Modern consumers are cognizant of the tradeoffs they make at the convenience of integrated technology services, and the downstream uses of their data. Accordingly, not every technical deviation from a company's privacy policy is an affront to consumer welfare that causes "unavoidable harms not outweighed by the benefits to consumers or competition."¹⁷⁹ The FTC has too long failed to articulate the privacy risks it intends to rectify, nor to quantify the "material" consumer harm through behavioral economics or any empirical metric substantiated beyond its usual *ipso facto* assertion of deception.

B. The Paperwork Reduction Act

A noteworthy legislation that defined the FTC's administrative authority after Congress imposed additional safeguards upon the FTC's Magnuson-Moss rule-making powers in 1980 is the Paperwork Reduction Act of 1980 ("PRA").¹⁸⁰ These two 1980 enactments must be understood together as embodying Carter-era attempts to reduce the burdens of government. Specifically, Congress intended the PRA to serve as an administrative check on the Federal agency's information collection policy, with the goal of reducing paperwork burdens for individuals, businesses, and nonprofits by requiring the FTC to seek clearance from the Office of Management and Budget ("OMB") on compulsory process orders surveying ten or more members of the public.

The "collection of information" that falls under the constraints of the PRA is defined as:

the obtaining, causing to be obtained, soliciting, or requiring the disclosure to third parties or the public, of facts or opinions by or for an agency, regardless

¹⁷⁴ *Id.* at 9–10.

¹⁷⁵ See Statement of Basis and Purpose, at 27.

¹⁷⁶ See generally Statement of Basis and Purpose.

¹⁷⁷ See generally 2012 Privacy Report.

¹⁷⁸ Clearwater Compliance LLC, *The Clearwater Definition of an Information Asset*, https://clearwatercompliance.com/wp-content/uploads/2015/11/Clearwater-Definition-of-Information-Assets-with-Exam-ples_V8.pdf.

¹⁷⁹ 12 U.S.C. § 5331(c)(1).

¹⁸⁰ Paperwork Reduction Act of 1980, Pub. L. No. 96–511, 94 Stat. 2812 (codified as amended at 44 U.S.C. §§ 3501–3520 (2012)).

of form or format, calling for either—answers to identical questions posed to, or identical reporting or recordkeeping requirements imposed on, ten or more persons, other than agencies, instrumentalities, or employees of the United States.¹⁸¹

Some have claimed that the PRA has hampered the FTC’s ability to collect data from companies and thus to perform better analysis of industry practices, informational injuries, and the like. The FTC’s power to gather information *without* “a specific law enforcement purpose” derives from Section 6(b) of the FTC Act, which the FTC has summarized in relevant part as follows:

Section 6(b) empowers the Commission to require the filing of “annual or special reports or answers in writing to specific questions” for the purpose of obtaining information about “the organization, business, conduct, practices, management, and relation to other corporations, partnerships, and individuals” of the entities to whom the inquiry is addressed.¹⁸²

Such reports would certainly be helpful for providing better substantiated guidance regarding data privacy and security practices. It is worth carefully considering what the PRA requires and how it might affect the FTC’s collection of data. There is indeed some circumstantial evidence to suggest that the FTC may be structuring its 6(b) inquiries to avoid the PRA, by limiting the number of firms from which the FTC requests data to fewer than ten¹⁸³—the threshold for triggering the PRA’s requirements.

A case study on the FTC’s survey of Patent Assertion Entities (“PAEs”)¹⁸⁴ illustrates two potential ways the PRA might affect the FTC’s collection of empirical data and thus the quality of its analysis and guidance in data security and privacy cases. First, by its own terms, the PRA applies even to *voluntary* data-collection of the sort that could allow the FTC compile “line of business” studies that consider wider practices beyond a single case:

[T]he obtaining, causing to be obtained, soliciting, or requiring the disclosure to an agency, third parties or the public of information by or for an agency . . . whether such collection of information is mandatory, voluntary, or required to obtain or retain a benefit.¹⁸⁵

The burden-minimization goal of the PRA is evaluated by the OMB based on broad, unpredictable criteria, such as whether the “the proposed collection of information is necessary for the proper performance of the functions of the agency, including whether the information will have practical utility.”¹⁸⁶ The PRA has been enforced by the OMB with tunnel vision on reducing the burden of paperwork and compliance, measured quite simply on the metric of man hours spent processing the paperwork.¹⁸⁷ However, the more important question lies on balancing the potential burden of information collection with the value of added research and empirical data on FTC policymaking. The balance was correctly struck on the Green Guides, where the PRA analysis was satisfied upon a consideration of the benefits of consumer surveys which outweighed the minimal burdens to the respondents:

¹⁸¹ 44 U.S.C. § 3502(3).

¹⁸² Fed. Trade Comm’n, A Brief Overview of the Federal Trade Commission’s Investigative and Law Enforcement Authority (July 2008), available at <https://www.ftc.gov/about-ftc/what-we-do/enforcement-authority>.

¹⁸³ See e.g., FTC To Study Credit Card Industry Data Security Auditing Commission Issues Orders to Nine Companies That Conduct Payment Card Industry Screening (March 2016) <https://www.ftc.gov/news-events/press-releases/2016/03/ftc-study-credit-card-industry-data-security-auditing>; FTC To Study Mobile Device Industry’s Security Update Practices (May 2016) <https://www.ftc.gov/news-events/press-releases/2016/05/ftc-study-mobile-device-industrys-security-update-practices>.

¹⁸⁴ Layne-Farrar, Anne, What Can the FTC’s § 6(B) PAE Study Teach Us? A Practical Review of the Study’s Methodology (March 1, 2016). Available at SSRN: <https://ssrn.com/abstract=2722057>, or <http://dx.doi.org/10.2139/ssrn.2722057>.

¹⁸⁵ 5 C.F.R. § 1320.3(c).

¹⁸⁶ United States Office of Personnel Management, Paperwork Reduction Act (PRA) Guide Version 2.0 (April 2011), available at <https://www.opm.gov/about-us/open-government/digital-government-strategy/fitara/paperwork-reduction-act-guide.pdf>.

¹⁸⁷ *Id.* See also Sam Batkins, Evaluating the Paperwork Reduction Act: Are Burdens Being Reduced? AAF, <https://www.americanactionforum.org/testimony/evaluating-paperwork-reduction-act-burdens-reduced/>.

Overall burden for the pretest and questionnaire would thus be 2,511 hours. The cost per respondent should be negligible. Participation is voluntary and will not require start-up, capital, or labor expenditures by respondents.¹⁸⁸

Moreover, the FTC integrated various suggestions on the study methodology and data collection methods submitted in a public comment by the General Electric Company (“GE”), to ensure that the Commission surveyed “a proper universe of consumers” upon which to “obtain accurate projections of national sentiment.”¹⁸⁹

With respect to GE’s concern about identifying the “proper universe of consumers,” FTC staff has included in the questionnaire a brief section of questions that address participants’ level of interest in environmental issues. For example, one question asks: “In the past six months, have you chosen to purchase one product rather than another because the product is better for the environment?” Through analyses of answers to such questions, staff can compare the study responses of participants who have a high degree of interest in environmental issues and who take these issues into account when making purchasing decisions with responses of participants who are not as concerned with environmental issues.

GE also asserts that the FTC should ensure a “proper sample size.” The FTC staff determined the sample size of 3,700 consumers based on several considerations, including the funds available for the study, the cost of different sample size configurations, the number of environmental claims to be examined, and a power analysis. In this study, 150 participants will see each of the various environmental marketing claims to be compared. Staff believes that this will be adequate to allow comparisons across treatment cells.¹⁹⁰

By contrast, the FTC study on PAEs, which also received PRA clearance, compiled “nonpublic data on licensing agreements, patent acquisition practices, and related costs and revenues”¹⁹¹ to illuminate how PAEs operate in patent enforcement activity outside the confines of litigation records. But even when the OMB cleared the PAE study, the FTC chose a limited sample size of “25 PAEs, 9 wireless chipset manufacturers that hold patents, and 6 non-practicing wireless chipset patent holders.”¹⁹² This restrictive sample size significantly limited the applicability of the Commission’s conclusions. More broadly, it suggests a shift towards a general reluctance to design and implement systemic research even when the required administrative blessing is obtained under the PRA.

The PRA Guide of 2011 outlines information collection policies and procedures, albeit with only a superficial explanation of statistical methodologies, and zero mention of survey design and quantitative research methods.¹⁹³ It is a cause for concern that the OMB’s task of cutting down on the amount of paperwork is framed so parochially, for the short term goal of reducing participation hours, without perhaps considering cases where the quality and usability of the research itself depends on obtaining a larger sample. The mandate to limit the sample size of survey respondents ironically defeats the “practical utility” of the research, which is one of the main cornerstones of the PRA.

On the other hand, the PRA does not apply to *all* voluntary collection—only when the FTC sends “identical” questions to ten or more companies (whether their answer is voluntary or compulsory). The PRA would *not* apply to the FTC requesting public comment, such as it has done through the Green Guides process. This point is critical: while targeting specific companies with the same questions might well prove useful in informing the FTC’s understanding of informational injuries, the FTC’s failure to collect more such data thus far, to analyze it, and to publish it in useful guidance can in no way be blamed on the requirements of the PRA. Nor can it excuse the FTC staff for relying on an expert witness in the LabMD case whose recommendations about “reasonable” data security referred exclusively to the practices

¹⁸⁸ Fed. Trade Comm’n, Agency Information Collection Activities; Submission for OMB Review; Comment Request (May 2009), Federal Register/VOL. 74, NO. 90, available at https://www.ftc.gov/sites/default/files/documents/federal_register_notices/green-marketing-consumer-perception-study-agency-information-collection-activities-submission-omb/090512greenmarketing.pdf.

¹⁸⁹ *Id.* at 22398.

¹⁹⁰ *Id.*

¹⁹¹ See What Can the FTC’s §6(B) PAE Study Teach Us? A Practical Review of the Study’s Methodology (March 1, 2016); “Supporting Statement for a Paperwork Reduction Act: Part B” available at <http://www.reginfo.gov/public/do/DownloadDocument?objectID=47563401>.

¹⁹² *Id.*

¹⁹³ See generally Paperwork Reduction Act (PRA) Guide Version 2.0.

of Fortune 500 companies, without referencing *any* small businesses comparable in size and technical sophistication to LabMD.¹⁹⁴

Indeed, the PRA Guide exempts from the definition of “information,” and thus eliminates the need for clearance on, the collection of “facts or opinions submitted in response to general solicitations of comments from the general public”¹⁹⁵ and “examinations designed to test the aptitude, abilities, or knowledge of the person tested for a collection.”¹⁹⁶ The PRA poses no impediment to the FTC taking a proactive approach on conducting empirical research on data privacy by calling for consumer survey participants, holding public workshops, or from analyzing public data such as companies’ privacy policies as a means to test privacy risk perception and consumer expectations. The Green Guides illustrate just how much data collection the FTC can do to substantiate its policymaking with empirical and economic research, based on real consumer studies.

VIII. Pleading, Settlement and Merits Standards under Section 5

In general, the FTC Act currently sets a very low bar for bringing complaints: “reason to believe that [a violation may have occurred]” and that “it shall appear to the Commission that [an enforcement action] would be to the interest of the public.”¹⁹⁷ In practice, this has become the standard for *settlements*, since the Act does not provide such a standard, and the FTC commonly issues both together. This raises three questions:

1. What should the standard be for issuing complaints?
2. Closely related, what should the standard be for courts weighing a defendant’s motions to dismiss?
3. What should the standard be for settling cases?

Raising all three bars would do much to improve the quality of the agency’s “common law” in several respects:

1. It would provide greater rigor for FTC staff throughout the course of the investigation;
2. Companies would be less likely to settle, and more likely to litigate, if they had a better chance of prevailing at the motion to dismiss stage; and
3. Complaints that settle before trial (after the FTC has survived a motion to dismiss) would, or complaints that the FTC has withdrawn (after the FTC has lost a motion to dismiss) would provide more guidance standing on their own as the final, principle record of each case.

We take the questions raised above in reverse order, beginning with the standard by which a court will assess a motion to dismiss and concluding with the standard by which Commissioners will decide whether to issue a complaint (and thus, in nearly every case, also a settlement):

A. Pleading & Complaint Standards

Fortunately, the courts are already moving towards requiring the FTC to do a better job of writing its pleadings (complaints) or face dismissal of its complaints—at least with respect to deception. Congress should take note of the current case law on this issue and consider codifying a heightened pleading requirement for any use of Section 5.

Heightened pleading standards can be fatal to normal plaintiffs, who need to survive a motion to dismiss in order to obtain the discovery they need to actually prevail on the merits. But the FTC has uniquely broad investigative powers. It is difficult to see why they would *ever* need court-ordered discovery—in other words, why would it be a problem for the Commission to have to do more to ground their complaints in the requirements of Section 5, as made clear in the FTC’s Deception and Unfairness policy statements, and Section 5(n). Today, the FTC wants the best of both worlds: vast pre-trial discovery power *and* the low bar for pleadings claimed by normal plaintiffs who lack that power.

¹⁹⁴ Gus Hurwitz, *The FTC’s Data Security Error: Treating Small Businesses Like the Fortune 1000* (Feb. 20, 2017), available at <https://www.forbes.com/sites/washingtonbytes/2017/02/20/the-ftcs-data-security-error-treating-small-businesses-like-the-fortune-1000/#58d2b735a825>.

¹⁹⁵ United States Office of Personnel Management, Paperwork Reduction Act (PRA), Version 2.0, OPM at 6 (April 2011), available at <https://www.opm.gov/about-us/open-government/digital-government-strategy/fitara/paperwork-reduction-act-guide.pdf>.

¹⁹⁶ *Id.*

¹⁹⁷ 15 U.S.C. 45(b).

At a minimum, the FTC should be required to plead its Section 5 claims with specificity. Ideally, this standard would closely mirror a “preponderance of the evidence,” as explained in the attached white paper.¹⁹⁸

1. Deception Cases

TechFreedom has long argued that the FTC’s deception complaints should have to satisfy the heightened pleading standards of Fed. R. Civ. Pro. 9(b).¹⁹⁹ Under that rule, “[i]n alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake.”²⁰⁰ In other words, such claims must be accompanied by the “who, what, when, where, and how” of the conduct charged.²⁰¹ Rule 9(b) gives defendants “notice of the claims against them, provide[] an increased measure of protection for their reputations, and reduce[] the number of frivolous suits brought solely to extract settlements.”²⁰²

Several district courts have concluded that 9(b) applies to FTC deception allegations.²⁰³ Most recently, the Northern District of California dismissed two of the FTC’s five deception counts in its data security complaint against D-Link²⁰⁴ for failure to satisfy the heightened pleading standard of Rule 9(b).²⁰⁵ The district court noted that the Ninth Circuit has yet to address the question, but nonetheless found controlling the appeals court’s decision holding that California’s Unfair Competition Law—the state’s “Baby FTC Act,” which, “like Section 5 outlaws deceptive practices without requiring fraud as an essential element”—is subject to Rule 9(b).²⁰⁶

The *D-Link* court’s analysis of each of the FTC’s five deception counts illustrates that, while a heightened pleading standard *would* require more work from Commission staff to establish their cases, this burden would be relatively small and would in no way hamstring the Commission from bringing legitimate cases. The court upheld the principal deception count (Count II: “that DLS has misrepresented the data security and protections its devices provide”) and two others, dismissing only two peripheral claims. If anything, merely applying Section 9(b) to the Commission’s complaints would likely not be enough, on its own, to provide adequate discipline to the Commission’s use of its investigation and enforcement powers—but it would certainly be a start.

The district court’s discussion of Count II illustrates what specificity in pleading deception claims would look like. The FTC’s allegations identified “specific statements DLS made at specific times between December 2013 and September 2015,” and that the allegations “also specify why the statements are deceptive.”²⁰⁷ The court goes on to say that “Count II identifies the time period during which DLS made the statements and provides specific reasons why the statements were false—for example, that the routers and IP cameras could be hacked through hard-coded user credentials or command injection flaws,” and that “this is all Rule 9(b) demands.”²⁰⁸

2. Unfairness Cases

The *D-Link* court noted that “[w]hether the FTC must also plead its unfairness claim under Rule 9(b) is more debatable,” finding “little flavor of fraud in the[] elements [of unfairness under Section 5(n)].” But, the court continued:

¹⁹⁸ See White Paper, *supra* note 51, at 18–21 (unfairness) and 28 (deception).

¹⁹⁹ See Brief of Amicus Curiae TechFreedom, International Center for Law and Economics, & Consumer Protection Scholars in Support of Defendants, *FTC v. Wyndham Worldwide Corp.*, 10 F. Supp. 3d 602 (D.N.J. 2014) (No. 13–1887), 2013 WL 3739729, available at <https://goo.gl/JGUE9e>.

²⁰⁰ Fed. R. Civ. P. 9(b).

²⁰¹ *Vess v. Ciba-Geigy Corp., USA*, 317 F.3d 1097, 1106 (9th Cir. 2003).

²⁰² *In re Burlington Coat Factory Sec. Litig.*, 114 F.3d 1410, 1418 (3d Cir. 1997).

²⁰³ See, e.g., *FTC v. Lights of Am., Inc.*, 760 F. Supp. 2d 848 (C.D. Cal. 2010); *FTC v. Ivy Capital, Inc.*, 2011 WL 2118626 (D. Nev. May 25, 2011); *FTC v. ELH Consulting, LLC*, No. CV 12–02246–PHX–FJM, 2013 WL 4759267, at *1 (D. Ariz. Sept. 4, 2013) (same); see also *FTC v. Swish Marketing, No. C–09–03814–RS*, 2010 WL 653486, at *2–4 (N.D. Cal. Feb. 22, 2010) (finding “a real prospect” that Rule 9(b) applies but not deciding the issue).

²⁰⁴ See Complaint for Permanent Injunction and Other Equitable Relief, *Fed. Trade Comm’n v. D-Link Sys., Inc.*, No. 3:17–CV–00039–JD, 2017 (N.D. Cal. Sept. 19, 2017), https://www.ftc.gov/system/files/documents/cases/d-link_complaint_for_permanent_injunction_and_other_equitable_relief_unredacted_version_seal_lifted_-_3-20-17.pdf.

²⁰⁵ See Order Re Motion to Dismiss, *Fed. Trade Comm’n v. D-Link Sys.*, No. 3:17–CV–00039–JD, 2017 (N.D. Cal. Sept. 19, 2017), at 2–3, <https://consumermediallc.files.wordpress.com/2017/09/dlinkdismissal.pdf>.

²⁰⁶ *Id.* at 2–3 (discussing *Vess v. Ciba-Geigy Corp. USA*, 317 F.3d 1097, 1103–04 (9th Cir. 2003)).

²⁰⁷ *Id.* at 4.

²⁰⁸ *Id.* at 4–5.

the FTC has expressly stated that the unfairness claim against DLS is not tied to an alleged misrepresentation. See Section III, below. At the same time, however, the FTC has said that for all of its claims “the core facts overlap, absolutely,” and there is no doubt that the overall theme of the complaint is that DLS misled consumers about the data security its products provide. The FTC also acknowledges that DLS’s misrepresentations are relevant to the unfairness claim because consumers could not have reasonably avoided injury in light of them.

Consequently, there is a distinct possibility that Rule 9(b) might apply to the unfairness claim. But the question presently is not ripe for resolution. As discussed below, the unfairness claim is dismissed under Rule 8. Whether it will need to satisfy Rule 9(b) will depend on how the unfairness claim is stated, if the FTC chooses to amend.²⁰⁹

Whatever the courts actually conclude about the applicability of Rule 9(b) to unfairness claims, we see no reason why the Commission should not be subject to the same heightened pleading requirements under unfairness.

B. Preponderance of the Evidence Standard

Applying Section 9(b) to all Section 5 pleadings would help greatly. But the more fundamental problem in unfairness cases is the low bar set by Section 5(b) for bringing a complaint—and the lack of *any* standard for settling it. We believe the answer is to require the Commission staff to demonstrate that it would prevail by a preponderance of the evidence. It may, at first, seem strange to apply this standard—the general standard for resolving civil litigation—at the early stages of litigation, but it must be remembered that this is not normal litigation. As noted above, the FTC has unique pre-trial discovery powers, and so is very likely to have accumulated all the evidence it will need at trial before the complaint is ever issued. Second, in nearly every “informational injury” case, the Commission’s decision over whether to issue a complaint *is* the final decision over the case—because the cause will simply settle at that point. Congress should consider applying this standard either to the issuance of unfairness complaints, or to the issuance of settlements. If the standard is applied only to the issuance of settlements, Congress should consider some other heightened standard for bringing unfairness complaints, above that required by Section 9(b). In any event, the purpose of any standard imposed at this stage would not be to change how litigation would work—which would still be resolved under separate standards for motions to dismiss, motions for summary judgment and final resolution of litigation on the merits—but rather to spur Commissioners to demand more analytical work of the staff. Some such change is likely the only way to create sustainable analytical discipline inside the Commission.

IX. Conclusion

There is little reason to expect that the FTC will not continue to more and more closely resemble the Federal Technology Commission with each passing year: the Commission will continue to grapple with new issues. This is just as Congress intended. But if the agency is to be trusted with such broad power, Congress should expect—and indeed take steps to ensure—that the FTC does more to justify how it wields that power. As Sens. Barry Goldwater (R-AZ) & Harrison Schmitt (D-AZ) said in 1980:

Considering that rules of the Commission may apply to any act or practice “affecting commerce”, and that the only statutory restraint is that it be unfair, the apparent power of the Commission with respect to commercial law is virtually as broad as the Congress itself. In fact, the Federal Trade Commission may be the second most powerful legislature in the country. . . . All 50 State legislatures and State Supreme Courts can agree that a particular act is fair and lawful, but the five-man appointed FTC can overrule them all. The Congress has little control over the far-flung activities of this agency short of passing entirely new legislation.²¹⁰

This testimony, and the attached documents, lay out some of the ideas that Congress should consider in assessing how to reform the FTC’s processes and standards. But these questions are sufficiently complex, and have been simmering for long enough, that the Committee would benefit from finding ways to maximize the input of outside experts.

²⁰⁹ *Fed. Trade Comm’n v. D-Link Sys.*, at *2 (N.D. Cal. Sept. 19, 2017).

²¹⁰ S. Rep. No. 96–184, at 18 (1980), available at <http://digitalcollections.library.emu.edu/aw-web/awarchive?type=file&item=417102>.

One model for that would be the House Energy & Commerce Committee's ongoing #CommActUpdate effort.²¹¹ The Committee has issued six white papers, each time taking public comment and refining its proposals. Given the complex interrelationships among the pieces of FTC reform, this would be a more constructive approach than having a flurry of separate bills, as Energy & Commerce did with FTC reform.

The Committee could also consider establishing a blue-ribbon Commission modeled on the Antitrust Modernization Commission—as TechFreedom and the International Center for Law & Economics proposed in 2014:

A Privacy Law Modernization Commission could do what Commerce on its own cannot, and what the FTC could probably do but has refused to do: carefully study where new legislation is needed and how best to write it. It can also do what no Executive or independent agency can: establish a consensus among a diverse array of experts that can be presented to Congress as, not merely yet another in a series of failed proposals, but one that has a unique degree of analytical rigor behind it and bipartisan endorsement. If any significant reform is ever going to be enacted by Congress, it is most likely to come as the result of such a commission's recommendations.²¹²

We stand ready to assist the Committee in whatever approach it takes.

Senator MORAN. Mr. Szóka, thank you very much. Let me begin with a question about privacy and data security.

The FTC is one of several agencies that play a role in addressing privacy and data security practices. Would you describe to me what the authorities of the FTC are in this arena? And should the Congress take any steps to increase or decrease that authority and its relationship with other agencies related to the topic of data security and breach? I'm happy to have anyone respond.

Ms. Rich.

Ms. RICH. I was there most recently. So the FTC has—

Senator MORAN. That means, you, Mr. Szóka, must come last.

[Laughter.]

Ms. RICH. The FTC has played the leading role in privacy and data security for quite a few years. It's what I started working on in the late 1990s, and that was mid to late 1990s, the FTC has been the lead agency. That said, there are others—and the FTC has several laws it uses. It uses the FTC Act, Unfair and Deceptive Practices, and then it has a few sectoral laws that bear on this, the Gramm-Leach-Bliley Act, the Fair Credit Reporting Act. There are gaps in those, and the FTC sometimes is frustrated and can't address privacy and data security because the practices don't happen to fall within those sectoral laws.

The FCC and the CFPB have both played some role in privacy and data security because they are active in consumer protection, but it really has not been nearly as substantial, and the agencies coordinate closely when anything like that arises, and they are all subject to MOUs that they follow. And, of course, the Department of Justice investigates the hackers, and so—and perhaps U.S. Attorneys Offices may—individual U.S. Attorneys Offices may do that. And, again, the FTC is in close contact when that occurs and coordinates very closely.

²¹¹The Energy and Commerce Committee, #COMMSUPDATE (last visited Sept. 25, 11:00 AM), <https://energycommerce.house.gov/commactupdate/>.

²¹²Comments of TechFreedom & International Center for Law and Economics, In the Matter of Big Data and Consumer Privacy in the Internet Economy, Docket No. 140514424-4424-01, at 4 (Aug. 5, 2014), available at http://www.laweconcenter.org/images/articles/tf-icle_ntia_big_data_comments.pdf

Senator MORAN. Ms. Rich, you say there are gaps. Does some other agency then fill in, or the gaps are unintended and need legislative attention?

Ms. RICH. The gaps need legislative attention. They aren't filled in by anybody else. If the data security isn't covered by the FTC Act, which covers unfair and deceptive practice across most of the marketplace, others can't fill that in. For example, there is a huge gap in that the FTC lacks jurisdiction over common carriers, entirely over common carrier activity. And the FCC's jurisdiction over common carrier activity does not cover everything that carriers do, so there are gaps there. And there are many other gaps that I can assist the Committee in if you need it.

Senator MORAN. Should Congress—I know, Ms. Parnes, you have comments, and I welcome them—should the Congress then repeal or modify the common carrier exclusion?

Ms. RICH. The Consumers Union would very much support the repeal of the common carrier exemption, which really hampers the FTC's ability to fully protect consumers in that area, and we also support enactment of a comprehensive data security law that would apply across the marketplace, it wouldn't just be data breach, it would apply to common carriers, it should apply to non-profits, and it should also have strong civil penalty authority, which the FTC, for the most part, lacks right now.

Senator MORAN. Others? Ms. Parnes?

Ms. PARNES. Thank you. Thank you, Mr. Chairman. So I think that one of the things that I would like to add is that it is true that the Commission enforces a number of sectoral laws and that Section 5 of the FTC Act is incredibly broad and does give the Commission the authority to reach virtually all other sectors of the economy, and, as Jessica notes, other than common carriers, which is a very, very big gap.

I think that the Commission has for many years supported repeal of that exemption, and it is a recommendation that's included in the task force report as well. I think it would go a long way toward addressing potential inconsistencies in enforcement, which is also a very big problem when you're looking at kind of a level playing field.

Senator MORAN. Thank you. Anyone else?

[No response.]

Senator MORAN. I'll turn then to Senator Blumenthal.

Senator BLUMENTHAL. Thanks, Mr. Chairman.

I have just received, as a matter of fact, while the Chairman was asking his questions, a response to a letter that I wrote to Equifax asking a number of detailed questions regarding the data breach. And the response from Paul Zurawski, Senior Vice President of External Affairs, which I will ask be made a part of the record—

Senator MORAN. Without objection.

[The information referred to follows:]

EQUIFAX
 Atlanta, GA, September 25, 2017

Hon. RICHARD BLUMENTHAL,
 United States Senate,
 Washington, DC.

Dear Senator Blumenthal:

I am in receipt of your letter to Mr. Smith dated September 11, 2017 in regard to Equifax's announcement of a cyber security incident. Thank you for your letter and please let me respond on behalf of Equifax.

We deeply regret this incident and apologize to every affected consumer. Protecting the security of information in our possession is a responsibility we take very seriously, and we are committed to making this right. We are all working diligently to support consumers and make the necessary changes to minimize the risk that something like this happens again.

With respect to our Congressional leaders, we are working cooperatively with a number of Congressional committees. We will continue these efforts in the coming weeks as we respond to questions and requests regarding the security incident and as we prepare for the upcoming Congressional hearings.

Thank you again for your letter and for sharing your questions and concerns.

Sincerely,

PAUL ZURAWSKI,
 Senior Vice President, External Affairs.

Senator BLUMENTHAL.—essentially says they're not going to respond to my questions. They're, quote, "working diligently to support consumers and make the necessary changes to minimize the risk that something like this happens again. We are working cooperatively with a number of congressional committees. We will continue these efforts in coming weeks as we respond to questions and requests," et cetera, et cetera.

So essentially they're saying they'll respond to committees. I would respectfully suggest that our Committee, I know that you don't have jurisdiction or authority to make this decision, but I hope that this Committee will have a hearing and that we will have those officials of Equifax come before us to be where you are sitting to answer these questions. And I'm disappointed that they haven't provided responses to my questions.

And I gather, Ms. Rich, that you agree that Section 5 is insufficient right now to protect privacy and ensure data security and that Congress ought to act to fill the gaps.

Ms. RICH. Absolutely. Section 5 may cover the breach that occurred, but then there are no penalties or proper deterrents under Section 5. It would just be an order after the fact, as we've noted.

The Fair Credit Reporting Act, which could govern this breach, has penalties, but it's by no means certain that this breach may fall within the Fair Credit Reporting Act. So the FTC has to do this careful analysis and balancing act to see whether one of these laws would apply when there seems to be enormous agreement across Congress and elsewhere that data security is a value every company should follow.

Senator BLUMENTHAL. Well, as about 143 million Americans are struggling and scrambling and deeply worrying about identify theft and criminality against them, I hope to fill that gap with legislation, I'm going to be introducing it this week, that would ensure that the FTC can investigate any data breach and exercise oversight and deter these kinds of breaches through negligent or careless practices by imposing strong and stringent penalties. I'll be in-

roducing that legislation this week, and I hope that it will have bipartisan support.

Is there anyone here who feels that such legislation should not be adopted?

Yes, sir, Mr. Szóka.

Mr. SZÓKA. Well, I would note, first of all, that if we want to make consumers whole, penalties don't do that; restitution is what does that. And the FTC has broad powers today to obtain restitution. That's the conversation that Lydia was just alluding to.

Senator BLUMENTHAL. Well, restitution is fine, and I agree that restitution should be made to anybody who is harmed, but restitution is usually inadequate, and, most importantly, it does not deter because it is insufficient to send that message that they need to do better. That's why we have penalties. And I think Equifax, you know, potentially could be criminally liable here. Criminal liability offers no restitution, it never does, but it sends a message and it deters that kind of misconduct in the future.

Mr. SZÓKA. So, Senator, I agree that there should be a remedy here, and I would just note again that losing 30 percent of your market capitalization is a far larger penalty than the government is ever going to be able to impose against a company like that.

So we should just note that there are many forces at work here. As you know, criminal law also plays a role. My concern in general with giving the FTC broad civil penalty authority for first-time violations boils down to this: The FTC deals with a wide range of conduct, and in many cases involving technology, it's not inherently nefarious conduct; we're not talking nefariously intended actors here. And then the problem is if you bring down the potential of civil liability on all of those parties, you—

Senator BLUMENTHAL. I just want to make the point to you, first of all, market value goes and it comes. It's not a finite penalty. But, second, maybe more important, market value decreases are a penalty not for the management that violated consumer trust, it falls on the shareholders. Now, you can argue that penalties do the same, but if those penalties can be assessed against individual managers, even if they're only civil penalties, they would send a strong message.

Mr. SZÓKA. Well, I would be even more concerned—I mean, it sounds great in theory to start talking about applying civil penalties against individuals, but if you apply that across the wide range of American businesses in a question of—now, we're not talking about someone intentionally defrauding a customer, we're talking about whether they've struck the right balance on how much data security they provide. That's a gray question. It may be in a particular case, it might be that a company really has had very lax data security, and they should be punished. But when you start talking about a general civil penalty authority, especially applied against individuals, it's actually very easy to see the sort of effect that could have, especially on small businesses and startups in the tech space.

Senator BLUMENTHAL. I'm going to yield because a number of my colleagues are waiting to ask questions, but perhaps we'll have a second round. And I appreciate your comments.

Senator MORAN. I just would inform the Committee that the full Committee is contemplating hearings mid-October on the topic that we're discussing and what Senator Blumenthal was suggesting.

The Senator from Oklahoma, Senator Inhofe.

**STATEMENT OF HON. JIM INHOFE,
U.S. SENATOR FROM OKLAHOMA**

Senator INHOFE. Thank you, Mr. Chairman. I was not here during the opening statements of Mr. MacLeod and Ms. Parnes, so I'll direct my questions—if you've already answered them, I want to hear it again.

So, Ms. Parnes, the Acting Director, Maureen Ohlhausen I guess it is, has prioritized connecting enforcement actions directly to concrete consumer injury. That's a novel idea. In your testimony, you note that the FTC has sought significant civil penalties, even when violations are unintentional and injury to the consumers is minimal or non-existing. In fact, it seems that the FTC sometimes seeks some action without regard to the underlying facts in litigation.

Do you believe that the consumer protection would be better served if the FTC aligned the penalties directly with the misconduct or harm? And I know your answer would be yes there. But then how do you do it?

Ms. PARNES. So I do agree with that, Senator. I think the FTC has the ability to obtain monetary relief in a number of situations; one is civil penalties. And the FTC Act very specifically says that a penalty needs to be related to injury, the degree of culpability, and the nature of the violation. But the Commission also has the authority to obtain equitable relief when it files actions in Federal court or settles with companies, and those settlements are entered into by a court. So in that context, the Commission can obtain restitution or can disgorge ill-gotten gains.

And so when the Report talks about monetary relief, it really is talking about all three prongs: civil penalties, disgorgement, restitution. And there's concern that the Commission has been seeking money generally and not tying it very specifically to the legal authority to obtain that monetary judgment and not really focusing on the extent of injury and the culpability of the defendants.

We're not suggesting—the Report doesn't suggest that money relief should be higher, that it should be lower, just that it should be considered within a more rigorous analytical framework.

Senator INHOFE. Yes. You're saying, though, that it doesn't really require a change in the existing law or—

Ms. PARNES. I don't think in this—

Senator INHOFE. Because it sounds to me like there's a change in the philosophy of those who are serving or in the case of the Obama administration, who had more tendencies toward more that type of regulation, that the language there that set this up is broad enough that it can be interpreted by the members. But my question would be, to preclude this from happening again, wouldn't it better—isn't there something that can be done legislatively that would be imperative? You might give some thought to that, and for the record, since my time will expire if I keep talking.

Mr. MacLeod, the enforcement actions by the FTC make headlines, but when the FTC is empowered with all of its other tools,

the tools at their disposal, to achieve its mission of preventing unfair competition in commerce, some of those tools include policy advocacy, business and consumer education, guiding research efforts, and convening experts to think through difficult issues.

Now, would the increased use of these tools in lieu of enforcement action to help protect consumers and ensure that small businesses and entrepreneurs are empowered to work with the FTC?

Mr. MACLEOD. Senator, I think the answer to that question is an emphatic yes. The——

Senator INHOFE. Are a lot of these not used, a lot of these tools that are out there?

Mr. MACLEOD. They are not used as often as I think they could be and should be. The Commission over the years has been a very powerful force for advising and spreading knowledge about the benefits of sensible law enforcement and about the cost of law enforcement gone awry. And one of the important things the Commission has been able to accomplish over the years has been to achieve a consensus among policymakers, law enforcers, enforcement agencies, as to an appropriate consumer-friendly approach to consumer protection. This is an economic issue, it's a legal issue, and it's something which I think the Commission could do in much more vigorous fashion than it has recently.

Senator INHOFE. Yes, I think so, too. And, well, my time is expired, but I'll have a question for the record on privacy that I'll submit at the appropriate time.

Senator MORAN. Thank you, Senator.

The Senator from West Virginia.

**STATEMENT OF HON. SHELLEY MOORE CAPITO,
U.S. SENATOR FROM WEST VIRGINIA**

Senator CAPITO. Thank you. Thank you, Mr. Chairman.

And thank you all for your opening remarks and for being with us here today.

I'm going to go back to the Equifax situation, realizing that almost half of my entire State of West Virginia was impacted by that. And then there has been a recent story about the SEC having a data breach. And I know this question has been asked sort of around, but I'm going to ask it again.

Ms. Parnes, with your experience at the FTC, you know, prevention is where we want to go. And also investigation of these data breaches. What other recommendations would you have to try to avoid these kinds of situations?

Ms. PARNES. It's a tough question. And I actually think that one thing that the Commission has started doing is to provide much more guidance to industry. They've begun to do this. I think it's a really important effort. I think companies need to understand what types of security measures are critical. But, you know, the truth is that no company wants to kind of throw its consumer data out into the public.

Senator CAPITO. Right.

Ms. PARNES. I mean, my sense is that companies that are subject to these major data breaches, they are attempting to keep data safe, and it is a big, big challenge. Frankly, my sense is that

issuing additional rules about what companies should do or should not do would not really solve this problem.

There are industry standards that are set. There are NIST standards and there are ISO standards that companies follow in terms of setting up their comprehensive data security programs, and those procedures, they're process-based, and they change on a regular basis. And it would be impossible, I think, to set a regulation that says this is what is the right data security. Five years ago, maybe we thought that complex passwords were good data security. Maybe 2 years ago, what we considered was two-factor authentication.

Senator CAPITO. Right.

Ms. PARNES. You know, maybe in a couple of years we'll be using facial recognition or some kind of biometrics to identify people. A rule would freeze the security measures in place.

Senator CAPITO. Right. So the technology needs to go—

Ms. PARNES. Absolutely.

Senator CAPITO.—and innovation. I'll get back to you in just a minute because I have one other question I wanted to ask Mr. MacLeod.

I don't even know if this is a proper question for this hearing, but because you mentioned advertising, it made me think about this. We all get these phone calls into our phones from these numbers that look like they're your next-door neighbor, you know, it says it's from Charleston, West Virginia, where I live, and if you make the mistake of picking it up, it's a voice trying to sell me relief on my student loan. Well, I don't know if you can tell by looking at me, but I haven't had a student loan for many, many years.

So my question is, does the regulatory framework to try to control those kinds of things come from the FTC? The FCC? CFPB? And if it's all of the above, what kind of regulatory coordination are we seeing here? Because you can see a scenario where, "Well, it's not really my bailiwick, it's more theirs."

Do you see this as a conflict? And how do we get around those kinds of things?

Mr. MACLEOD. This I don't see as a conflict, this I see as a major challenge that law enforcement has faced for as long as I have observed it. And it's a little bit like bank robberies and car thefts, we are always going to see these things. The Federal Trade Commission has done some very valuable work and has brought some very big cases against robocallers and other fraudsters using the telephone—

Senator CAPITO. Right.

Mr. MACLEOD. but there has also been some pretty impressive law enforcement coming out of the Department of Justice and local criminal authorities. These folks should go to jail. The Federal Trade Commission can't do that, but some of this is just outright fraud that is no different from robbing a bank except it's taking it from consumers.

Senator CAPITO. To this Committee's credit, we have looked at this issue of phantom calls or where they're using phantom numbers, I can't remember the exact title of it, but we have tried to look into that to try to cut that off as an avenue for fraudulent

marketing and I would say misuse of privacy, too, if you're getting into somebody's cell phone to get that.

Ms. RICH. I——

Senator CAPITO. Yes, Ms.——

Ms. RICH. Robocalls and unwanted telemarketing calls are an area where the FTC and the FCC have worked really closely together. And, in fact, my organization has been somewhat critical of the current FCC. But one thing that the FCC is doing is more to allow the phone companies to block these types of calls, and they've got a bunch of rulemaking underway to push forward in that area, and we're very supportive of that. And this is an area where the two agencies have worked very harmoniously together to push on different angles.

Senator CAPITO. Thank you.

Thank you, Mr. Chairman.

Senator MORAN. Senator Young.

**STATEMENT OF HON. TODD YOUNG,
U.S. SENATOR FROM INDIANA**

Senator YOUNG. Thank you, Mr. Chairman. Thanks so much for holding this timely hearing on the FTC reform proposals intended to improve innovation and consumer protection.

The FTC is important to the safety of all American lives, especially Hoosiers, when it comes to keeping data secure and safe. And we have recently, of course, been reminded of the extraordinary risk of personal information being compromised by the massive data breach at Equifax.

In my home state, that breach affected 3.8 million Hoosiers. Now, that sounds like a big number, and that's because it is. That breach has compromised the personal information of nearly 60 percent of the people I represent.

What's unique about this breach is the nature of the information that Equifax and all credit reporting agencies have on the American people and the fact that most Hoosiers have absolutely no idea what they have. It's a case of 143 million Americans, many unknowingly, having their sensitive personal information maintained by a credit reporting company compromised to an unprecedented level.

Now, given the nature of the breach, the criminals who stole this information could easily apply for fraudulent loans and open bank accounts and credit cards and engage in other nefarious activities. Not only that, but with just part of the information stolen, scam artists are now armed with new information to more credibly target senior citizens and other vulnerable people, which, frankly, is all of us today, in our communities. Part of the problem is that the FTC has failed to provide clear guidance on data security to American businesses. Their approach is to receive a feedback loop from the courts—inadequate to signal to the business community what they must do to keep Hoosier information safe.

But it's not all the FTC's fault. Congress itself has fallen short in providing a bipartisan solution to this problem. And so I'm calling, Mr. Chairman, on this Committee to hold a hearing on the Equifax data breach, and I have a sense that that's going to be forthcoming fairly soon. You may have already discussed that——

Senator MORAN. We expect the full Committee to have a hearing on this topic mid-October.

Senator YOUNG. That's really encouraging, so thank you.

Mr. Szóka, you mentioned in your testimony you'd like to see the FTC implement process reforms that make certain consumers' data and privacy are afforded the greatest protection possible. Candidly, Hoosiers I spoke with after the Equifax data breach don't feel like that's the case right now, understandably.

You also referenced the FTC's very different approach to the Green Guides and how this might be a better model when approaching data and privacy.

What steps can the FTC take today to begin addressing this issue in a tangible way? And how can the Green Guides provide a better model for addressing these issues?

Mr. SZÓKA. Well, thank you. Thank you for asking, Senator. The conversation about agency process reform is often framed as a conversation about whether an agency should do more or less. I just want to disabuse everyone of that notion. I actually think that process reform is important precisely because it would encourage the agency not just to be more active, but to do a better job of explaining what good data security looks like.

So the reason that I think it's important that we get some litigation here and that we undertake process reforms to make sure that happens is that the courts will actually force the agency to do a better job of explaining itself. So that is one track. And the goal is clear guidance to companies so they know what they need to do to provide good data security.

What we're talking about here is negligence. So some companies are, of course, negligent, just as people across the economy are. We need clear guidance to them to encourage them not to do that. And I think we start there before even getting to the conversation about penalties.

And then, Senator, I think you're asking the right question. What is notable here to me is that the FTC has been dealing with data security now for 15, 16, 17 years, depending on how you count, and it has never done what it has done in the context of the Green Guides.

The Green Guides represented, to my mind, the best, most rigorous, most thoughtful attempt by the agency to study a new area of, in that case, it was how companies were making claims about the environmental benefits of their products, whether they were recyclable and so on, and to gather data and study, what do consumers understand? What do they expect? And what should companies do? Right? If the FTC were to have done that 16 years ago, I think we'd be in a very different place today. I think companies would have much clearer guidance and the data security would be better.

It's not too late for them to start. And that's what Commissioner Ohlhausen's workshop offers now.

Senator YOUNG. Are there additional statutory authorities, say, the FTC would need to ensure that these sort of breaches don't occur in the first place, to your mind?

Mr. SZÓKA. Well, they don't need any changes at all to do something like the Green Guides, I want to make that very clear. So

there are two separate conversations here: one is what Congress should do, and the other is what the agency itself should do with the tools it has today. But, yes, I think there are some statutory changes.

I do agree that there is a problem surrounding the common carrier exception. I think the Committee needs to study that, and I've explained that in my testimony. There are a range of options. Ending the exception altogether is one end of the spectrum of options. At the other end, we absolutely need to make sure that the Commission is at least able to go after the data security and privacy practices of companies that provide both a common carrier service and a non-common carrier service. That non-common carrier service, like broadband is about to become again, needs to be within the FTC's jurisdiction. So I would certainly support that kind of change.

Senator YOUNG. Ms. Rich, I see I'm over time here, so—

Ms. RICH. I just want to make one point, which is there is extensive guidance on data security that has been created over the years, and somebody here could probably pull it up on their phone and see all the guidance that the FTC has put out on data security. So I just wanted to correct that one point.

Mr. SZÓKA. If I may just quote briefly from the Third Circuit's decision in Wyndham in 2015. "At oral argument, we asked how private parties in 2008 would have known to consult the guidance that the Commission had issued or its consent decrees. The FTC's only answer was, 'If you're a careful general counsel, you do pay attention to what the FTC is doing and you do look at these things.' We also asked whether the FTC has informed the public that it needs to look at complaints and consent decrees, and the Commission could offer no examples."

I mean, if the Commission is pointing to its settlements, it's putting out guidance, that is not the same thing as the Green Guides, which, for example, involve 314 pages in the last update where the Commission explained why it was recommending certain things, and went into detail. That would be quality guidance that would encourage the high level of data security that Americans should enjoy.

Senator YOUNG. Thank you all.

Senator MORAN. Senator Hassan.

**STATEMENT OF HON. MAGGIE HASSAN,
U.S. SENATOR FROM NEW HAMPSHIRE**

Senator HASSAN. Thank you, Chairman Moran and Ranking Member Blumenthal.

And thank you all to the witnesses for being here today.

Ms. Rich, you state in your testimony that some of the recommendations from the American Bar Association's report—and this is a quote "would limit the FTC's effectiveness in protecting consumers." Could you explain for the Committee which of the ABA's recommendations would do so and how?

Ms. RICH. I'll mention two. The ABA report suggests that both administrative and Federal court orders should be as short as 5 years. The longer orders are very important for deterrence, especially where many of the orders actually have no money. So the dis-

cussion today about how the money is disproportionate to the injury just bear no relation to what really happens, which is often the FTC can't get money back to consumers.

So most cases address fraud or straightforward deception warranting long orders to make sure they don't do it again. The FTC has been able to cite instances where companies violated their order after 15 years, at least 10 instances of that. And it's just very important for deterrence. So that's one.

The second is the argument that we've heard that monetary relief is too high. As I mentioned, most of the time, it's really too low. Consumers don't get their money back. The company has already spent the money. They claim inability to pay. It's very frustrating bringing a case and not being able to return money to consumers.

If it's not a hardcore fraud case, but if a company deceived consumers, it's fine to say, "Well, it wasn't intentional," but who should have that money? Should it be the company that deceived the consumers, or should consumers get their money back? The FTC should give the money back to consumers who were deceived. And far from there being no systematic way to calculate the money, there are rules governing how you calculate civil penalties. If consumers lost money, and the FTC is returning it, they calculate how much money consumers lost, and try to get that back to consumers. So those are the two issues.

Senator HASSAN. Thank you. I want to go back to the issue of overlapping or sometimes siloed jurisdictions. Earlier this year, Congress utilized an arcane tool known as the Congressional Review Act to undo critical privacy protections for consumers by the Federal Communications Commission.

The FCC and the FTC play complementary roles in protecting consumer privacy. The FCC protects consumers when they use their broadband connection. The FTC protects consumers using websites and social media and so on. People in my home State of New Hampshire and most Americans I talk to really don't want their private and personal data used or sold without their consent just to line the pockets of Internet service providers.

So, Ms. Rich, how important is it that the Federal Trade Commission work with the Federal Communications Commission to protect consumers' privacy in our data-driven society? And how can these agencies collaborate to protect consumers from bad actors?

Ms. RICH. It was very unfortunate that the broadband privacy rule was rolled back. That was a very important rule to protect consumers in an area where the ISPs have extraordinary access to consumer information. Many consumers do not have choice in who their ISP is. And consumers really do care about this issue, as we saw after the rule was rolled back.

The FTC and the FCC have long worked together in a complementary way. They have different authority. For example, the FTC can get redress. The FCC gets penalties. They have different jurisdiction over different entities, as you note. So they've done joint work on cramming, on robocalls, on privacy, and that's been very important. Unfortunately, right now, with the rollback of the privacy rule, consumers have very weak protections over their ISP privacy, and right now, because of the Federal order and various

other things, the FTC completely lacks jurisdiction over carriers at all.

So consumers are the losers. Consumers have virtually no protections in this vital telecom space for their data. And it's something that needs to be repaired by repealing the common carrier exemption.

Senator HASSAN. Thank you very much.

And thank you, Mr. Chairman.

Senator MORAN. Thank you, Senator.

Senator Klobuchar.

**STATEMENT OF HON. AMY KLOBUCHAR,
U.S. SENATOR FROM MINNESOTA**

Senator KLOBUCHAR. Thank you very much, Ms. Rich—this hearing.

And thank you to the Chairman and Ranking Member.

This hearing is focused on the FTC's consumer protection mission, and I am the Ranking Member on the Antitrust Subcommittee in Judiciary. And I appreciate Consumer Union's work in this area. Particularly, you've been supportive of the paper delay bill that I have with Senator Grassley to stop the practice of pharmaceuticals paying off generics to keep their products off the market, which means no competition for consumers, costing the CBO score \$2.9 billion to the government in 10 years.

And I also appreciate the statement and letter from the Consumers Union on my two recent antitrust bills that I introduced. And Senator Blumenthal was helpful with that.

Ms. Rich, can you explain why strengthening merger enforcement is important to Consumers Union?

Ms. RICH. Yes. And thank you for your leadership. We were delighted to see that you were moving forward on these important issues.

So antitrust enforcement is extremely important for the free market to work, giving consumer choices, keeping prices down. There is a growing concern among many that the market is too concentrated right now. That harms consumers, it harms businesses, it harms small businesses, startups, suppliers, workers, and the overall economy.

We, at Consumers Union, have expressed concern that enforcers have too high a burden to show that mergers will cause immediate harm, while disregarding the kind of cumulative harm that mergers and the trend toward bigger is causing. So we do think it's a very important issue. It's time to look closely at this area. And we thank you for your leadership on it.

Senator KLOBUCHAR. OK. Senator Hassan asked you a bit about the FTC and the FCC and the issue of data, and I think we know how hard these cases can be and how complex they are. And I always believe that our government, if we want to even the playing field against fraudsters, have to have as much sophistication in the law and the tools that we use as the people that are committing the crimes. So does the FTC have the resource it needs, resources that it needs, to adequately protect consumers?

Ms. RICH. It has a lot of expertise in that it has its own tech shop. It has a chief privacy and technology officer. And it has been

bringing these cases in the data security area, which has been the subject of discussion for a long time, and it has been bringing fraud and deception cases.

But there are some areas—and the ABA agreed with some of this—where the FTC really needs stronger tools. It needs jurisdiction over common carriers very badly right now for consumers' benefit. I think consumers deserve general data security legislation, which we've all been talking about with tough penalties to plug the holes, and, frankly, privacy legislation, which is for maybe another hearing, and stronger rulemaking authority. It's very important that when laws are passed, it gets ABA rulemaking and not something more difficult or something that doesn't allow the FTC to change a rule with time to make sure it keeps pace. It needs stronger remedies for consumers, including strong penalties in many instances. And more resources. I'm done.

[Laughter.]

Senator KLOBUCHAR. No, very good. Thank you.

Mr. MacLeod, changing the subject a little bit here. On July 17th, the FTC announced reforms to its civil investigation demands process to add more clarity, streamlining it. While CIDs are an important part of the investigative process if not tailored appropriately, which I think is why you did this, they did this, they can create unnecessary burdens that can be especially difficult for small businesses. What effect will these reforms have on how businesses comply with civil investigative demands?

Mr. MACLEOD. We are very encouraged at this announcement that came from the FTC. This included some of the recommendations that we had in our report. So we are looking forward very much to see how these announcements will play out in the orders.

It is hard to exaggerate the effect of a broad CID on a company. It can take months. It can divert the top leadership. And if it is not reasonably necessary to get the Commission the evidence that it needs, then it ought to be diverted.

Another point that we recommended that has not yet been addressed by the Commission, but which is, we think, very important, is that it is very difficult for a company to contest the scope of a CID because when one moves to petition or quash a CID, that's when an otherwise non-public investigation becomes public. You may never have violated the law, but all of a sudden you are litigating in public over a Commission investigative demand, and that is a very difficult thing for a company to do.

Mr. SZÓKA. Senator, if I could just note, LabMD, the small cancer testing lab that has been in litigation with the FTC, they started to go out of business the day they decided to fight back against the CID because it was that public revelation that caused them to lose the insurance that made their business possible.

So the stakes here really are very high. When I talk about the reputational consequences, you know, we could talk about maybe Equifax could survive losing 30 percent of its market cap, but a small business, you know, once that fight goes public or once even a small corporation has to notify its shareholders that they're now subject to investigation, it's over.

So we need to keep in mind that we can give—keep the FTC with those broad powers, but if the FTC is able to use those powers to

coerce settlement, that's what changes this from a true common law process into what we have today.

Senator KLOBUCHAR. Thanks. I have questions that I'll ask on the record about the senior fraud bill I have with Senator Collins. Maybe I'll give them to all of you so I can be fair and equal and everything else.

So thank you very much, everyone.
Senator MORAN. Senator Markey.

**STATEMENT OF HON. EDWARD MARKEY,
U.S. SENATOR FROM MASSACHUSETTS**

Senator MARKEY. Thank you, Mr. Chairman, very much.

The arguments that we are hearing today to limit, limit, the Federal Trade Commission's authority are yet another reason why the Federal Communications Commission must stop its harmful proposal to rescind net neutrality protections. If the Federal Communications Commission reclassifies broadband as an information service, the Federal Trade Commission would regain jurisdiction over broadband and net neutrality.

So here is the broadband giant's industry formula: Give the Federal Trade Commission authority over broadband, and then gut the Federal Trade Commission's authority to protect competition and innovation. That's their ideal scenario. You can put that on a 3-by-5 card as a business plan for the broadband giants.

Now, the big broadband industry and their allies say the Federal Trade Commission provides a light-touch regulatory framework. So what do they mean when they say a "light touch"? Well, what they mean is hands off, hands off the broadband companies' ability to choose the online winners and losers because they know the Federal Trade Commission currently does not have the authority to establish net neutrality protections.

The Federal Trade Commission only enforces policies companies create for themselves, and brings enforcement action if, and only if, a company violates those policies. But if a broadband giant has a policy that says you have no net neutrality protections, well, there's nothing to enforce because it's not unfair and deceptive to say you have no protections, you're on your own.

So the Federal Trade Commission is then left with no ability to be able to protect people from having their rights, as consumers, being compromised. And if that's not a sufficient guarantee for the broadband giants, Congress is now considering proposals to actually undermine the Federal Trade Commission's limited enforcement authority.

So, Ms. Rich, shouldn't the Federal Communications Commission really protect the free and open Internet? Isn't that where the jurisdiction should be, given the limited ability, which the Federal Trade Commission has legally?

Ms. RICH. Absolutely. In this case, I would note that the carriers, or particularly AT&T, have simultaneously been arguing that the FTC should have jurisdiction over this issue, but fighting the FTC in court, which is what led to the FTC losing jurisdiction over carriers. So I do think it's just a matter of not having net neutrality addressed at all.

This is an area where it makes sense to have clear rules of the road across the entire industry. The rule, the net neutrality rule, put out was very clear. There are gaps, serious gaps, in what the FTC can do on net neutrality, so absolutely.

Senator MARKEY. OK. So let me ask you this, Ms. Rich. OK. So can the Federal Trade Commission, like the Federal Communications Commission, through affirmative rulemaking authority, ensure that broadband providers do not block, prioritize, or slow down online contact? Can the Federal Trade Commission do that?

Ms. RICH. The FTC does not have general rulemaking authority to do that.

Senator MARKEY. It has no ability. So on privacy, can the Federal Trade Commission, like the Federal Communications Commission, through affirmative rulemaking authority, require the broadband giants to receive user consent before selling browsing history?

Ms. RICH. The same answer, no.

Senator MARKEY. No, they don't have that authority. So let's then move over to—because so far the Republicans have brought out a repeal of the FCC rule to protect privacy of Americans that broadband companies had to provide them, they've already repealed that. Now we move on to this next front, and crocodile tears being shed about Equifax, "Oh, how can this happen in America?" You know, one of my staffers right behind me was just telling me that his information was compromised on Equifax, which might be the reason I'm asking this next question.

[Laughter.]

Senator MARKEY. Earlier this month, Equifax was subject to a cyber attack that compromised the personally identifiable information of 143 million consumers. This massive data breach has exemplified the total lack of consumer recourse when their sensitive information, names, Social Security Numbers, birthdates, addresses, is stolen.

Ms. Rich, should data brokers be required to develop comprehensive privacy and data security programs, and to provide reasonable notice to end the case of breachers?

Ms. RICH. As a general matter, absolutely, yes.

Senator MARKEY. OK. And that's why I have introduced with Senator Blumenthal the Data Broker Accountability and Transparency Act, to give consumers meaningful control over their sensitive information. So instead of debating whether to take authority away from the Federal Trade Commission, we should instead be discussing how we will give more authority to the Federal Trade Commission to better protect consumers in our increasingly digital world where people's most sensitive information is bought and sold on the black market.

We're having the wrong conversation in this room. The public is wild that 143 million people's, you know, credit can be compromised, and rather than saying, "We're going to come in here and ensure that the rules and regulations are in place, that it never happens again," instead, you know, we are just pretending that we don't have the ability to be able to respond to that. And it's just a part of a pattern that we saw with the repeal of the Federal Communications Commission's authority to protect the privacy of broadband consumers. So all that information just becomes a prod-

uct to be sold by the broadband companies for their own profit. It's just plain wrong and I think it's fundamentally un-American. It's just plain and simple wrong that people can't have protections of their most private, sensitive information.

Thank you, Mr. Chairman.

Senator MORAN. Thank you, Senator.

Senator Cortez Masto.

**STATEMENT OF HON. CATHERINE CORTEZ MASTO,
U.S. SENATOR FROM NEVADA**

Senator CORTEZ MASTO. Thank you, Mr. Chair, and Ranking Member Blumenthal.

So I appreciate this conversation because I served as the Attorney General for Nevada for 8 years, and one of my best partners was the FTC. And I don't support some of the recommendations that were made, and I want to talk about that.

And maybe, Mr. MacLeod, if you could enlighten me because you started with one of the cases that you actually defended, and it was a pesticide company. And the reason why I'm curious, because I know, I know, as the State of Nevada, we are involved in some actions against pesticide companies because they misused or mislabeled their pesticides, which could cause serious illness to humans and be toxic to wildlife.

And the reason why we have consent decrees, the reason why we enter into these agreements, is to change that conduct, to protect the consumer forever, not for 10 years, not for 20 years, it's forever. You want to change that conduct, you want to make sure they're not going to engage it in the future for monetary gain.

And so I'm curious your thoughts on that. Are you looking at—are you saying that that long-term oversight and that change of conduct is burdensome to these companies or—if you don't mind giving me your thoughts.

Mr. MACLEOD. The FTC orders typically go well beyond telling a company not to violate the law. They impose numerous affirmative requirements that over time can end up having very little relevance to the world in which a company is operating.

The point that we made in our report, which I think is very important to emphasize, is that we are not suggesting that every order be a limited order. There are some con artists out there who could well deserve what they sometimes get from the FTC, and that's a lifetime ban from participating in an industry.

On the other hand, when there are orders that require a company—Toys “R” Us is a perfect example of a company that petitioned the FTC, probably spent tens of thousands of dollars, 16 years after it had entered an order, to try to get relief from some of the fencing-in provisions that just restricted Toys “R” Us and made it a less effective competitor to Amazon, to Target, and to some of the other retailers. And the FTC ultimately said, Yes, we see no reason for all these extra provisions in the order anymore. Our point is that 16 years after an order has been entered, you probably don't need to require a company to petition the FTC or petition a court to be treated like everybody else in its industry.

Senator CORTEZ MASTO. Thank you.

Ms. Rich, do you have any comments to that?

Ms. RICH. One important issue is that some of these affirmative requirements in the order that Bill is talking about expire well before 20 years; they are 5 years, they are much shorter. So the rest of the order is largely, in many of these cases, an obey-the-law order. And I don't know the particulars of the cases that Bill is mentioning. I assume they were Bill's clients. So you know, you have a particular perspective, but I would love to hear the perspective of those that brought the action against the companies.

Senator CORTEZ MASTO. And I appreciate that because as I read through the report, knowing from my perspective, as somebody from the attorney general's office for 8 years that was focused on consumer protection and worked closely with the FTC, there is give-and-take. I know I was in meetings with the corporations before the consent decrees were entered into.

The last thing we wanted to do was bring litigation, so we were trying to change the conduct to address any monetary component, to hold them accountable, and deter their conduct in the future, but they were in the meetings with us. We were in roundtables talking about how we address this. And then when we entered into an agreement, it was brought before a judge. And if anybody disagreed with it, then the judge would help us make that determination.

So it's not like there isn't negotiation, it's not like there isn't some give-and-take at the end of the day. So to say that we should be eroding the FTC's enforcement and tools to the benefit of corporations that somehow they are not in the room at the beginning when we're talking about this, I don't understand.

Now, with that said, I also get—sometimes you're on the other side of a negotiation with somebody from the FTC, a staffer, who may not be reasonable or who may not be willing to sit and talk with you, and I think those are times where then you're going to reach above their heads or try to figure out how you address that. I get that. I get that. And I've seen that happen in government, but at the same time, that doesn't mean we erode the tools for law enforcement to do the jobs that they need.

So, Ms. Parnes, and then, Ms. Rich, please, I'd love to hear from you.

Ms. PARNES. Thank you, Senator. Just, you know, kind of some context on this. I mentioned that I was at the FTC for 27 years, and in the mid nineties, I was the Deputy Director of the Bureau of Consumer Protection, and at that time, administrative orders, like Federal court orders, were perpetual in nature, and we all thought that's the way they should be. You know, this is how it's always been, and this is how it always should be.

And a new Chairman came in, Robert Pitofsky, and he said, you know, "I think we should revisit this, I think perpetual administrative orders need to be reevaluated." And there was that reevaluation. And ultimately the Commission decided to limit the administrative orders to 20 years with a lot of, you know, kind of bells and whistles around if a company violates the order during that time-frame.

I think the point is that in 1995, when this happened, a 20-year order, it was a significant change, but it seemed as if it gave companies the opportunity to kind of get it right. And then if there was going to be movement at the company, if there were changes in the

way the business was operating, just life didn't move as quickly back in the mid nineties. And our sense is that because things move so much more quickly now, that it makes—certainly makes sense to re-evaluate the length of these orders and to consider a shorter order, and we did put a shorter timeframe in our recommendations.

I don't think that anybody who was involved in drafting this report looks at this as in some way trying to weaken the Commission or its use of its enforcement authority.

Senator CORTEZ MASTO. Thank you. And I know my time is up, but I'd like to hear from Ms. Rich if that's—with the Chairman's indulgence.

Ms. RICH. I just want to bring the focus back on consumers because there has been a lot of talk on the burdens on businesses, but keep in mind that in the vast majority of orders here, we're talking about situations where consumers were either ripped off or harmed in other serious ways, and these orders are designed to return money to consumers and make sure these companies don't do it again.

In addition, the processes at the FTC are fairly extensive in terms of how many bites of the apple you get to appeal through the chain and make your arguments to different people. And so that's an opportunity that people don't have at all Federal agencies, and companies really do make use of that to try to change what they may disagree with the staff. And there also is an opportunity for order modification over time.

Senator CORTEZ MASTO. Thank you. I appreciate the comments. Thank you very much for the conversation today.

Senator MORAN. We're about to conclude our hearing. Let me turn to Senator Blumenthal and see if he has any closing comments.

Senator BLUMENTHAL. I appreciate all of your testimony here today, and I look forward to hearing your comments on the legislation that we're going to propose. I think all of you, I hope all of you, would agree that restitution is often appropriate even where there is no precise or provable harm to consumers as when a Social Security Number is stolen, it's out there, its value depends on its security and its confidentiality. And so Equifax, in my view, should be held accountable and made liable for the loss of privacy as to those Social Security Numbers, even for consumers who may not be able to prove a precise loss due to identity theft. I hope you would all agree.

Thank you. That concludes my questioning.

Senator MORAN. Thank you, Senator Blumenthal.

I had hoped to ask some questions at least about mergers, but I'll submit it for the record. Let me take just a moment to tell you I was significantly impressed by the quality of the panel. Thank you all very much for testifying. You're all very articulate, very intelligent, and seemingly have experiences that are of great value to us as we figure out the right public policy related to the FTC.

With that, the hearing record will remain open for two weeks. During this time, Senators are asked to submit any questions for the record. Upon receipt, we'd ask the witnesses to respond as quickly as possible. With that, this concludes our hearing. And I again thank the witnesses. We are adjourned.

[Whereupon, at 4:02 p.m., the hearing was adjourned.]

A P P E N D I X

THE FTC AND PRIVACY REGULATION: THE MISSING ROLE OF ECONOMICS

GEORGE MASON UNIVERSITY LAW AND ECONOMICS CENTER

BRIEFING ON NOMI, SPOKEO, AND PRIVACY HARMS—NOVEMBER 12, 2015

Joshua D. Wright*

Introduction

Good morning, I am pleased to be here today for the Law and Economics Center's Briefing on Nomi, Spokeo, and Privacy Harms. I want to thank the Law and Economics Center for the invitation to speak with you today, and especially my colleague James Cooper. I'm very excited about his work here at the Law and Economics Center on privacy and economics. And it is nice to finally be able to give a speech where I do not have to begin with a disclaimer about how the things I am about to say are not the views of the Commissioner or any of its Commissioners.

Privacy is an ever-evolving and remarkably important regulatory landscape and it has been, unfortunately in my view, even more remarkably resistant to the influence of economics. As an antitrust economist, law professor, and practitioner, I see close parallels between privacy regulation and competition law and policy. The problem is that the closest parallels are to antitrust in the 1960s—before the influence of economics had made that body of law coherent as a consumer welfare prescription. That resistance to economics is harming consumers. We can do better. The FTC has the tools to do better right now.

I'm going to focus my remarks on how the FTC can and should integrate economics in assessing privacy regulation. I will also focus more specifically upon the FTC's settlement with *Nomi*. In particular, as I argued in my dissent in that case why a consumer-welfare focused and economic approach to privacy regulation requires that promises in privacy policies be proven rather than presumed material to consumers. Presuming materiality when actual evidence of consumer behavior suggests otherwise is even more misguided.

Economic Analysis of Privacy At The FTC

A primary goal of my tenure at the FTC was to encourage a deeper integration of economics and cost-benefit analysis into the consumer protection framework at the Commission. The hesitancy to fully incorporate economic tools into consumer protection analysis is discouraging, but not completely surprising given the Commission's portfolio of consumer protection work. It is important to understand where the reluctance and resistance comes from in order to know how to fix it.

The issue is not whether economics will influence privacy regulation, but when. So let me start with what is intended to be a provocative proposition: economic analysis of privacy will exert a significant influence on the development of law and regulation in this area within this decade. In the 1960s and 70s, antitrust lawyers and agencies too were reluctant to allow economic analysis to seep into their body of law. But as was the case with antitrust, it will simply be impossible for privacy—which is inherently economic regulation—to remain impervious to the insights from economics, such as how firms compete with respect to privacy protections, the effect of privacy regulation on consumer welfare and competition, and consumer preferences for privacy.

So let's begin with why the FTC has rejected an economic view of privacy thus far. The vast majority of work that the Bureau of Consumer Protection performs simply does not require significant economic analysis. In most consumer protection cases, the business practices at issue create substantial risk of consumer harm but

*Professor, George Mason University School of Law and Director, Global Antitrust Institute. I thank James Cooper and Beth Delaney for comments and Khouryanna DiPrima for research assistance.

little or nothing in the way of consumer benefits. A team of Ph.D. economists, or even one, is usually unnecessary in a simple fraud case. The FTC's consumer protection arm has "grown up" around its deception authority. The consumer protection enforcement culture at the FTC remains at its core one that contemplates its role as smiting out business practices that always harm consumers. That approach is substantively correct, intellectually coherent, and efficient when applied to business conduct like fraud that always harms consumers.

Applying economic theory in the consumer protection realm at all is a fairly recent development. Only in 1980, when the Commission adopted the Policy Statement on Unfairness, did it begin considering the benefits of various business practices on consumers. Under this revised standard, and as subsequently codified by Congress in 1994 in Section 5(n) of the FTC Act, the agency may pursue enforcement action on the basis of "unfairness," in cases where an act or practice "causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers themselves and not outweighed by countervailing benefits to consumers or competition." In reformulating its unfairness standard, the Commission recognized that in utilizing its authority to deem an act or practice as "unfair" it must undertake a much more rigorous analysis than is necessary when it uses its deception authority. However, even deception authority is not immune to the need for analysis. It too has a proxy for analysis of whether an unavoidable injury occurred—the "materiality" requirement codified in the Commission's 1983 Policy Statement on Deception, which I will discuss in a moment.

There are technological and economic forces that point toward an inevitable conflict between the old, fraud-based consumer protection culture at the FTC and the realities of the digital economy. For example, as we become fully immersed in the digital age, and as the Commission considers policy issues relating to topics such as the "Internet of Things," this conflict becomes apparent. On one hand, there are innumerable gains to consumers from new and enhanced products and services resulting from the Internet of Things, all of which depend critically upon the free flow and exchange of data. While on the other hand, there are privacy and data security concerns that may arise *because* of that free flow and exchange of data.

An economic approach to privacy regulation is guided by the tradeoff between the consumer welfare benefits of these new and enhanced products and services against the potential harm to consumers, both of which arise from the same free flow and exchange of data. Unfortunately, government regulators have instead been slow, and at times outright reluctant, to embrace the flow of data. What I saw during my time at the FTC is what appears to be a generalized apprehension about the collection and use of data—whether or not the data is actually personally identifiable or sensitive—along with a corresponding, and arguably crippling, fear about the possible misuse of such data.

This generalized fear of data takes many forms. And it has many costs. Any sensible approach to regulating the collection and use of data will take into account the risk of abuses that will harm consumers. But those risks must be weighed with as much precision as possible, as is the case with potential consumer benefits, in order to guide sensible policy for data collection and use. The appropriate calibration, of course, turns on our best estimates of how policy changes will actually impact consumers on the margin, not whether we can identify plausible yet speculative narratives about how particular business practices might result in consumer harm.

The failure to engage in a thorough and appropriate cost-benefit analysis that incorporates recent economic insights can lead to serious policy errors. And, unfortunately, the failure has maintained all too common in the FTC's consumer protection work involving the digital economy generally, and privacy regulation specifically. If the benefits of these welfare-enhancing business practices are not weighed correctly against the harms they present to consumers, we run the risk of squelching innovation and depriving consumers of these benefits. There is still serious resistance to adequately accounting for the full economic costs and benefits of various business decisions and practices.

The tendency appears to be to discount benefits, as is the case in the Internet of Things Report. As I noted in my dissent, the Report only "pay[s] lip service to the obvious fact that the various best practices and proposals . . . might have both costs and benefits," and places far too much emphasis on speculative and anecdotal risks without adequately assessing whether the benefits of these new technologies outweigh the concerns. Indeed, the Report seems to go out of its way to avoid discussing key components of how the Internet of Things is already improving society—for example, not adequately considering how consumer-facing Internet of Things devices fuel the development of smart cities, smart grids, and other socially beneficial technologies.

Other times, the Commission simply asserts that consumer benefits do not exist, as the Commission chose to do in justifying its settlement with Apple. In Apple, the Commission found unlawful Apple's decision to allow the entry of a password upon a first transaction to trigger a 15-minute window during which users could make additional purchases without reentering the password. The Commission's clear disregard for rigorous cost-benefit analysis in Apple is also apparent in various recent Workshop Reports produced by the FTC—for example, the Data Broker Report or the Internet of Things Report—that disseminate best practices and legislative recommendations without conducting such an analysis. In other contexts, the FTC relies upon slogans like “data minimization” and “security by design” to guide policy decisions—but those slogans and catchphrases simply don't bear any meaningful analytical content and their pursuit at any cost will simply mean higher prices and less useful products for consumers.

This is simply not good enough; there is too much at stake for consumers as the Digital Revolution begins to transform their homes, vehicles, and other aspects of daily life, not to mention the potential for addressing societal problems on a broader scale. What is needed to guide consumer-welfare enhancing privacy regulation is an economic and evidence-based approach sensitive to key tradeoffs between the value to consumers and society of the free flow and exchange of data and the creation of new products and services on the one hand, against the value lost by consumers from any associated reduction in privacy.

I've been fairly critical of the FTC to this point. But it is important to note that I do not view the problem with privacy regulation at the FTC to be a lack of talent or leadership. The FTC has a collection of highly talented consumer protection lawyers and the best collection of economists in any government agency. The issue is that the FTC is at a crossroads when it comes to consumer protection in the digital economy generally. An ever-increasing proportion of the business practices the FTC is asked to engage with on a daily basis are no longer the types of practice that can simply be dismissed as fraud and enforced without the fear that aggressive enforcement might chill virtuous competition.

While the FTC must always remain vigilant in identifying and prosecuting fraud, it is critical that it develop a sensible and more nuanced approach to business practices that might produce benefits for consumers. When it comes to privacy regulation, the fraud-based culture of the FTC's consumer protection mission cannot be robotically and mechanically employed where that framework no longer makes sense. Adapting the culture within any institution to recognize these changes and develop the human capital and skills to deal with them is always a tricky problem; and perhaps at its trickiest when that institution is a government agency. It will be no surprise that an economist who was formerly an intern within the Bureau of Economics believes that the key to changing the culture within the agency is to empower the economists. And I will close with a few suggestions along those lines.

But for now, I'd like to turn to *Nomi*, which is an important case with significant implications for privacy regulation, but is also in my view a misguided attempt to retrofit the fraud-based FTC consumer protection culture to an area of privacy regulation that requires economic analysis.

FTC v. Nomi Technologies

Nomi was a startup company that provided analytics services to retailers based upon data collected from mobile device tracking technology to brick-and-mortar retailers through its “Listen” service. Nomi uses sensors placed in its clients' retail locations or its clients' existing WiFi access points to detect the media access control (MAC) address broadcast by a consumer's mobile device when it searches for WiFi networks. Nomi passed MAC addresses through a cryptographic hash function before collection and created a persistent unique identifier for the mobile device. Nomi did not “unhash” this identifier to retrieve the MAC addresses and Nomi did not store the MAC addresses of the mobile devices.

The FTC's case against Nomi rested on a single line within its privacy policy that stated “Nomi pledges to . . . Always allow consumers to opt out of Nomi's service on its website as well as at any retailer using Nomi's technology.” Nomi did allow consumers to opt out of its service on the website, but the FTC argued that because some retailers did not have the ability to allow consumers to opt-out of tracking within the store, this statement was deceptive.

Importantly, yet completely ignored by the FTC majority, Nomi did not track individual consumers—instead, Nomi's technology recorded whether individuals are unique or repeat visitors, but it did not identify them. The information collected was used only to provide analytics to Nomi's clients. The data provided by Nomi's Listen service can generate potentially valuable insights that allowed retailers to measure how different retail promotions, product offerings, displays, and services impact con-

sumers. In short, these insights help retailers optimize consumers' shopping experiences, inform staffing coverage for their stores, and improve store layouts, all without knowing the identity of those visiting the store.

Let's talk about the law. Section 5(b) of the FTC Act requires us, before issuing any complaint, to establish "reason to believe that [a violation has occurred]" and that an enforcement action would "be to the interest of the public." In my dissent, I argued that the Commission did not meet the relatively low "reason to believe" bar because its complaint did not meet the basic requirements of the Commission's 1983 Deception Policy Statement. This failure has significant economic consequences because it runs the risk of deterring industry participants from adopting business practices that benefit consumers.

The fundamental failure of the Commission's complaint is that the evidence simply does not support the allegation that Nomi's representation about an opportunity to opt out of the Listen service at the retail level—in light of the immediate and easily accessible opt out available on the webpage itself—was material to consumers. This failure alone is fatal. A representation simply cannot be deceptive under the long-standing FTC Policy Statement on Deception in the absence of materiality.

The Policy Statement on Deception makes this requirement clear, observing that the "basic question is whether the act or practice is likely to affect the consumer's conduct or decision with regard to a product or service." It is important to understand the economic function of the materiality requirement. Once again, the FTC's own Policy Statement on Deception does our work for us when it describes materiality as an evidentiary proxy for consumer injury: "[i]njury exists if consumers would have chosen differently but for the deception. If different choices are likely, the claim is material, and injury is likely as well."

Now why would the FTC choose to enforce only those misrepresentations that are material—that is, misrepresentations that cause consumers to make choices that reduce their welfare? The answer is that this essential link between materiality and consumer injury ensures the Commission's deception authority is employed to deter only conduct that is likely to harm consumers and does not chill business practices that makes consumers better off. This link also unifies the Commission's two foundational consumer protection authorities—deception and unfairness—by tethering them to consumer injury.

Historically, the FTC has applied its deception authority in the context of advertising. In the advertising setting, the Commission enjoys a legal presumption of materiality. The underlying logic of that presumption is that advertising communications reflect the judgment and investment of the advertiser that the communication will indeed affect consumer behavior. But that logic simply doesn't fit in the context of privacy policies. Unlike advertising, privacy policies are not designed by marketers to influence consumer behavior, rather they are often drafted by attorneys and included on websites to comply with state laws or industry self-regulatory regimes. The logic of the materiality presumption built for advertising simply does not fit when evaluating representations in privacy policies.

The practical reality is that, while privacy policies do serve valuable functions, most consumers do not read privacy policies and when they do, they do not understand them. Researchers have shown that it is virtually impossible for consumers to read and understand all the privacy policies typically encountered, given the time commitment required. It is not surprising that according to a recent Pew Research Center survey, half of Americans believe that when a company posts a private policy, it ensures that the company keeps confidential all the information it collects on users. The point is not that privacy policies should be *presumed* immaterial; it is that privacy policies are so fundamentally different than mass advertising communications from a consumer perspective that it makes sense for the Commission to bear the burden of proof of demonstrating materiality.

Nomi illustrates why the materiality requirement is so important. The FTC Act does not legally obligate Nomi to produce a privacy policy or to publish one at all. It did. And the FTC's case against Nomi rested on a single line within its privacy policy that stated "Nomi pledges to . . . Always allow consumers to opt out of Nomi's service on its website as well as at any retailer using Nomi's technology." The FTC argued that because some retailers did not have the ability to allow consumers to opt-out of tracking within the store, this statement was deceptive. However, Nomi did provide consumers the ability to opt-out of being tracked through its website. The fundamental failure of the Commission's complaint is that the evidence simply does not support the allegation that Nomi's representation about an opportunity to opt out of the Listen service at the retail level—in light of the immediate and easily accessible opt out available on the webpage itself—was material to consumers. In other words, the Commission did not show any evidence, empirical

or otherwise, the consumers would not “have chosen differently” but-for the allegedly deceptive representation.

In fact, the evidence strongly implies that specific representation was not material and therefore not deceptive. Nomi’s “tracking” of users was widely publicized in a story that appeared on the front page of *The New York Times*, a publication with a daily reach of nearly 1.9 million readers. Most likely due to this publicity, Nomi’s opt-out rate (3.8 percent) was significantly higher than the opt-out rate for other online activities. This high rate, relative to website visitors, likely reflects the ease of a mechanism that was immediately and quickly available to consumers at the time they may have been reading the privacy policy. This behavior indicates that consumers that were interested in opting out of the tracking service took their first opportunity to do so. To presume the materiality of a representation in a privacy policy concerning the availability of an additional and more onerous in-store opt-out mechanism requires one to accept the proposition that the privacy-sensitive consumer would be more likely to bypass the easier and immediate route (the online opt out) in favor of waiting until she had the opportunity to opt out in a physical location.

Untethered from the materiality requirement, the FTC’s consumer protection efforts in privacy regulation are no longer about consumer harm—or promoting consumer welfare—they are about micromanaging privacy policies and placing broad sectors of the digital economy under the thumb of a single agency. And in Nomi in particular, the approach is about micromanaging privacy policies for firms that do not need to have one in the first place. Firms in Nomi’s position or those reading the complaint and consent carefully have an increased incentive to take down voluntary privacy policies or not generate one. This will leave consumers and privacy watchdogs with even less information than they are already receiving about website activity—exacerbating the very problem the FTC was attempting to solve. This unintended consequence is one that is easily foreseeable; and one that is obvious to most economists. But the Commission’s analysis simply ignores these tradeoffs.

By enforcing the FTC Act against trivial misstatements in privacy policies that nobody reads, the Commission has been able to put an increasingly large number of firms in the digital economy under 20-year orders. Putting businesses under order for 20 years, including intrusive monitoring and reporting requirements, seems especially questionable in the digital economy in which a firm’s half-life is closer to two years than 10. What’s more, the FTC can obtain substantial monetary penalties for violations of orders and certain statutes—*Spokeo* will pay \$800,000 for violations of the Federal Credit Reporting Act.

Not only does this approach threaten to chill innovation in the digital economy, they will deter firms from engaging in voluntary practices that promote consumer choice and transparency—the very principles that lie at the heart of the Commission’s consumer protection mission. If the benefits of these welfare-enhancing business practices are not weighed correctly against the harms they present to consumers, we run the risk of squelching innovation and depriving consumers of these benefits. Indeed, innovation in new privacy-enhancing tools and technologies might be at risk—if a company might face legal action for incorrectly yet harmlessly describe an opt-out feature they did not need to provide in the first place, then why bother? So long as economic analysis is a marginal player in privacy regulation at the FTC, this unfortunate equilibrium will remain.

Let me conclude with a few remarks on how to set the FTC on a course toward embracing the intersection of economics and privacy rather than resisting it.

Recommendations

Recommendation #1: The Bureau of Economics must serve the Commission, not the Bureau of Consumer Protection, when those two conflict.

This is quite simple but bears repeating. The question of how to best organize economists within regulatory agencies is one that has attracted a significant amount of attention from legal scholars, economists, practicing lawyers, and regulators. One possible conception of the relationship between the Bureau of Consumer Protection and the Bureau of Economics is that the latter should be a litigation and research support team for the former. And to be sure, the economists within the agency have an important function in conducting economic analyses to facilitate investigations and enforcement. But sometimes the objectives of the FTC and the Bureau of Consumer Protection should be in conflict from an economic perspective. Sometimes, from an economic perspective, the direction the FTC is going in terms of consumer protection enforcement does not make economic sense.

When such a conflict exists, it is important that the institutional design structure of the agency makes room for the economists—indeed, encourages the economists—to have a voice in terms of policy and case selection. A structure that subordinates

economists to lawyers runs the risk of not only encouraging economically misguided privacy policy, but also a reduction in alternative information flow to the Commissioners, poorer staff skill retention, and inefficient use of economists with specialized skills or knowledge.

BE must not become a mere input supplier to the Bureau of Consumer Protection. While the economists—like the smaller group within any bureaucracy—must pick their battles wisely and economize on their own scarce reputational capital within the agency, the Commission as a whole must recognize that the optimal level of economist and lawyer conflict over the direction of privacy regulation is not zero.

Recommendation #2: The FTC Should Be an Intellectual Leader in the Movement to Create Economically Coherent Privacy Regulation

The FTC is at its best when it combines its unique combination of institutional features. Perhaps the most unique is that the FTC's statutory mandate includes a research and reporting function that distinguishes it from many agencies. The Commission has a long and well-regarded history of conducting its own research and using its authority to produce public reports that examine novel, emerging or otherwise important issues. Privacy should be no exception. The case for strengthening the incentives within the agency for FTC economists to produce their own research, and to be active and engaged scholars in the field of privacy economics, is quite clear. But I do want to elaborate a bit about what we mean when discussing the type of report that the FTC should be producing.

The Commission will often seek information using its Section 6(b) authority to compel private parties to submit information for review. Commission staff reports often are the result of extensive research, rigorous investigation into certain industry sectors, practices or products, and economic analysis. Reports taking advantage of the Commission's unique ability to collect and analyze data and to conduct economic analyses to form the basis of its recommendations predictably have had significant impact on public policy debates.

Reports that do not meet that standard of research and analytical rigor should not make legislative recommendations at minimum and, frankly, ought not be published at all in many cases. The track record of rigorous reports and research show that the issue here is not capability but discretion. The FTC Bureau of Economics has housed some of the most influential consumer protection economists in history and can claim many of the most influential papers as its own. Reports that do not meet this standard detract from the agency's limited reputational capital and its ability to perform its missions.

The FTC has the legal authority, the human capital, and the economic talent to be a leader in the economic approach to privacy. It should do so. An obvious candidate is to set forth a comprehensive and rigorous research agenda for understanding the economics of privacy policies.

Recommendation #3: The FTC Should Require the Bureau of Economics to Make Public Its Views in All Consents

I continue to believe that the FTC should consider interpreting or amending FTC Rule of Practice 2.34 to mandate that BE publish, in matters involving consent decrees, and as part of the already required "explanation of the provisions of the order and the relief to be obtained," a separate explanation of the economic analysis of the Commission's action. This is especially important in the area of privacy regulation where most of the Commission's work takes place in consents.

The public-facing documents associated with this rule are critical for communicating the role that economic analysis plays in Commission decision-making in cases. In many cases, public facing document surrounding consents in privacy cases either do not describe well or at all the economic analysis conducted by staff or upon which BE recommended the consent. In cases where there is no economic analysis to explain, the Commission should make the information public as well.

The additional explanation I have in mind would be a BE document, not requiring approval of the Commission. Aside from a high-level and general description of the economic analyses relied upon in recommending or rejecting the proposed consent order, the BE explanation could also provide the more general economic rationale for its recommendation. Requiring BE to make public its economic rationale for supporting or rejecting a consent decree voted out by the Commission could offer a number of benefits at little cost. First, it would offer BE an avenue to communicate its findings to the public. Second, it reinforces the independent nature of the recommendation that BE offers. Third, it breaks the agency monopoly the FTC consumer protection lawyers currently enjoy in terms of framing a particular matter to the public. The internal leverage BE gains by the ability to publish such a document may increase conflict between bureaus on the margin in close cases, but it will

also provide BE a greater role in the consent process and a mechanism to discipline privacy consents that are not supported by sound economics.

Thank you very much for your time today. I am happy to take any questions that you have for me.

DISSENTING STATEMENT OF COMMISSIONER JOSHUA D. WRIGHT

IN THE MATTER OF APPLE, INC.

FTC FILE NO. 1123108

JANUARY 15, 2014

Today, through the issuance of an administrative complaint, the Commission alleges that Apple, Inc. (“Apple”) has engaged in “unfair acts or practices” by billing parents and other iTunes account holders for the activities of children who were engaging with software applications (“apps”) likely to be used by children that had been downloaded onto Apple mobile devices.¹ In particular, the Commission takes issue with a product feature of Apple’s platform that opens a fifteen-minute period

during which a user does not need to re-enter a billing password after completing a first transaction with the password.² Because Apple does not expressly inform account holders that the entry of a password upon the first transaction triggers the fifteen-minute window during which users can make additional purchases without once again entering the password, the Commission has charged that Apple bills parents and other iTunes account holders for the activities of children without obtaining express informed consent.³

Today’s action has been characterized as nothing more than a reaffirmance of the concept that “companies may not charge consumers for purchases that are unauthorized.”⁴ I respectfully disagree. This is a case involving a miniscule percentage of consumers—the parents of children who made purchases ostensibly without their authorization or knowledge. There is no disagreement that the overwhelming majority of consumers use the very same mechanism to make purchases and that those charges are properly authorized. The injury in this case is limited to an extremely small—and arguably, diminishing—subset of consumers. The Commission, under the rubric of “unfair acts and practices,” substitutes its own judgment for a private firm’s decisions

as to how to design its product to satisfy as many users as possible, and requires a company to revamp an otherwise indisputably legitimate business practice. Given the apparent benefits to some consumers and to competition from Apple’s allegedly unfair practices, I believe the Commission should have conducted a much more robust analysis to determine whether the injury to this small group of consumers justifies the finding of unfairness and the imposition of a remedy.

Section 5 of the FTC Act prohibits, in part, “unfair . . . acts or practices in or affecting commerce.”⁵ As set forth in Section 5(n), in order for an act or practice to be deemed unfair, it must “cause[] or [be] likely to cause substantial injury to consumers which is not reasonably avoidable by consumers themselves and not outweighed by countervailing benefits to consumers or competition.”⁶

The test the Commission uses to evaluate whether an unfair act or practice is unfair used to be different. Previously the Commission considered: whether the practice injured consumers; whether it violated established public policy; and whether it was unethical or unscrupulous.⁷ Only after an aggressive enforcement initiative that culminated in a temporary rulemaking suspension and Congressional threats of stripping the Commission of its unfairness authority altogether, was the current

¹ Complaint, Apple, Inc., FTC File No. 1123108, at para. 28–30 (Jan. 15, 2014) [hereinafter *Apple Complaint*].

² As indicated in the complaint, initially the fifteen-minute window was triggered when an app was downloaded. *Id.* at para. 16. Apple changed the interface in March 2011 and subsequently the fifteen-minute window was triggered upon the first in-app purchase. *Id.* at para. 17. *See also infra* note 13.

³ *Apple Complaint, supra* note 1, at para. 4, 20, 28.

⁴ Statement of Chairwoman Ramirez and Commissioner Brill at 1.

⁵ 15 U.S.C. § 45(a).

⁶ 15 U.S.C. § 45(n).

⁷ FTC Policy Statement on Unfairness, *appended to Int’l Harvester Co.*, 104 F.T.C. 949, 1070 (1984), available at <http://www.ftc.gov/ftc-policy-statement-on-unfairness> [hereinafter *Unfairness Statement*].

iteration of the unfairness test reached.⁸ Importantly, this articulation, as set forth in the FTC Policy Statement on Unfairness (“Unfairness Statement”), not only requires that the alleged injury be substantial, it also includes the critical requirements that such injury “must not be outweighed by any countervailing benefits to consumers or competition that the practice produces” and “it must be an injury that consumers themselves could not reasonably have avoided.”⁹

As set forth in more detail below, I do not believe the Commission has met its burden to satisfy all three requirements in the unfairness analysis. In particular, although Apple’s allegedly unfair act or practice has harmed some consumers, I do not believe the Commission has demonstrated the injury is substantial. More importantly, any injury to consumers flowing from Apple’s choice of disclosure and billing practices is outweighed considerably by the benefits to competition and to consumers that flow from the same practice. Accordingly, I respectfully dissent from the issuance of this administrative complaint and consent order.

Introduction

This case requires the Commission to analyze consumer injury under the unfairness theory in a novel context: an allegation of a failure to disclose a product feature to consumers that results in some injury to one group of consumers but that generates benefits for another group.

The circumstances surrounding Apple’s decision to forgo disclosing during the transaction the fifteen-minute window to its users—and according to the Commission’s complaint, thereby failing to obtain express informed consent—are distinguishable

from any other prior Commission case alleging unfairness. The economic consequences of the allegedly unfair act or practice in this case—a product design decision that benefits some consumers and harms others—also differ significantly from those in the Commission’s previous unfairness cases.

The Commission commonly brings unfairness cases alleging failure to obtain express informed consent. These cases invariably involve conduct where the defendant has intentionally obscured the fact that consumers would be billed. Many of these cases involve unauthorized billing or cramming—the outright fraudulent use of payment information.¹⁰ Other cases involve conduct just shy of complete fraud—the consumer may have agreed to one transaction but the defendant charges the consumer for additional, improperly disclosed items.¹¹ Under this scenario, the allegedly unfair act or practice injures consumers and does not provide economic value to consumers or competition. In such cases, the requirement to provide adequate disclosure itself does not cause significant harmful effects and can be satisfied at low cost.

However, the particular facts of this case differ in several respects from the above scenario. First, there is no evidence Apple intended to harm consumers by not disclosing the fifteen-minute window.¹² For example, when Apple began receiving complaints about children making unauthorized in-app purchases on their parents’ iTunes accounts, the company took steps to address the problem.¹³ In addition,

⁸ABA SECTION OF ANTITRUST LAW, CONSUMER PROTECTION LAW DEVELOPMENTS, 57–59 (2009); J. Howard Beales, III, Director, Bureau of Consumer Protection, Fed. Trade Comm’n, The FTC’s Use of Unfairness Authority: Its Rise, Fall, and Resurrection at 9 (May 2003), available at <http://www.ftc.gov/public-statements/2003/05/ftcs-use-unfairness-authority-its-rise-fall-and-resurrection> [hereinafter *Beales’ Unfairness Speech*].

⁹*Unfairness Statement, supra* note 7, at 1073.

¹⁰*See, e.g.*, Complaint at 6, *FTC v. Jesta Digital, LLC*, Civ. No. 1:13-cv-01272 (D.D.C. Aug. 20, 2013) (alleging that “Jesta charged consumers who did not click on the subscribe button and charged consumers for products they did not order.”); Complaint, *FTC v. Wise Media, LLC*, Civ. No. 1:13-CV-1234 (N.D. Ga. Apr. 16, 2013) (alleging that defendants charge consumers for purported services without consumers ever knowingly signing up for such services).

¹¹Complaint at 15–16, *FTC v. JAB Ventures, LLC*, Civ. No. CV08–04648 (RZx) (C.D. Cal. July 8, 2008) (alleging unauthorized billing when defendants charged consumers who had cancelled their enrollment or who had not been adequately informed about negative option features); *FTC v. Crescent Publ’g Group, Inc.*, 129 F. Supp. 2d 311 (S.D.N.Y. 2001) (pornography website failing to disclose the point at which a “free tour” ended and a monthly membership would begin).

¹²By distinguishing the facts of this case from other unfairness cases brought by the Commission alleging the failure to obtain express informed consent, I do not imply that intent is a required element of the analysis. However, I think drawing the distinction informs the discussion. Furthermore, I am unaware that the Commission has ever exercised its unfairness authority where it has alleged only that the defendant inadvertently charged consumers.

¹³*See* Chris Foresman, *Apple facing class-action lawsuit over kids’ in-app purchases*, *arstechnica*, Apr. 15, 2011, <http://arstechnica.com/apple/2011/04/apple-facing-class-action-lawsuit-over-kids-in-app-purchases/> (“After entering a password to purchase an app from the

Apple has an established relationship with its customers and its business model depends upon customer satisfaction and repeat business.

Second, rather than an unscrupulous or questionable practice, the nature of Apple's disclosures on its platform is an important attribute of Apple's platform that affects the demand for and consumer benefits derived from Apple devices and services. Disclosures made on the screen while consumers interact with mobile devices are a fundamental part of the user experience for products like mobile computing devices. It is well known that Apple invests considerable resources in its product design and functionality.¹⁴ In streamlining disclosures on its platform and in its choice to integrate the fifteen-minute window into Apple users' experience on the platform, Apple has apparently determined that most consumers do not want to experience excessive disclosures or to be inconvenienced by having to enter their passwords every time they make a purchase.

The Commission has long recognized that in utilizing its authority to deem an act or practice as "unfair" it must undertake a much more rigorous analysis than is necessary under a deception theory.¹⁵ As a former Bureau Director has noted, "the primary difference between full-blown unfairness analysis and deception analysis is that deception does not ask about offsetting benefits. Instead, it presumes that false or misleading statements either have no benefits, or that the injury they cause consumers can be avoided by the company at very low cost."¹⁶ It is also well established that one of the primary benefits of performing a cost-benefit analysis is to ensure that government action does more good than harm.¹⁷ The discussion below explains why I believe the Commission's action today fails to satisfy the elements of the unfairness framework and thereby conclude that placing Apple under a twenty-year order in a marketplace in which consumer preferences and technology are rapidly changing is very likely to do more harm to consumers than it is to protect them.

I. The Evidence Does Not Support a Finding of Substantial Injury as Required by the Unfairness Analysis

Apple's choice to include the fifteen-minute window in its platform design, and its decision on how to disclose this window, resulted in harm to a small fraction of consumers. Any consumer harm is limited to parents who incurred in-app charges that would have been avoided had Apple instead designed its platform to provide specific disclosures about the fifteen-minute window for apps with in-app purchasing capability that are likely to be used by children. That harm to some consumers results from a design choice for a platform used by millions of users with disparate preferences is not surprising. The failure to provide perfect information to consumers will always result in "some" injury to consumers. The relevant inquiry is whether the injury to the subset of consumers is "substantial" as contemplated by the Commission's unfairness analysis.

Consumer injury may be established by demonstrating the allegedly unfair act or practice causes "a very severe harm to a small number"¹⁸ of people or "a small harm to a large number of people."¹⁹ While it is possible to demonstrate substantial

App Store, the password now has to be reentered in order to make any initial in-app purchases.").

¹⁴ Nigel Hollis, *The Secret to Apple's Marketing Genius (Hint: It's Not Marketing)*, The Atlantic, July 11, 2011, <http://www.theatlantic.com/business/archive/2011/07/the-secret-to-apples-marketing-genius-hint-its-not-marketing/241724/> (in discussing Apple's functionality, "[u]sing an Apple product feels so natural, so intuitive, so transparent, that sometimes, even people paid to know what makes products great completely miss the cause of their addiction to Apple products. It's the natural, intuitive transparency of the technology. The superlative product experience comes from an unusual combination of human and technical understanding, and it creates the foundation of all the other positive aspects of the brand."); Peter Eckert, *Dollars And Sense: The Business Case For Investing In UI Design*, Fast Company, Mar. 15, 2012, <http://www.fastcodesign.com/1669283/dollars-and-sense-the-business-case-for-investing-in-ui-design> ("As we have seen with Apple's success, creating products that offer as much simplicity as functionality drives market share and premium pricing."). See also Neil Hughes, *Apple's research & development costs ballooned 32 percent in 2013 to \$4.5B*, Apple Insider, Oct. 30, 2013, <http://appleinsider.com/articles/13/10/30/apples-research-development-costs-ballooned-32-in-2013-to-45b>; Cliff Kuang, *The Six Pillars of Steve Jobs' Design Philosophy*, Fast Company, Nov. 7, 2011, <http://www.fastcodesign.com/1665375/the-6-pillars-of-steve-jobs-design-philosophy>.

¹⁵ Int'l Harvester Co., 104 F.T.C. 949, 1070 (1984); *Beales' Unfairness Speech*, *supra* note 8, § III.

¹⁶ *Beales' Unfairness Speech*, *supra* note 8, § III.

¹⁷ Int'l Harvester, 104 F.T.C. at 1070.

¹⁸ Int'l Harvester, 104 F.T.C. at 1064.

¹⁹ *Unfairness Statement*, *supra* note 7, at n.12.

injury occurred as a result of an act or practice causing a small harm to a large number of consumers, substantiality is analyzed relative to the magnitude of any offsetting benefits.²⁰ This is particularly critical when the allegedly unfair practice is not a fraudulent activity such as unauthorized billing or cramming, where there are no offsetting benefits.

By reasonable measures of the potential harms and benefits available to the Commission, the injury is relatively small and not necessarily substantial in this case. The complaint alleges Apple has received “at least tens of thousands of complaints related to unauthorized in-app charges by children”²¹ while playing games acquired on Apple’s platform, which supports all music, books, and applications purchased for use with Apple mobile devices (*e.g.*, iPhone, iPad, iPod, hereinafter “iDevices”). Although “tens of thousands” sounds like a large number, the unfairness inquiry requires this number be evaluated in an appropriate context. Apple announced its 50 billionth app download in May 2013.²² Even 200,000 complaints in 50 billion downloads would represent only four complaints in a million, which is quite a small fraction.

In addition, the complaint presents a few examples in which children made unauthorized in-app purchases that were relatively large, some greater than \$500, and one bill as high as \$2,600.²³ There is undoubtedly consumer harm in these instances, assuming the purchases are correctly attributed to the alleged failure to disclose, but again, in order to qualify as substantial, the harm “must be large compared to any offsetting benefits.”²⁴

The relevant economic context required to understand substantiality of injury in this case includes the proportions of populations potentially harmed and benefitted by the failure to disclose product features in this case. A measure of harm that gives weight to both the number of consumers harmed and the size of the individual harms is the ratio of the value of unauthorized purchases to the total sales affected by the practice. We can construct such a measure as follows. The \$32.5 million in consumer refunds required by the consent decree presumably relates in some way to the harm arising from Apple’s disclosure practices. Recognizing that monetary amounts emerging from consent decrees are a product of compromise and an assessment of litigation risk, suppose that the value of unauthorized purchases is ten times higher than the negotiated settlement amount. This assumption gives a conservatively high estimate of \$325 million in unauthorized purchases since the inception of the App Store.

The total sales affected by Apple’s disclosure practices likely include not only the sale of apps and in-app purchases, but also the sale of iDevices. This is likely because the benefits from using apps and making in-app purchases are components of the stream of benefits generated by iDevices, and a customer’s decision to purchase an iDevice will depend upon the stream of benefits derived from the device. Indeed, the degree of integration across all components of Apple’s platform is remarkably high, suggesting that Apple’s disclosure practices may affect all Apple’s sales. For completeness, Charts 1 and 2 below measure the estimated harm as a fraction of all three variants of Apple’s sales—App Store sales, iDevice sales, and total sales. These data are available from Apple’s Annual Reports and press releases.

Chart 1 shows that the estimated value of the harm is a miniscule fraction of both Apple total sales (about six one-hundredths of one percent) and iDevice sales (about eight one-hundredths of one percent) over the five-year period from the inception of the App Store to September 2013. This measure of harm, a conservatively high estimate, is also a relatively small fraction of App Store sales (about 4.6 percent).

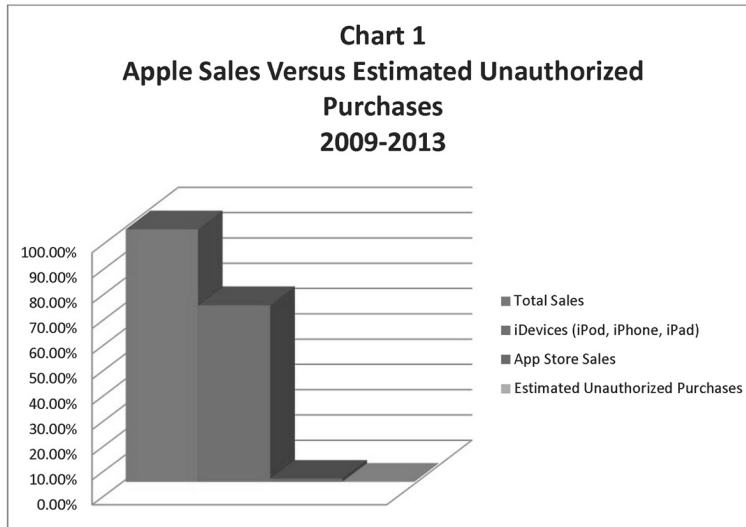
²⁰ *Beales’ Unfairness Speech*, *supra* note 8, § III (“relative to the benefits, the injury may still be substantial” and “[t]o qualify as substantial, an injury must be real, and it must be large compared to any offsetting benefits.”).

²¹ *Apple Complaint*, *supra* note 1, at para. 24.

²² Press Release, Apple, Inc., Apple’s App Store Marks Historic 50 Billionth Download (May 16, 2013), available at <http://www.apple.com/pr/library/2013/05/16Apples-App-Store-Marks-Historic-50-Billionth-Download.html>.

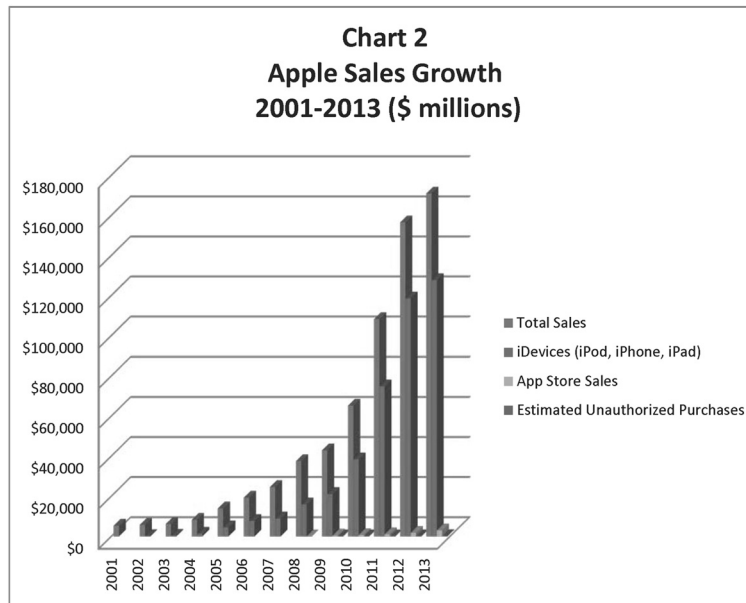
²³ *Apple Complaint*, *supra* note 1, at para. 25–26.

²⁴ *Beales’ Unfairness Speech*, *supra* note 8, § III.



Sources: Apple, Inc., Annual Reports for 2009–2013 (Form 10–K); Marin Perez, *Apple App Store A \$1.2 Billion Business In 2009*, InformationWeek, June 11, 2008, available at [http://www.informationweek.com/mobile/mobile-devices/apple-app-store-a-\\$12-billion-business-in-2009/d/d-id/1068794](http://www.informationweek.com/mobile/mobile-devices/apple-app-store-a-$12-billion-business-in-2009/d/d-id/1068794); *Apple Complaint*, *supra* note 1 (for the \$32.5 million settlement amount).

Chart 2 illustrates the same relationship with respect to Apple sales growth over the last 13 years.



Sources: Same as Chart 1, plus Apple, Inc., Annual Reports for 2002–2008 (Form 10–K). Calculations assume the App Store sales and estimated unauthorized purchases grew at a constant percentage growth rate from 2009 through 2013.

Taking into account the full economic context of Apple’s choice of disclosures relating to the fifteen-minute window undermines the conclusion that any consumer injury is substantial.

II. At Least Some of the Injury Could Be Reasonably Avoided by Consumers

The Unfairness Statement provides that the “injury must be one which consumers could not reasonably have avoided.”²⁵ In explaining that requirement the Commission noted, “[i]n some senses any injury can be avoided—for example, by hiring independent experts to test all products in advance, or by private legal actions for damages—but these courses may be too expensive to be practicable for individual consumers to pursue.”²⁶ The complaint does not allege that the undisclosed fifteen-minute window is an unfair practice as to any consumer other than parents of children playing games likely to be played by children that have in-app purchasing capability.²⁷ In the instant case, it is very likely that most parents were able to reasonably avoid the potential for injury, and this avoidance required nothing as drastic as hiring an independent expert, but rather common sense and a modicum of diligence.

The harm to consumers contemplated in the complaint involves app functionality that changed over time. In the earliest timeframe, the harm occurred when a parent typed in their Apple password to download an app with in-app purchase capability, handed the Apple device to their child, and then unbeknownst to the parent, the child was able to make in-app purchases by pressing the “buy” button during the fifteen-minute window in which the password was cached. This was apparently an oversight on Apple’s part. When it came to the company’s attention, Apple implemented a password prompt for the first in-app purchase after download.²⁸

During the later timeframe, after being handed the Apple device, a child again would press the “buy” button to make an in-app purchase. At this point, the child would have needed to turn the device back over to the parent for entry of the password. Alternatively, some children may have known their parent’s password and entered it themselves. In either case, the fifteen-minute window was opened and additional in-app purchases could be made without further password prompts.

Under the first scenario, account holders received no password prompt for the first in-app purchase and thus the injury experienced by some consumers arguably may not have been reasonably avoidable. Because the opening of the fifteen-minute window *in this context* does not appear to be a product design feature, but rather an unintended oversight, I will focus my attention upon the harm experienced by consumers in the latter scenario and discuss their ability to reasonably avoid it.

Irrespective of the existence of the fifteen-minute window, a user can only make an in-app purchase by pressing a “buy” button while engaging with the app. In other words, the user must decide to make an in-app purchase. To execute the first in-app purchase, the user must enter a password. The fifteen-minute window eliminates the second step of verification—entering a password—only *after* the user has made the first in-app purchase by clicking the “buy” button and entering the password.

By entering their password into the Apple device—an action that is performed in response to a request for permission—parents were effectively put on notice that they were authorizing a transaction.²⁹ Although the complaint alleges that the fifteen-minute window was not expressly disclosed to parents, regular users of Apple’s platform become familiar with the opportunity to make purchases without entering a password every time.³⁰ Even if some parents were not familiar with the fifteen-minute window, the requirement to re-enter their password to authorize a trans-

²⁵ *Unfairness Statement*, *supra* note 7, at 1074.

²⁶ *Unfairness Statement*, *supra* note 7, at n.19.

²⁷ Indeed, there are many financial, banking, and retail apps and websites that allow consumers to conduct a series of transactions after entering a password only once. These services usually only require re-entry of a password after a certain amount of time has elapsed, or the session expires because of inactivity on the user’s part. It is doubtful that the Commission would bring an unfairness case because these services do not disclose this window.

²⁸ See Foresman, *supra* note 13.

²⁹ Furthermore, Apple sends an e-mail receipt to the iTunes account holder after a purchase has been made in either the iTunes or App Store. See e.g., <http://www.apple.com/privacy/>

³⁰ To the extent that users read the Apple Terms and Conditions when they opened their iTunes accounts, consumer injury would also have been avoided. The Terms and Conditions explain the fifteen-minute window and other aspects of how Apple’s platform works, including the App Store. It appears that Apple has included these explanations since at least June 2011. See <http://www.apple.com/legal/internet-services/itunes/us/terms.html#SALE> (Apple’s current Terms and Conditions) and <http://www.proandcontracts.com/wp-content/uploads/2011/06/2011.06.09-iTunes-Terms-and-Conditions-June-2011-Update-with-Highlighting.pdf> (cached copy of what appears to be its Terms and Conditions as of June 2011).

action arguably triggered some obligation for them to investigate further, rather than just to hand the device back to the child without further inquiry.³¹

III. Any Consumer Injury Caused by Apple's Platform is Outweighed by Countervailing Benefits to Consumers and Competition

Assuming for the moment there is at least some harm that consumers cannot reasonably avoid, the question turns to whether the harms are substantial relative to any benefits to competition or consumers attributable to the conduct. In performing this balancing, the Commission must also take "account of the various costs that a remedy would entail. These include not only the costs to the parties directly before the agency, but also the burdens on society in general in the form of increased paperwork, increased regulatory burdens on the flow of information, reduced incentives to innovation and capital formation, and similar matters."³² I now turn to that question.

A. Apple's Platform as a Benefit to Consumers and Competition

Unfairness analysis requires an evaluation and comparison of the benefits and costs of Apple's decision not to increase or enhance its disclosure of how Apple's platform works, including the fifteen-minute window. The fifteen-minute window is a *feature* of Apple's platform that applies to purchases of songs, books, apps, and in-app purchases. This feature has long been a part of the iTunes Store for downloading music, and regular users of iTunes apparently value it. In the context here, disclosure is perhaps better thought of as a product attribute—*guidance*—that Apple provides to the customer through on-screen and other explanations of how to use Apple's platform.³³

In deciding what guidance to provide and how to provide it, firms face two important issues. First, since it is generally not possible to customize guidance for every individual customer, the optimal guidance inevitably balances the needs of different customers. In drawing this balance, the potential for harm from misinterpretation is likely important in deciding which customer on the sophistication spectrum might represent the least common denominator for directing the guidance. For any given degree of guidance, some customers will get it immediately, while others will have to work harder. If the potential for harm is very large, *e.g.*, harm from a drug overdose, then both the firm and consumers want obvious, strong disclosures about dosage, and perhaps other steps like childproof caps. If the potential for harm is small, then strong guidance (or caps that are hard to open in the drug context) may make it more costly for consumers to use the product. Platform designers clearly face such tradeoffs in their decision-making regarding guidance and disclosures. Apple clearly faces the same tradeoff with respect to its decisions concerning the fifteen-minute window. This tradeoff is relevant for evaluating the benefit-cost test at the core of unfairness analysis.

Second, because it is difficult to anticipate the full set of issues that might benefit from guidance of various types, the firm must decide how much time to spend researching, discovering, and potentially fixing possible issues *ex ante* versus finding and fixing issues as they arise. With complex technology products such as computing platforms, firms generally find and address numerous problems as experience is gained with the product. Virtually all software evolves this way, for example. This tradeoff—between time spent perfecting a platform up front versus solving problems as they arise—is also relevant for evaluating unfairness.

Apple presumably weighs the costs and benefits to Apple of different ways to provide guidance. In doing so, Apple must consider: (i) the benefit to Apple of greater sales of mobile devices, music, books, apps, and in-app components to customers who benefit from the additional guidance and make more purchases; (ii) the cost to Apple of fewer sales of mobile devices, music, books, apps, and in-app components by customers who find that more real-time guidance hampers their experience; and (iii) the cost to Apple of developing and implementing more guidance. In weighing

³¹The Terms and Conditions also explain how to use the parental control settings to control how the App Store works. See <http://support.apple.com/kb/HT1904> and <http://support.apple.com/kb/HT4213>. These parental control settings allow users to disable in-app purchasing capability as well as establish settings that require a password each time a purchase is made, thereby eliminating the fifteen-minute window.

³²*Unfairness Statement*, *supra* note 7, at 1073–74.

³³Compare the disclosure contemplated here with disclosure in the mortgage context, for example. Here, the disclosure itself—or the guidance offered while the user is interacting with the product—is an intrinsic part of the product's value. Indeed, Apple's business model is built on offering an integrated platform with a clean design that customers find intuitive and easy to use. The way the platform is presented, including disclosures or guidance offered during use, is a critically important component of value. In the mortgage context, the disclosures signed at closing are not a significant component of the value of the mortgage.

(i) and (ii), Apple is particularly concerned about the effects on the sales of mobile devices that use Apple's platform, as they constitute the bulk of Apple's business, as indicated in Charts 1 and 2.³⁴

The relevant universe for assessing unfairness of Apple's guidance provision, including disclosures relating to the fifteen-minute window, is the set of users to whom the guidance is directed. This includes all users of Apple's platform who might make online purchases through the platform.

The ratio of estimated unauthorized purchases in this case to all purchases made by users of Apple's platform is miniscule, as Charts 1 and 2 illustrate. This fact, by itself, does not establish that the benefits of Apple's decision to forgo additional guidance of the type required by the consent order outweigh its costs. However, the remarkably low ratio does provide perspective on the following question: How much would the average non-cancelling customer need to be harmed by a requirement of additional guidance in order to outweigh the benefit of preventing harm to other consumers? Suppose the fraction of customers that would benefit from additional guidance is approximated by the ratio of estimated unauthorized purchases to total sales of iDevices. The analysis in Charts 1 and 2 indicates that estimated unauthorized purchases have been about 0.08 percent of iDevice-related sales since the App Store was launched. Suppose that customers that make unauthorized purchases cancel them and seek a refund. Suppose also that the time cost involved in seeking a refund return is \$11.95.³⁵ Then, if the average harm to non-cancelling customers from additional guidance sufficient to prevent cancellations is more than about a penny per transaction, the additional guidance will be counter-productive.³⁶

To be clear, the sales of iDevices are not an estimate of consumer benefits but rather they approximate the total universe of economic activity implicated by the Commission's consent order. Similarly, estimated unauthorized purchases merely approximate the total universe of consumers potentially harmed by Apple's practices. The harm from Apple's disclosure policy is limited to users that actually make unauthorized purchases. However, the potential benefits from Apple's disclosure choices are available to the entire set of iDevice users because these are the consumers capable of purchasing apps and making in-app purchases. The disparity in the relative magnitudes of these universes of potential harms and benefits suggests, at a minimum, that further analysis is required before the Commission can conclude that it has satisfied its burden of demonstrating that any consumer injury arising from Apple's allegedly unfair acts or practices exceeds the countervailing benefits to consumers and competition.³⁷

Nonetheless, the Commission effectively rejects an analysis of tradeoffs between the benefits of additional guidance and potential harm to some consumers or to competition from mandating guidance by assuming that "the burden, if any, to users who have never had unauthorized charges for in-app purchases, or to Apple, from the provision of this additional information is *de minimis*" and that any mandated disclosure would not "detract in any material way from a streamlined and seamless user experience." I respectfully disagree. These assumptions adopt too cramped a view of consumer benefits under the Unfairness Statement and, without more rigorous analysis to justify their application, are insufficient to establish the Commission's burden.

³⁴In 2012, sales of the iPhone, iPad, and iPod accounted for over 76 percent of Apple's \$157 billion in sales. See Apple, Inc., Annual Report (Form 10-K), at 73 (Oct. 31, 2012), available at <http://files.shareholder.com/downloads/AAPL/2661211346x0xS1193125-12-444068/320193/filing.pdf>.

³⁵The \$11.95 figure represents the seasonally adjusted average earnings per half hour across all employees on private nonfarm payrolls, as reported by the Bureau of Labor and Statistics in May 2013. See <http://www.bls.gov/news.release/empsit.t19.htm> for the most recent report. The assumption is that customers asked for returns were reimbursed for the charges as Apple attests, and that obtaining a reimbursement takes half an hour.

³⁶Let Y be the harm to non-cancelling customers from additional guidance sufficient to prevent cancellations. This harm will just equal the benefit of avoiding cancellations if (% Cancelling) x (Refund Time Cost) — (% Not Cancelling) x Y = 0. Assuming (% Cancelling) is .0008, (Refund Time Cost) is \$11.95, and (% Not Cancelling) is .9992, solving for Y gives Y = \$.009. In other words, if the harm to non-cancelling customers from additional guidance is more than roughly one cent for each transaction, then the costs of the additional guidance will outweigh the benefits.

³⁷Commissioner Ohlhausen suggests that our unfairness analysis compares inappropriately the injury caused by Apple's lack of clear disclosure with the benefits of Apple's disclosure policy to the entire ecosystem. She argues that this approach "skew[s] the balancing test for unfairness and improperly compare[s] injury 'oranges' from an individual practice with overall 'Apple' ecosystem benefits." Statement of Commissioner Ohlhausen at 3. For the reasons discussed, this analysis misses the point.

B. The Costs and Benefits to Consumers and Competition of Apple's Product Design and Disclosure Choices

To justify a finding of unfairness, the Commission must demonstrate the allegedly unlawful conduct results in net consumer injury. This requirement, in turn, logically implies the Commission must demonstrate Apple's chosen levels of guidance are less than optimal because consumers would benefit from additional disclosure. There is a considerable economic literature on this subject that sheds light upon the conditions under which one might reasonably expect private disclosure levels to result in net consumer harm.³⁸

To support the complaint and consent order the Commission issues today requires evidence sufficient to support a reason to believe that Apple will undersupply guidance about its platform relative to the socially optimal level. Economic theory teaches that such a showing would require evidence that "marginal" customers—the marginal consumer is the customer that is just indifferent between making the purchase or not at the current price—would benefit *less* from the consent order than the "inframarginal" customers who are willing to pay significantly more for the product than the current price and therefore would purchase the product irrespective of a small adjustment in an attribute. Nobel Laureate Michael Spence points out in his seminal work on the subject that this analysis generally requires information on the valuations of inframarginal consumers.³⁹ Here, marginal consumers are those who would not have made in-app purchases if Apple would have disclosed the fifteen-minute window. Inframarginal consumers are those Apple customers who would not change their purchasing behavior in response to a change in Apple's disclosures.

Staff has not conducted a survey or any other analysis that might ascertain the effects of the consent order upon consumers. The Commission should not support a case that alleges that Apple has underprovided disclosure without establishing this through rigorous analysis demonstrating—whether qualitatively or quantitatively—that the costs to consumers from Apple's disclosure decisions have outweighed benefits to consumers and the competitive process. The absence of this sort of rigorous analysis is made more troublesome in the context of a platform with countless product attributes and where significant consumer benefits are intuitively obvious and borne out by data available to the Commission. We cannot say with certainty whether the average consumer would benefit more or less than the marginal consumer from additional disclosure without empirical evidence. This evidence might come from a study of how customers react to different disclosures. However, given the likelihood that the average benefit of more disclosure to unaffected customers is less than the benefit to affected customers who are likely to be customers closer to the margin, I am inclined to believe that Apple has more than enough incentive to disclose.⁴⁰

C. Other Considerations When Examining the Costs and Benefits of Platforms and other Multi-Attribute Products

Unfairness analysis also requires the Commission to consider the impact of contemplated remedies or changes in the incentives to innovate new product features upon consumers and competition.⁴¹ I close by discussing some additional dimensions of an economic analysis of the costs and benefits of product disclosures in the context of complicated products and platforms with many attributes, like Apple's platform, where such disclosures are a critical component of the user experience and have considerable impact upon the value consumers derive from the product.

For complicated products—for example, a web-based platform for purchasing and interacting with potentially millions of items using a mobile device—there are many things that can negatively impact user experience. The number of potential issues

³⁸Disclosure in this context is analogous to a quality decision that may affect different customers differently. A. Michael Spence, *Monopoly, Quality and Regulation*, 6 BELL J. OF ECON. 417–29 (1975); Eytan Sheshinski, *Price, Quality and Quantity Regulation in Monopoly Situations*, 43 ECONOMICA 127–37 (1976). The analysis of this issue is also explained in JEAN TIROLE, *THE THEORY OF INDUSTRIAL ORGANIZATION* §2.2.1 (MIT Press 1988).

³⁹Spence, *supra* note 38.

⁴⁰This argument does not, as Chairwoman Ramirez and Commissioner Brill suggest, "presuppose that a sufficient number of Apple customers will respond to the lack of adequate information by leaving Apple for other companies." Statement of Chairwoman Ramirez and Commissioner Brill at 5–6. Nor does the economic logic require any belief about the magnitude of switching costs. Rather, the analysis relies only upon the standard economic assumption that Apple chooses disclosure to maximize shareholder value, weighing how customers react to different disclosure policies. If Apple behaves this way, the average benefit of more disclosure to unaffected customers is less than the benefit to affected customers, and affected customers are more likely to be on the margin than unaffected customers, then economic theory implies that Apple is likely to have more than enough incentive to disclose.

⁴¹*Unfairness Statement*, *supra* note 7, at 1073–74.

for products that involve hardware, software, and a human interface is large. This is the nature of technology. When designing a complex product, it is prohibitively costly to try to anticipate *all* the things that might go wrong. Indeed, it is very likely impossible. Even when potential problems are found, it is sometimes hard to come up with solutions that that one can be confident will fix the problem. Sometimes proposed solutions make it worse. In deciding how to allocate its scarce resources, the creator of a complex product weighs the tradeoffs between (i) researching and testing to identify and determine whether to fix potential problems in advance, versus (ii) waiting to see what problems arise after the product hits the marketplace and issuing desirable fixes on an ongoing basis. We observe the latter strategy in action for virtually all software.

The relevant analysis of benefits and costs for allegedly unfair omissions requires weighing of the benefits and costs of discovering and fixing the issue that arose *in advance* versus the benefits and costs of finding the problem and fixing it *ex post*. These considerations fit comfortably within the unfairness framework laid out by the Commission.⁴² The Commission also takes account of the various costs that a remedy would entail. These include not only the costs to the parties directly before the agency, but also the burdens on society in general in the form of increased regulatory burdens on the flow of information, reduced incentives to innovate and invest capital, and other social costs.⁴³

Here, Apple did not anticipate the problems customers would have with children making in-app purchases that parents did not expect. When the problem arose in late 2010, press reports indicate that Apple developed a strategy for addressing the problem in a way that it believed made sense, and it also refunded customers that reported unintended purchases.⁴⁴ This is precisely the efficient strategy described above when complex products like Apple's platform develop problems that are difficult to anticipate and fix in advance. Establishing that it is "unfair" unless a firm anticipates and fixes such problems in advance—precisely what the Commission's complaint and consent order establishes today—is likely to impose significant costs in the context of complicated products with countless product attributes. These costs will be passed on to consumers and threaten consumer harm that is likely to dwarf the magnitude of consumer injury contemplated by the complaint.

This investigation began largely because of complaints that arose when in-app purchases were first introduced into the marketplace and Apple had not had enough experience with the platform to recognize how parents and children would use the App Store. In late 2010, complaints began to emerge. In March 2011, Apple first altered its platform to address complaints about unauthorized in-app purchases. It is not unreasonable to surmise that as Apple has modified its policies based on experience, and customers have learned more about how to use the platform, unauthorized in-app purchases by children have most likely steadily declined.

The Commission has no foundation upon which to base a reasonable belief that consumers would be made better off if Apple modified its disclosures to conform to the parameters of the consent order. Given the absence of such evidence, enforcement action here is neither warranted nor in consumers' best interest.

PREPARED STATEMENT OF SCOTT SMITH, PRESIDENT,
PRECIOUS METALS ASSOCIATION OF NORTH AMERICA

Chairman Moran and Members of the Subcommittee,

My name is Scott Smith and I am the CEO of Pyromet, which is a privately owned precious metals manufacturer and refiner of silver, gold, and platinum group metals. Since 1969, Pyromet is a reputable name in precious metals and precious metals management. I also serve as President of the of the Precious Metals Association of North America (PMANA) and am submitting this written testimony on behalf of our members. Our association's members are made up of refiners, manufacturers, traders, and distributors of products that are essentially comprised of precious metals such as gold, silver, platinum, and palladium. All of our members have a vested interest in the great work being done at the Federal Trade Commission, but we believe steps can be taken to improving fairness and innovation, all the while continuing to protect consumer welfare.

⁴²The Commission must take "account of the various costs that a remedy would entail" including "reduced incentives to innovation and capital formation, and similar matters." *Unfairness Statement, supra* note 7, at 1073–74.

⁴³*Unfairness Statement, supra* note 7, at 1073–74.

⁴⁴See Foresman, *supra* note 13.

For most products, unless they are automobiles or items made from textile or wool, there is no law requiring manufacturers and marketers to make a “Made in USA” claim. But if a business chooses to make the claim, the FTC’s “Made in USA” standard applies. “Made in USA” means that “all or virtually all” the product has been made in America. That is, all significant parts, processing, and labor that go into the product must be of U.S. origin. Products should not contain any—or should contain only negligible—foreign content.

Manufacturers of products made with recycled materials can’t claim products were “Made in USA” unless they can show that the materials originated domestically, according to the Federal Trade Commission. This makes “Made in USA” claims tricky for recycled materials. Gold that is used to make jewelry is likely to have been recycled many times, which makes it impossible to determine the location from which it was originally mined. As much as 90 percent of gold jewelry contains recycled material, and some of it may have been mined centuries ago. This is due to the fact that gold can be recycled indefinitely without degrading the quality, and the metal’s high intrinsic value means little if it is not eventually recycled. Given the long and complex history of this gold, the FTC’s requirement to substantiate that material was originally mined in the U.S. is not possible for most of the gold jewelry that is crafted here by American hands.

The innovative process of recycling scrap precious metals—particularly gold—begins with the collection of used jewelry, coins, electronic and industrial components, investment bars and manufacturing by-products. Most recycled gold originates from pre-owned jewelry, with smaller amounts deriving from other sources. The material is melted, then undergoes the same chemical refining process as would newly mined gold to produce a bar that is at least 99.5 percent gold for use by jewelry manufacturers.

Since 1997 when the “all or virtually all” standard was adopted, globalization and innovation has increased the accessibility and use of precious metal scrap. Thus, precious metal scrap is constantly recycled and the minerals extracted for production purposes. As precious metal scrap continues to be recycled and refined for use by American workers, it becomes increasingly difficult to determine the location from which the raw materials were mined.

In addition to the “all or virtually all” standard being outdated, it appears to conflict with current policies and practices used by other agencies regarding scrap, particularly those followed by the Commerce department and the United States Trade Representative as defined by U.S. Customs in 19 C.F.R. Section 102.1. Additionally, the U.S. Customs standard, otherwise known as “substantial transformation,” takes into consideration the value of American labor in recycling, refining, and preparing precious metal scrap for future uses.

The value of American labor—especially in a globalized economy—is crucial for promoting our products both domestically and worldwide. According to an industry survey approved by the FTC, 62 percent of consumers said it didn’t matter if some of the materials originated elsewhere for something to be labeled “Made in USA,” as long as the product was created by U.S. labor in the United States. Clearly, consumers are aware of the benefits of trade—including the recovery of valuable materials by U.S. labor for domestic manufacturing.

Also, when it comes to trade, it is important to maintain consistency policies. It is important to note that the FTC is the *only* government agency to use the “all or virtually all” standard to determine origination. That being said, the same FTC-approved consumer survey found that 92 percent of Americans agreed that only one standard for “Made in USA” should be applied to all government agencies. This is an indication that American consumers very well understand the importance of government efficiency in a globalized economy.

Policy Proposal

Moving forward, as the United States enters into and renegotiates trade agreements, we believe that the FTC should reexamine its “Made in USA” standard and its effect on industries that take in, recycle, and refine valuable materials to be used in production by U.S. labor. When considering valuable materials whose unknown origins date back centuries ago, the “Made in USA” standard should give deference to U.S. labor and the significant contributions such labor has made to the U.S. economy as a result of skilled American craftsmanship.

Thank you and I look forward to working with the subcommittee and the FTC to ensure a “Made in USA” standard that improves fairness among industries, considers the innovative processes utilized by American industries to prepare recycled materials for use by U.S. labor, and upholding the highest common-sense standards for protecting consumer welfare. If you have any questions, I am happy to meet with you and/or your staff to discuss this issue in greater detail. Thank you for the time

and I hope the subcommittee will look closely at this issue and the impacts it has on U.S. labor and the economy.

THE FEDERAL TRADE COMMISSION:
RESTORING CONGRESSIONAL OVERSIGHT OF THE SECOND NATIONAL LEGISLATURE
An Analysis of Proposed Legislation

Berin Szókaⁱ & Geoffrey A. Manneⁱⁱ—May 2016

REPORT 2.0 OF THE FTC: TECHNOLOGY & REFORM PROJECT

The “FTC: Technology & Reform Project” was convened by the International Center for Law & Economics and TechFreedom in 2013. It is not affiliated in any way with the FTC.

Executive Summary

Congressional reauthorization of the FTC is long overdue. It has been twenty-two years since Congress last gave the FTC a significant course-correction and even that one, codifying the heart of the FTC’s 1980 Unfairness Policy Statement, has not had the effect Congress expected. Indeed, neither that policy statement nor the 1983 Deception Policy Statement, nor the 2015 Unfair Methods of Competition Enforcement Policy Statement, will, on their own, ensure that the FTC strikes the right balance between over- and under-enforcement of its uniquely broad mandate under Section 5 of the FTC Act.

These statements are not without value, and we support codifying the other key provisions of the Unfairness Policy Statement that were not codified in 1980, as well as codifying the Deception Policy Statement. In particular, we urge Congress or the FTC to clarify the meaning of “materiality,” the key element of Deception, which the Commission has effectively nullified.

But a shoring up of substantive standards does not address the core problem: ultimately, that the FTC’s *processes* have enabled it to operate with essentially unbounded discretion in developing the doctrine by which its three high level standards are applied in real-world cases.

Chiefly, the FTC has been able to circumvent judicial review through what it calls its “common law of consent decrees,” and to effectively circumvent the rulemaking safeguards imposed by Congress in 1980 through a variety of forms of “soft law”: guidance and recommendations that have, if indirectly and through amorphous forms of pressure, essentially regulatory effect.

At the same time, and contributing to the problem, the FTC has made insufficient use of its Bureau of Economics, which ought to be the agency’s crown jewel: a dedicated, internal think tank of talented economists who can help steer the FTC’s enforcement and policymaking functions. While BE has been well integrated into the Commission’s antitrust decisionmaking, it has long resisted applying the lessons of law and economics to its consumer protection work.

The FTC is, in short, in need of a recalibration. In this paper we evaluate nine of the seventeen FTC reform bills proposed by members of the Commerce, Manufacturing and Trade Subcommittee, and suggest a number of our own, additional reforms for the agency.

Many of what we see as the most needed reforms go to the lack of economic analysis. Thus we offer detailed suggestions for how to operationalize a greater commitment to economic rigor in the agency’s decision-making at all stages. Specifically, we propose expanding the proposed requirement for economic analysis of recommendations for “legislation or regulatory action” to include best practices (such as the FTC commonly recommends in reports), complaints and consent decrees. We also propose (and support bills proposing) other mechanisms aimed at injecting more rigor into the Commission’s decisionmaking, particularly by limiting its use of various sources of informal or overly discretionary sources of authority.

The most underappreciated aspect of the FTC’s processes is investigation, for it is here that the FTC wields incredible power to coerce companies into settling lawsuits rather than litigating them. Requiring that the staff satisfy a “preponderance of the evidence” standard for issuing consumer protection complaints would help, on

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the margin, to embolden some defendants not to settle. Other proposed limits on the aggressive use of remedies and on the allowable scope of the Commission's consent orders would help to accomplish the same thing. Changing this dynamic even slightly could produce a significant shift in the agency's model, by injecting more judicial review into the FTC's evolution of its doctrine.

Commissioners themselves could play a greater role in constraining the FTC's discretion, as well, keeping the FTC focused on advancing consumer welfare in everything it does. Together with the Bureau of Economics, these two internal sources of constraint could partly substitute for the relative lack of external constraint from the courts.

We are not wholly critical of the FTC. Indeed, we are broadly supportive of its mission. And we support several measures to *expand* the FTC's jurisdiction to cover telecom common carriers and to make it easier for the FTC to prosecute non-profits that engage in for-profit activities. We enthusiastically support expansion of the FTC's Bureau of Economics. And we recommend expansion of the Commission's competition advocacy work into a full-fledged Bureau, so that the Commission can advocate at all levels of government—federal, state and local—on behalf of consumers and against legislation and regulations that would hamper the innovation and experimentation that fuel our rapidly evolving economy.

But most of all, Congress should not take the FTC's current processes for granted. Ultimately, the FTC reports to Congress and it is Congress's responsibility to regularly and carefully scrutinize how the agency operates. The agency's vague standards, sweeping jurisdiction, and its demonstrated ability to circumvent both judicial review and statutory safeguards on policy making make regular reassessment of the Commission through biennial reauthorization crucial to its ability to serve the consumers it is tasked with protecting.

TABLE OF CONTENTS

- Executive Summary
- Introduction
 - The FTC's History: Past is Prologue
 - The Inevitable Tendency Towards the Discretionary Model
 - The Doctrinal Pyramid
 - Our Proposed Reforms
- FTC Act Statutory Standards
 - Unfairness
 - The Statement on Unfairness Reinforcement & Emphasis (SURE) Act
 - Deception & Materiality
 - No Bill Proposed
 - Unfair Methods of Competition
 - No Bill Proposed
- Enforcement & Guidance
 - Investigations and Reporting on Investigations
 - The Clarifying Legality & Enforcement Action Reasoning (CLEAR) Act
 - Economic Analysis of Investigations, Complaints, and Consent Decrees
 - No Bill Proposed
 - Economic Analysis in Reports & "Recommendations"
 - The Revealing Economic Conclusions for Suggestions (RECS) Act
 - Other Sources of Enforcement Authority (Guidelines, etc.)
 - The Solidifying Habitual & Institutional Explanations of Liability & Defenses (SHIELD) Act
- Remedies
 - Appropriate Tailoring of Remedies
 - No Bill Proposed
 - Consent Decree Duration & Scope
 - The Technological Innovation through Modernizing Enforcement (TIME) Act
- Other Process Issues
 - Open Investigations
 - The Start Taking Action on Lingering Liabilities (STALL) Act
 - Commissioner Meetings
 - The Freeing Responsible & Effective Exchanges (FREE) Act
 - Part III Litigation
 - Standard for Settling Cases
 - No Bill Proposed
- Competition Advocacy

- Expanding FTC Jurisdiction
 - FTC Jurisdiction over Common Carriers
 - The Protecting Consumers in Commerce Act of 2016
 - FTC Jurisdiction over Tax-Exempt Organizations & Nonprofits
 - The Tax Exempt Organizations Act
- Rulemaking
 - Economic Analysis in All FTC Rulemakings
 - No Bill Proposed
 - Issue-Specific Rulemakings
 - Several Bills Proposed
- Conclusion

Considering that rules of the Commission may apply to any act or practice “affecting commerce”, and that the only statutory restraint is that it be unfair, *the apparent power of the Commission with respect to commercial law is virtually as broad as the Congress itself. In fact, the Federal Trade Commission may be the second most powerful legislature in the country.* . . . All 50 State legislatures and State Supreme Courts can agree that a particular act is fair and lawful, but the five-man appointed FTC can overrule them all. *The Congress has little control over the far-flung activities of this agency short of passing entirely new legislation.*¹—Sens. Barry Goldwater & Harrison Schmitt, 1980

*Within very broad limits, the agency determines what shall be legal. Indeed, the agency has been “lawless” in the sense that it has traditionally been beyond judicial control.*²—Former FTC Chairman Tim Muris, 1981

*The FTC’s investigatory power is very broad and is akin to an inquisitorial body. On its own initiative, it can investigate a broad range of businesses without any indication of a predicate offense having occurred.*³—Prof. Chris Hoofnagle, 2016

Introduction

Only by the skin of its teeth did the Federal Trade Commission survive its cataclysmic confrontation with Congress in 1980. Today, the Federal Trade Commission remains the closest thing to a second national legislature in America. Its jurisdiction covers nearly every company in America. It powers over unfair and deceptive acts and practices (UDAP) and unfair methods of competition (UMC) remain so inherently vague that the Commission retains unparalleled discretion to make policy decisions that are essentially legislative. The Commission increasingly wields these powers over high tech issues affecting not just the high tech *sector*, but, increasingly, every company in America. It has become the de facto Federal *Technology* Commission—a moniker we coined,⁴ but which Chairwoman Edith Ramirez has embraced.⁵

For all this power, either by design or by neglect, the FTC is also “a largely unconstrained agency.”⁶ “Although appearing effective, most means of controlling Commission actions are virtually useless, owing to lack of political support and information, lack of interest on the part of those ostensibly monitoring the FTC, or FTC maneuvering.”⁷ At the same time, “[t]he courts place almost no restraint upon what commercial practices the FTC can proscribe. . . .”⁸

The vast majority of what the FTC does is uncontroversial—routine antitrust, fraud and advertising cases. Yet, as the FTC has dealt with cutting-edge legal

¹S. Rep. No. 96–184, at 18 (1980), available at <http://digitalcollections.library.cmu.edu/awweb/awarchive?type=file&item=417102>.

²Timothy J. Muris, *Judicial Constraints*, in *THE FEDERAL TRADE COMMISSION SINCE 1970: ECONOMIC REGULATION AND BUREAUCRATIC BEHAVIOR*, 35, 49 (Kenneth W. Clarkson & Timothy J. Muris, eds., 1981).

³CHRIS JAY HOOFNAGLE, *FEDERAL TRADE COMMISSION PRIVACY LAW & POLICY* 102 (2016).

⁴Berin Szóka & Geoffrey Manne, *The Second Century of the Federal Trade Commission*, *TECHDIRT* (Sept. 26, 2013), available at <https://www.techdirt.com/blog/innovation/articles/20130926/16542624670/second-century-federal-trade-commission.shtml>; see also *Consumer Protection & Competition Regulation in a High-Tech World: Discussing the Future of the Federal Trade Commission*, Report 1.0 of the FTC: Technology & Reform Project, 3 (Dec. 2013), available at http://docs.techfreedom.org/FTC_Tech_Reform_Report.pdf.

⁵Kai Ryssdal, *The FTC is Dealing with More High Tech Issues*, *MARKETPLACE* (Mar. 7, 2016), available at <http://www.marketplace.org/2016/03/07/tech/ftc-dealing-more-high-tech-issues>.

⁶*Part I: The Institutional Setting*, in *THE FEDERAL TRADE COMMISSION SINCE 1970*, *supra* note 2 at 11.

⁷*Id.* at 11–12.

⁸Timothy J. Muris, *Judicial Constraints*, in *id.* 35, 43.

issues, like privacy, data security and product design, it has raised deep concerns not merely about the specific cases brought by the FTC, but also that the agency is drifting away from the careful balance it struck in its 1980 Unfairness Policy Statement (UPS)⁹ and its 1983 Deception Policy Statement (DPS).¹⁰

We applaud the Commerce, Manufacturing & Trade Subcommittee for taking up the issue of FTC reform, and for the seventeen bills submitted by members of both parties. Even if no legislation passes this Congress, active engagement by Congress in the operation of the Commission was crucial in the past to ensuring that the FTC does not stray from its mission of serving consumers. But active congressional oversight has been wanting for far too long.

Not since 1996 has Congress reauthorized the FTC,¹¹ and not since 1994 has Congress actually substantially modified the FTC's standards or processes.¹²

The most significant thing Congress has done regarding the FTC since 1980 was the 1994 codification of the Unfairness Policy Statement's three-part balancing test in Section 5(n). But even that has proven relatively ineffective: The Commission pays lip service to this test, but there has been essentially none of analytical development promised by the Commission in the 1980 UPS:

The present understanding of the unfairness standard is the result of an evolutionary process. The statute was deliberately framed in general terms since Congress recognized the impossibility of drafting a complete list of unfair trade practices that would not quickly become outdated or leave loopholes for easy evasion. The task of identifying unfair trade practices was therefore assigned to the Commission, *subject to judicial review, in the expectation that the underlying criteria would evolve and develop over time.*

The Commission no doubt believes that it has carefully weighed (1) substantial consumer injury with (2) countervailing benefit to consumers or to competition, and carefully assessed whether (3) consumers could “reasonably have avoided” the injury, as Congress required by enacting Section 5(n). But whatever weighing the Commission has done in its internal decision-making is far from apparent from the outside, and it has not been done by the courts in any meaningful way.¹³ As former Chairman Tim Muris notes, “the Commission’s authority remains extremely broad.”¹⁴

The situation is little on better on Deception—at least, on the cutting edge of Deception cases, involving privacy policies, online help pages, and enforcement of other promises that differ fundamentally from traditional marketing claims. Just as the Commission has rendered the three-part Unfairness test essentially meaningless, it has essentially nullified the “materiality” requirement that it volunteered in the 1983 Deception Policy Statement. The Statement began by presuming, reasonably, that express *marketing* claims are always material, but the Commission has extended that presumption (and other narrow presumptions of materiality in the DPS) to cover essentially *all* deception cases.¹⁵

Congress cannot fix these problems simply by telling the FTC to dust off its two bedrock policy statements and take them more seriously (as it essentially did in 1994 regarding Unfairness). Instead, Congress must fundamentally reassess the *process* that has allowed the FTC to avoid judicial scrutiny of how it wields its discretion.

The last time Congress significantly reassessed the FTC's *processes* was in May 1980, when it created procedural safeguards and evidentiary requirements for FTC rulemaking. These reforms were much needed, and remain fundamentally necessary (although we do, below, encourage the FTC to attempt a Section 5 rulemaking for the first time in decades in order to provide a real-world experience of how such

⁹ *Letter from the FTC to the House Consumer Subcommittee, appended to In re Int'l Harvester Co.*, 104 F.T.C. 949, 1073 (1984) [“Unfairness Policy Statement” or “UPS”], available at <http://www.ftc.gov/ftc-policy-statement-on-unfairness>.

¹⁰ *Letter from the FTC to the Committee on Energy & Commerce, appended to Cliffdale Assocs., Inc.*, 103 F.T.C. 110, 174 (1984) [“Deception Policy Statement” or “DPS”], available at <http://www.ftc.gov/ftc-policy-statement-on-deception>.

¹¹ Federal Trade Commission Reauthorization Act of 1996, Pub. L. 104–216, 110 Stat. 3019 (Oct. 1, 1996), available at <http://uscode.house.gov/statutes/pl/104/216.pdf>.

¹² Federal Trade Commission Act Amendments of 1994, Pub. L. 103–312, 108 Stat. 1691 (Aug. 26, 1994) available at <http://uscode.house.gov/statutes/pl/103/312.pdf>.

¹³ See *infra* at 39.

¹⁴ Statement of Timothy J. Muris, Hearing on Financial Services and Products: The Role of the Fed. Trade Commission in Protecting Customers, before the Subcomm. on Consumer Protection, Product Safety, and Insurance of the S. Comm. on Commerce, Science, and Transportation, 111th Cong. 2 (2010), 28, available at http://lawprofessors.typepad.com/files/muris_senate_testimony_ftc_role_protecting_consumers_3-17-101.pdf.

¹⁵ See *infra* at 21.

rulemakings work and whether Congress might make changes at the margins to facilitate reliance on that tool).¹⁶

But these 1980 reforms failed to envision that the Commission would, eventually, find ways of exercising the vast discretion inherent in Unfairness and Deception through what it now proudly calls its “common law of consent decrees”¹⁷—company-specific, but cookie-cutter consent decrees that have little to do with the facts of each case (and always run for twenty years). These consent decrees are bolstered by the regular issuance of recommended best practices in reports and guides that function as quasi-regulations, imposed on entire industries not by rulemaking but by the administrative equivalent of a leering glare. Together, these new tactics have allowed the FTC to effectively circumvent not only the process reforms of May 1980 but also the substantive constraints volunteered by the FTC later that year in the Unfairness Policy Statement and, three years later, in the Deception Policy Statement.

Such process reforms are the focus of this paper. The seventeen bills currently before the Subcommittee would begin to address these problems—but only begin. In this paper we evaluate nine of the proposed bills in turn, offer specific recommendations, and also offer a slate of our own additional suggestions for reform.

Our most important point, though, is not any one of our proposed reforms, but this: The default assumption should not be that the FTC continues operating indefinitely without course corrections from Congress.

Justice Scalia put this point best in his 2014 decision, striking down the EPA’s attempt to “rewrite clear statutory terms to suit its own sense of how the statute should operate,” when he said: “We are not willing to stand on the dock and wave goodbye as EPA embarks on this multiyear voyage of discovery.”¹⁸ The point is more, not less, important when a statute like Section 5 has been “deliberately framed in general terms since Congress recognized the impossibility of drafting a complete list of unfair trade practices that would not quickly become outdated or leave loopholes for easy evasion”: trusting the FTC to follow an “evolutionary process” requires regular, searching reassessments by Congress. This need is especially acute given that the “underlying criteria” have *not* “evolve[d] and develop[ed] over time” through the “judicial review” expected by both Congress and the FTC in 1980—at least, not in any analytically meaningful way.

Reauthorization should happen at regular two-year intervals and it should never be a *pro forma* rubber-stamping of the FTC’s processes. Each reauthorization should begin from the assumption that the FTC is a uniquely important and valuable agency—one that can do enormous good for consumers, but also one whose uniquely broad scope and broad discretion require constant supervision and regular course corrections. Regular tweaks to the FTC’s processes should be expected and welcomed, not resisted.

The worst thing defenders of the FTC could do would be allowing the FTC to drift along towards the kind of confrontation with Congress that nearly destroyed the FTC in 1980.

The FTC’s History: Past is Prologue

It is no exaggeration to say that the 1980 compromise over unfairness saved the FTC from going the way of the Civil Aeronautics Board, which Congress began phasing out in 1978 under the leadership of Alfred Kahn, President Carter’s

¹⁶ See *infra* at 99.

¹⁷ “Together, these enforcement efforts have established what some scholars call ‘the common law of privacy’ in the United States.” Julie Brill, Commissioner, Fed. Trade Comm’n, *Remarks to the Mentor Group Forum for EU-US Legal-Economic Affairs Brussels, April 16, 2013*, 3 (Apr. 16, 2013), available at https://www.ftc.gov/sites/default/files/documents/public_statements/remarks-mentor-group-forum-eu-us-legal-economic-affairs-brussels-belgium/130416mentorgroup.pdf (citing Christopher Wolf, *Targeted Enforcement and Shared Lawmaking Authority As Catalysts for Data Protection in the United States* (2010), available at http://www.justice.gov/il/NR/rdonlyres/8D438C53-82C8-4F25-99F8-E3039D40E4E4/26451/Consumer_WOLF_DataProtectionandPrivacyCommissioners.pdf (FTC consent decrees have “created a ‘common law of consent decrees,’ producing a set of data protection rules for businesses to follow.”)). FTC Chairman Edith Ramirez said roughly the same thing in a 2014 speech:

I have expressed concern about recent proposals to formulate guidance to try to codify our unfair methods principles for the first time in the Commission’s 100 year history. While I don’t object to guidance in theory, I am less interested in prescribing our future enforcement actions than in describing our broad enforcement principles revealed in our recent precedent.

Quoted in Geoffrey Manne, *FTC Commissioner Joshua Wright gets his competition enforcement guidelines*, TRUTH ON THE MARKET (Aug. 13, 2015), available at <https://truthonthemarket.com/2015/08/13/ftc-commissioner-joshua-wright-gets-his-competiton-enforcement-guidelines/> (speech video available at <http://masonlec.org/media-center/299>).

¹⁸ *Util. Air Regulatory Grp. v. EPA*, 134 S. Ct. 2427, 2446 (2014).

deregulator-in-chief. President Carter signed the 1980 FTC Improvements Act even though he objected to some of its provisions because, as he noted, “the very existence of this agency is at stake.”¹⁹ Those reforms to the FTC’s rulemaking process, enacted in May 1980, were only part of what saved the FTC from oblivion.

Driven largely by outrage over the FTC’s attempt to regulate children’s advertising, Congress had allowed the FTC’s funding to lapse, briefly shuttering the FTC. As Howard Beales, then (in 2004) director of the FTC’s Bureau of Consumer Protection, noted, “shutting down a single agency because of disputes over policy decisions is almost unprecedented.”²⁰ In the mid-to-late 1970s, the FTC had interpreted “unfairness” expansively in an attempt to regulate everything from funeral home practices to labor practices and pollution. Beales and former FTC Chairman, Tim Muris, summarize the problem thusly:

Using its unfairness authority under Section 5, but unbounded by meaningful standards, in the 1970s the Commission embarked on a vast enterprise to transform entire industries. Over a 15-month period, the Commission issued a rule a month, usually without a clear theory of why there was a law violation, with only a tenuous connection between the perceived problem and the recommended remedy, and with, at best, a shaky empirical foundation.²¹

When the FTC attempted to ban the advertising of sugared cereals to children, the *Washington Post* dubbed the FTC the “National Nanny.”²² This led directly to the 1980 FTC Improvements Act—the one Sens. Goldwater and Schmitt endorsed in the quotation that opens this paper.

In early 1980, by a vote of 272–127, Congress curtailed the FTC’s Section 5 rulemaking powers under the 1975 Magnuson-Moss Act, imposing additional evidentiary and procedural safeguards.²³ But the FTC refused to narrow its doctrinal interpretation of unfairness until Congress briefly shuttered the FTC in the first modern government shutdown. In December, 1980, the FTC issued its Unfairness Policy Statement, promising to weigh (a) substantial injury against (b) countervailing benefit and (c) to focus only on practices consumers could not reasonably avoid. Last year, the FTC finally adopted a Policy Statement on Unfair Methods of Competition that parallels the two UDAP statements.²⁴

In 1994, in Section 5(n), Congress codified the core requirements of the UPS, and further narrowed the FTC’s ability to rely on its assertions of what constituted public policy. This was the last time Congress substantially modified the FTC Act—meaning that the Commission has operated since then without course-correction from Congress.²⁵ This is itself troubling, given that independent agencies are supposed to operate as creatures of Congress, not regulatory knights errant. But it is even more problematic given the extent of the FTC’s renewed efforts to escape the bounds of even its minimal discretionary constraints.

The Inevitable Tendency Towards the Discretionary Model

To paraphrase Winston Churchill on democracy, the FTC offers the “worst form of consumer protection and competition regulation—except for all the others.” Democracy, without constant vigilance and reform, will inevitably morph into the unaccountable exercise of power—what the Founders meant by the word “corruption” (literally, “decayed”). When Benjamin Franklin was asked, upon exiting the Con-

¹⁹ Jimmy Carter, *Federal Trade Commission Improvements Act of 1980 Statement on Signing H.R. 2313 into Law* (May 28, 1980), available at <http://www.presidency.ucsb.edu/ws/?pid=44790>.

²⁰ J. Howard Beales III, *Advertising to Kids and the FTC: A Regulatory Retrospective that Advises the Present*, 8 n.32 (2004), available at https://www.ftc.gov/sites/default/files/documents/public_statements/advertising-kids-and-ftc-regulatory-retrospective-advises-present/040802adsto-kids.pdf.

²¹ J. Howard Beales III & Timothy J. Muris, *Striking the Proper Balance: Redress Under Section 13(B) of the FTC Act*, 79 ANTITRUST L. J. 1, 1 (2013), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2764456.

²² Editorial, WASH. POST (Mar. 1, 1978), reprinted in MICHAEL PERTSCHUK, REVOLT AGAINST REGULATION, 69–70 (1982); see also Beales, *supra* note 20, at 8 n.37 (“Former FTC Chairman Pertschuk characterizes the *Post* editorial as a turning point in the Federal Trade Commission’s fortunes.”).

²³ Federal Trade Commission Act Improvements Act of 1980, Pub. L. 96–252, 94 Stat. 374 (May 28, 1980), available at <http://uscode.house.gov/statutes/pl/96/252.pdf>.

²⁴ Fed. Trade Comm’n, *Statement of Enforcement Principles Regarding “Unfair Methods of Competition” Under Section 5 of the FTC Act* (Aug. 13, 2015) [“UMC Policy Statement”], available at https://www.ftc.gov/system/files/documents/public_statements/735201/150813section5enforcement.pdf.

²⁵ The 1996 FTC reauthorization was purely *pro forma*.

stitutional Convention of 1787, “Well, Doctor, what have we got—a Republic or a Monarchy?” he famously remarked “A Republic, if you can keep it.”²⁶

The same can be said for the FTC: an “evolutionary process . . . subject to judicial review,”²⁷ *if we can keep it*. Any agency given so broad a charge as to prohibit “unfair methods of competition . . . and unfair or deceptive acts or practices . . .” will inevitably tend towards the exercise of maximum discretion.

This critique is of a dynamic inherent in the FTC itself, not of particular Chairmen, Commissioners, Bureau Directors or other staffers. The players change regularly, each leaving their mark on the agency, but the agency has institutional tendencies of its own, inherent in the nature of the agency.

The Commission itself most clearly identified the core of the FTC’s institutional nature in the Unfairness Policy Statement, in a passage so critical it bears quoting in full:

The present understanding of the unfairness standard is the result of an evolutionary process. The statute was deliberately framed in general terms since Congress recognized the impossibility of drafting a complete list of unfair trade practices that would not quickly become outdated or leave loopholes for easy evasion. The task of identifying unfair trade practices was therefore assigned to the Commission, subject to judicial review, in the expectation that the underlying criteria would evolve and develop over time. As the Supreme Court observed as early as 1931, the ban on unfairness “belongs to that class of phrases which do not admit of precise definition, but the meaning and application of which must be arrived at by what this court elsewhere has called ‘the gradual process of judicial inclusion and exclusion.’”²⁸

In other words, Congress delegated vast discretion to the Commission from the very start because of the difficulties inherent in prescriptive regulation of competition and consumer protection. The Commission generally exercised that discretion primarily through case-by-case adjudication, but began issuing rules on its own authority in 1964,²⁹ setting it on the road that culminated in the cataclysm of 1980.

Indeed, given the essential nature of bureaucracies, it was probably only a matter of time before the FTC reached this point. It is no accident that it took just three years from 1975, when Congress affirmed the FTC’s claims to “organic” rulemaking power (implicit in Section 5), until the FTC was being ridiculed as the “National Nanny.” In short, the 1975 Magnuson-Moss Act created a monster, magnifying the effects of the FTC’s inherent Section 5 discretion with the ability to conduct statutorily sanctioned rulemakings. If it had not been then-Chairman Michael Pertschuk who pushed the FTC too far, it probably would have, eventually, been some other chairman. The power was simply too great for any government agency to resist using without some feedback mechanism in the system telling it to stop.

In that sense, we believe the rise of the Internet played a role analogous to the 1975 Magnuson-Moss Act, spurring the FTC to greater activity where it had previously been more restrained.³⁰

After 1980, the FTC ceased conducting new Section 5 rulemakings. Between 1980 and 2000, the FTC brought just sixteen unfairness cases, all of which fell into narrow categories of clearly “bad” conduct: “(1) theft and the facilitation thereof (clearly the leading category); (2) breaking or causing the breaking of other laws; (3) using insufficient care; (4) interfering with the exercise of consumer rights; and (5) advertising that promotes unsafe practices.”³¹ Just how easy these cases were conveys in turn just how *cautious* the Commission was in using its unfairness powers—not only because it was chastened by the experience of 1980 but also because of Congress’s reaffirmation of the limits on unfairness in its 1994 codification of Section 5(n). In a 2000 speech, Commissioner Leary summarized the Commission’s restrained, “gap-filling” approach to unfairness enforcement over the preceding two decades:

The overall impression left by this body of law is hardly that policy has been created from whole cloth. Rather, the Commission has sought through its un-

²⁶ Benjamin Franklin, *quoted in* Respectfully Quoted: A Dictionary of Quotations, BARTLEBY.COM (last visited May 22, 2016), <http://www.bartleby.com/73/1593.html>

²⁷ UPS, *supra* note 9.

²⁸ UPS, *supra* note 9.

²⁹ Statement of Basis and Purpose, Unfair or Deceptive Advertising and Labeling of Cigarettes in Relation to the Health Hazards of Smoking, 29 Fed. Reg. 8324, 8355 (1964).

³⁰ Of course, we also recognize that other societal forces were at work, such as the Naderite consumer protection movement of the 1970s, and the growing privacy protection movement of the 1990s and 2000s. But the analogy still offers some value.

³¹ Stephen Calkins, *FTC Unfairness: An Essay*, 46 WAYNE L. REV. 1935, 1962 (2000).

fairness authority to challenge commercial conduct that under any definition would be considered wrong but which escaped or evaded prosecution by other means.³²

Yet even then Commissioner Leary noted his concerns about the burgeoning unfairness enforcement innovation in two of the Commission's then-recent cases: *Touch Tone* (1999)³³ and *ReverseAuction* (2000). Tellingly, his concern was over the Commission's failure to properly assess the substantiality of the amorphous privacy injuries alleged in those cases. Still, he concluded on a note of optimism:

The extent of the disagreement should not be exaggerated, however. The majority [in *Reverse Auction*] did not suggest that all privacy infractions are sufficiently serious to be unfair and the minority did not suggest that none of them are. The boundaries of unfairness, as applied to Internet privacy violations, remain an open question.

The Commission has so far used its unfairness authority in relatively few cases that involve the Internet. These cases, however, suggest that future application of unfairness will be entirely consistent with recent history. Internet technology is new, but we have addressed new technology before. I believe that the Commission will do what it can to prevent the Internet from becoming a lawless frontier, but it will also continue to avoid excesses of paternalism.

The lessons of the past continue to be relevant because the basic patterns of dishonest behavior continue to be the same. Human beings evolve much more slowly than their artifacts.³⁴

The Commission began bringing cases in 2000 alleging that companies employed unreasonable data security practices. While these early cases alleged that the practices were "unfair *and* deceptive," they were, in fact, pure deception cases.³⁵ In 2005, the FTC filed its first pure unfairness data security action, against BJ's Warehouse. Unlike past defendants, BJ's had, apparently, made no promise regarding data security upon which the FTC could have hung a deception action.³⁶ Since 2009, we believe the Commission has become considerably more aggressive in its prosecution of unfairness cases, not just about data security, but about privacy and other high tech issues like product design.

Yet it would be hard to pinpoint a single moment when the FTC's approach changed, or to draw a clear line between Republican data security cases and Democratic ones. And this is precisely a function of the first of the two crucial attributes of the modern FTC with which we are concerned: Legal doctrine continues to evolve even in the absence of judicial decisions, its evolution just becomes less transparent and more amorphous. As Commissioner Leary remarked in a footnote that now seems prescient:

Because this case was settled, I cannot be sure that the other Commissioners agreed with this rationale.³⁷

Indeed, this is the crucial difference between the FTC's pseudo common law and *real* common law. There is an observable directedness to the evolution of the real common law, which rests on a sort of ongoing conversation among the courts and the economic actors that appear before them. The FTC's ersatz common law, however, has little of this directedness or openness, and the conversations that do occur are more like whispered tête-à-têtes in the corner that someone else occasionally overhears.

³²Thomas B. Leary, Former Commissioner of the Fed. Trade Comm'n, *Unfairness and the Internet*, II (Apr. 13, 2000), available at <http://www.ftc.gov/public-statements/2000/04/unfairness-and-internet>.

³³*Id.* at II-C ("The unfairness count in *Touch Tone* also raised interesting questions about whether an invasion of privacy by itself meets the statutory requirement that unfairness cause "substantial injury." Unlike most unfairness prosecutions, there was no concrete monetary harm or obvious and immediate safety or health risks. The defendants' revenue came, not from defrauding consumers, but from the purchasers of the information who received exactly what they had requested.")

³⁴*Id.*, at III-IV.

³⁵See, e.g., *FTC v. Rennert*, Complaint, FTC File No. 992 3245, <http://www.ftc.gov/os/2000/07/iogcomp.htm> (2000); *In re Eli Lilly*, Complaint, File No. 012 3214, <http://www.ftc.gov/os/2002/05/elilillycomp.htm> (2002).

³⁶Complaint, *In the Matter of BJ's Wholesale Club, Inc.*, a corporation, Fed. Trade Comm'n Docket No. C-4148, available at <http://www.ftc.gov/enforcement/cases-proceedings/042-3160/bjs-wholesale-club-inc-matter>.

³⁷Leary, *Unfairness and the Internet*, *supra* note 32, n.50.

But the second point is actually the more important, although the two are related: In this institutional structure, how often individual Commissioners dissent and how much rigor they demand matters far, far less than the structure of the agency itself. There is only so much an individual can do to divert the path of an already-steaming ship.

This leads back to the point made above: that we should expect regulatory agencies, over time, to expand their discretion as much as the constraints upon the agency allow. In this, regulatory agencies resemble gases, which, when unconstrained, do not occupy a fixed volume (defined by a clear statutory scheme, as in the Rule-making Model) but rather expand to fill whatever space they occupy. What ultimately determines the size, volume and shape of a gas is its container. So, too, with regulatory agencies: what ultimately determines an agency's scale, scope, and agenda are the external constraints that operate upon it.

The FTC has evolved the way it has because, most fundamentally, Section 5 offers little in the way of prescriptive, statutory constraints, and because the FTC's processes have enabled it to operate case-by-case with relatively little meaningful, ongoing oversight from the courts.

We distinguish this from two other models of regulation: (1) the *Rulemaking Model*, in which the agency's discretion is constrained chiefly by the language of its organic statute, procedural rulemaking requirements and the courts; and (2) the *Evolutionary Model*, in which the agency applies a vague standard case by case, but is constrained in doing so by its ongoing interaction with the courts.³⁸ By contrast, we call the FTC's current approach the *Discretionary Model*, in which the agency also applies a vague standard case-by-case, but in which it operates without meaningful judicial oversight, such that doctrine evolves at the Commission's discretion and with little of the transparency provided by published judicial opinions. (Dialogue between majority and minority Commissioners seldom approaches the analysis of judicial opinions.)

We believe there is an inherent tendency of agencies that begin with an Evolutionary Model—which is very much the design of the FTC—to slide towards the Discretionary Model, simply because all agencies tend to maximize their own discretion, and because the freedom afforded by the lack of statutory constraints on substance or the agency's case-by-case process enable these agencies to further evade judicial constraints. The only way to check this process, without, of course, simply circumscribing its discretion by substantive statute (*i.e.*, amending section 5(a)(2)), is regular assessment and course-correction by Congress—not with the aim of its own micromanagement of the agency, but rather with the aim of invigorating the ability of the courts to exert their essential role in steering doctrine.

This is not to be taken as an admission of defeat or a condemnation of the Commission. There is no reason to think that the FTC was in every way ideally constituted from the start (or in 1980 or in 1994), that its model could perform exactly as intended and perfectly in the public interest no matter what changed around it. Rather, limited, thoughtful oversight by Congress is simply in the nature of the beast. As Justice Holmes said (of the importance of free speech):

That, at any rate, is the theory of our Constitution. It is an experiment, as all life is an experiment. Every year, if not every day, we have to wager our salvation upon some prophecy based upon imperfect knowledge.³⁹

That, in a nutshell, is why regular reauthorization is critical for agencies like the FTC. As President Carter said, “[w]e need vigorous congressional oversight of regulatory agencies.” This is more true for the FTC—with its vast discretion, immense investigative power, and all-encompassing scope—than any other agency. As we wrote in the precursor to this report:

Thus, while the Congress of 1914 intended to create an agency better suited than itself to establish a flexible but predictable and consistent body of law governing commercial conduct, the modern trend of administrative law has relaxed the requirement that an agency's output be predictable or consistent.

³⁸We derive the term “evolutionary” from the Unfairness Policy Statement itself, *supra* note 9:

The present understanding of the unfairness standard is the result of an evolutionary process. The statute was deliberately framed in general terms since Congress recognized the impossibility of drafting a complete list of unfair trade practices that would not quickly become outdated or leave loopholes for easy evasion. The task of identifying unfair trade practices was therefore assigned to the Commission, subject to judicial review, in the expectation that the underlying criteria would evolve and develop over time.

³⁹*Abrams v. United States*, 250 U.S. 616, 630 (1919) (Holmes, J. dissenting).

The FTC has embraced this flexibility as few other agencies have. Particularly in its efforts to keep pace with changing technology, the FTC has embraced its role as an administrative agency, and frequently sought to untether itself from ordinary principles of jurisprudence (let alone judicial review).⁴⁰

The Doctrinal Pyramid

One of the chief reasons the FTC has come to operate the way it does is that the vocabulary around its operations is deeply confused, particularly around the word “guidance” and the term “common law.” In an (admittedly first-cut) effort to introduce some concreteness, we view the various levels of “guidance” as steps in a Doctrinal Pyramid that looks something like the following, from highest to lowest degrees of authority:

1. *The Statute*: Section 5 (and other, issue-specific statutes)
2. *Litigated Cases*: Only these are technically binding on courts, thus they rank near the top of the pyramid, even though they are synthesized in, or cited by, the guidance summarized below. There are precious few of these on Unfairness or the key emerging issues of Deception
3. *Litigated Preliminary Injunctions*: Less meaningful than full adjudications of Section 5, these are, unfortunately, largely the only judicial opinions on Section 5.
4. *High-Level Policy Statements*: Unfairness, Deception, Unfair Methods of Competition
5. *Lower-Level Policy Statements*: The now-rescinded Disgorgement Policy Statement, the (not-yet existent) Materiality Statement we propose, *etc.*
6. *Guidelines*: Akin to the several DOJ/FTC Antitrust Guidelines, synthesizing past approaches to enforcement into discernible principles to guide future enforcement and compliance
7. *Consent Decrees*: Not binding upon the Commission and hinging (indirectly) upon the very low bar of whether the Commission has “reason to believe” a violation occurred, these provide little guidance as to how the FTC really understands Section 5
8. *Closing Letters*: Issued by the staff, these letters at times provide some limited guidance as to what the staff believe is *not* illegal
9. *Reports & Recommendations*: In their current form, the FTC’s reports do little more than offer the majority’s views of what companies should do to comply with Section 5, but carefully avoid any real legal analysis
10. *Industry Guides*: Issue-specific discussions issued by staff (*e.g.*, photo copier data security)
11. *Public Pronouncements*: Blog posts, press releases, congressional testimony, FAQs, *etc.*

In essence, under today’s Discretionary Model, the FTC puts great weight on the base of the pyramid, while doing little to develop the top. Under the Evolutionary Model, the full Commission would develop doctrine primarily through litigation, and do everything it possibly could to provide guidance at higher levels of the pyramid, such as by debating, refining and voting upon new Policy Statements on each of the component elements of Unfairness and Deception and Guidelines akin to the Horizontal Merger Guidelines. Instead, the FTC staff issues Guides and other forms of casual guidance. Yet not all “guidance” is of equal value. Indeed, much of the “guidance” issued by the FTC serves not to constrain its discretion, but rather to expand it by increasing the agency’s ability to coerce private parties into settlements—which begins the cycle anew.

Our Proposed Reforms

Seventeen bills have been introduced in the House Energy & Commerce Committee’s Subcommittee on Commerce, Manufacturing and Trade aimed at reforming the agency for the modern, technological age and improving FTC process and subject-matter scope in order to better protect consumers. Most of these will, we hope, be consolidated into a single FTC Reauthorization Act of 2016, passed in both chambers, and signed by the President.

With the hope of aiding this process, we describe and assess nine of these proposed bills, focusing in particular on whether and how well each proposal addresses

⁴⁰ *Consumer Protection & Competition Regulation in a High-Tech World*, *supra*, note 4.

the fundamental issues that define the problems of today's FTC. In broad strokes, the proposed bills address the following areas:

- Substantive standards
- Enforcement and guidance
- Remedies
- Other process issues
- Jurisdictional issues
- Other issues

Our analysis addresses the bills within the context of these broad categories, and adds our own suggestions (and one additional category: Competition Advocacy) for both minor amendments and additional legislation in each category.

Despite our concerns, we remain broadly supportive of the FTC's mission and we generally support expanding the agency's jurisdiction, to the extent that doing so effectively addresses substantial, identifiable consumer harms or reduces the scope of authority for sector-specific agencies. Although the process reforms proposed in these bills are, we believe, relatively minor, targeted adjustments, taken together they would do much to make the FTC more effective in its core mission of maximizing consumer welfare. But these proposed reforms are only a beginning.

Even if all of these reforms were enacted immediately, they would not fundamentally, or even substantially, change the core functioning of the FTC—and the core problem at the FTC today: its largely unconstrained discretion.

The FTC loudly proclaims the advantages of its *ex post* approach of relying on case-by-case enforcement of UDAP and UMC standards rather than rigid *ex ante* rulemaking, especially over cutting-edge issues of consumer protection. And there is much to commend this sort of approach relative to the prescriptive regulatory paradigm that characterizes many other agencies—again, the Evolutionary Model. But under the FTC's *Discretionary* Model, the Commission uses its “common law of consent decrees” (more than a hundred high-tech cases settled without adjudication, and with essentially zero litigated cases to guide these settlements) and a mix of other forms of soft law (increasingly prescriptive reports based on workshops tailored to produce predetermined outcomes, and various other public pronouncements), to “regulate”—or, more accurately, to try to steer—the evolution of technology.

The required balancing of tradeoffs inherent in unfairness and deception have little meaning if the courts do not review, follow or enforce them; if the Bureau of Economics has little role in the evaluation of these inherently economic considerations embodied in the enforcement decision-making of the Bureau of Consumer Protection or in its workshops; and if other Commissioners are able only to quibble on the margins about the decisions made by the FTC Chairman. Simply codifying these standards, as Congress codified the heart of the Unfairness Policy Statement in Section 45(n) back in 1994, and as the proposed CLEAR Act would finish doing, will not solve the problem: The FTC has routinely circumvented the rigorous analysis demanded by these standards, and the same processes would enable it to continue doing so.

To address these concerns, we also propose here a number of further process reforms that we believe would begin to correct these problems and ensure that the Commission's process really does serve the consumers the agency was tasked with protecting.

Our aim is not to hamstring the Commission, but to ensure that it wields its mighty powers with greater analytical rigor—something that should inure significantly to the benefit of consumers. Ideally, the impetus for such rigor would be provided by the courts, through careful weighing of the FTC's implementation of substantive standards in at least a small-but-significant percentage of cases. Those decisions would, in turn, shape the FTC's exercise of its discretion in the vast majority of cases that will—and should, in such an environment—inevitably settle out of court. The Bureau of Economics and the other Commissioners would also have far larger roles in ensuring that the FTC takes its standards seriously. But reaching these outcomes requires adjustment to the Commission's *processes*, not merely further codification of the standards the agency already purports to follow.

We believe that our reforms should attract wide bipartisan support, if properly understood, and that they would put the FTC on sound footing for its second century—one that will increasingly see the FTC assert itself as the Federal Technology Commission.

FTC Act Statutory Standards

Unfairness

THE STATEMENT ON UNFAIRNESS REINFORCEMENT & EMPHASIS (SURE) ACT

Rep. Markwayne Mullin’s (R–OK) bill (H.R. 5115)⁴¹ further codifies promises the FTC made in its 1980 Unfairness Policy Statement—thus picking up where Congress left off in 1994, the last time Congress reauthorized the FTC in Section 5(n):

The Commission shall have no authority . . . to declare unlawful an act or practice on the grounds that such act or practice is unfair unless the act or practice [i] causes or is likely to cause substantial injury to consumers [ii] which is not reasonably avoidable by consumers themselves and [iii] not outweighed by countervailing benefits to consumers or to competition. In determining whether an act or practice is unfair, the Commission may consider established public policies as evidence to be considered with all other evidence. Such public policy considerations may not serve as a primary basis for such determination.⁴²

This effectively codified the core of the Unfairness Policy Statement, while barring the FTC from relying on public policy determinations alone.⁴³ The bill would add several additional clauses to Section 5(n), drawn from the Unfairness Policy Statement. Most importantly:

1. It would exclude “trivial or merely speculative” harm from the definition of “substantial” injury.⁴⁴
2. It would enhance the Act’s “countervailing benefits” language to require consideration of the “net effects” of conduct, including dynamic, indirect consequences (like effects on innovation).⁴⁵
3. It would prohibit the Commission from “second-guess[ing] the wisdom of particular consumer decisions,” and encourage it to ensure “the free exercise of consumer decisionmaking.”⁴⁶

These provisions in particular (along with the others included in the bill, to be sure) would codify core aspects of the economic trade-off embodied in the UPS. They would enhance the Commission’s administrative efficiency and direct its resources where consumers are most benefited. They would ensure that the FTC’s weighing of costs and benefits is as comprehensive as possible, avoiding the systematic focus on concrete, short-term costs to the exclusion of larger, longer-term benefits. And they would help to preserve the inherent benefits of consumer choice, and avoid the intrinsic costs of agency paternalism.

Codification of these provisions would benefit consumers. And because H.R. 5115’s language hews almost verbatim to the Unfairness Policy Statement, it should be uncontroversial. Effectively, it simply makes binding those parts of the UPS that Congress did not codify back in 1994.

Value of the Bill: Codifying the Unfairness Policy Statement Would Reaffirm its Value, Encouraging Dissents and Litigation

Codifying a policy statement, even if verbatim and only in part, does essentially four things:

⁴¹The Statement on Unfairness Reinforcement and Emphasis Act, H.R. 5115, 114th Cong. (2016) [hereinafter SURE Act] available at <https://www.congress.gov/bills/114/congress/house-bill/5115/text>.

⁴²15 U.S.C. § 45(n).

⁴³The Unfairness Policy Statement had said:

Sometimes public policy will independently support a Commission action. This occurs when the policy is so clear that it will entirely determine the question of consumer injury, so there is little need for separate analysis by the Commission. . . .

To the extent that the Commission relies heavily on public policy to support a finding of unfairness, the policy should be clear and well-established. In other words, the policy should be declared or embodied in formal sources such as statutes, judicial decisions, or the Constitution as interpreted by the courts, rather than being ascertained from the general sense of the national values. The policy should likewise be one that is widely shared, and not the isolated decision of a single state or a single court. If these two tests are not met the policy cannot be considered as an “established” public policy for purposes of the S&H criterion. The Commission would then act only on the basis of convincing independent evidence that the practice was distorting the operation of the market and thereby causing unjustified consumer injury.

UPS, *supra* note 9.

⁴⁴SURE Act, *supra* note 41.

⁴⁵*Id.*

⁴⁶*Id.*

1. Legally, it makes the policy binding upon the Commission, since Policy Statements, technically, are not. On the margin this should deter the FTC from bringing more-tenuous cases that may not benefit consumers but that it might otherwise have brought.
2. Practically, it confers greater weight on the codified text in the Commission's deliberations, empowering dissenting Commissioners to point to the fact that Congress has chosen to codify certain language and requiring the majority to respond.
3. Legally, it somewhat reduces the deference the courts will give the FTC when it applies the statute (under *Chevron*) relative to the stronger deference given to agencies applying their own policy statements (under *Auer*).⁴⁷
4. Perhaps most importantly, it gives defendants a stronger leg to stand on in court, thus increasing, on the margin, the number that will actually litigate rather than settle. That, in turn, benefits everyone by increasing the stock of judicial analysis of doctrine.

In all four respects, the FTC would greatly benefit from the H.R. 5115's further codification of the Unfairness Policy Statement. As a string of dissenting statements by former Commissioner Wright make lays bare, the FTC is not consistently taking the Unfairness Policy Statement seriously.⁴⁸ At most, it pays lip service even to the three core elements of unfairness set forth in Section 5(n)—and even less regard to those aspects of the UPS not codified in Section 5(n).⁴⁹

Indeed, it is difficult to imagine any principled objection to codifying a document that the FTC already claims to observe carefully. And if the agency plans to bring unfairness cases that are *not* covered by the four corners of the Unfairness Policy Statement (yet somehow within Section 5(n)), that should be a matter of grave concern to Congress.

Recommendation: Require a Preponderance of the Evidence Standard for Unfairness Complaints

As valuable as codification of the substantive standards of the Unfairness Policy Statement would be, mere codification, or even tweaking, is unlikely to change much about the FTC's apparent evasion of its obligation to adhere to those standards. Rather, unless the *process* of enforcement by which the FTC has evaded the limits of the Statement is adjusted, the Commission will remain free to avoid the rigor it contemplates.

Indeed, it is far from clear that even the 1994 codification of the heart the Unfairness Policy Statement has been effective in actually changing the FTC's approach to enforcement. It is certainly possible that, but for Section 5(n), the Commission would have taken an even more aggressive approach to unfairness, and done even less to analyze its component elements in enforcement actions.

The process reforms we propose below are intended either (a) to increase the likelihood that the FTC will actually litigate unfairness cases, thus gaining judicial development of the doctrine, (b) that the Commissioners themselves will better develop doctrine through debate, or (c) that FTC staff, particularly through the involvement of the Bureau of Economics, will do so. Some combination of these (and, doubtless, other) reforms is essential to giving effect to Section 5(n) in its current form, to say nothing of expanding 5(n).

But the reform that would make the biggest difference within 5(n) itself would be to amend the existing Section 5(n) as follows:

The Commission may not issue a complaint under this section unless the Commission demonstrates by a *preponderance of objective evidence* that an act or practice causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers themselves and not outweighed by countervailing benefits to consumers or to competition.

The preponderance of the evidence standard is certainly a higher standard than the FTC currently faces for bringing complaints, but only because that standard is

⁴⁷Note that not everyone agrees that *Chevron* deference is weaker than *Auer* deference. See Sasha Volokh, *Auer and Chevron*, THE VOLOKH CONSPIRACY (Mar. 22, 2013), available at <http://volokh.com/2013/03/22/auer-and-chevron/>.

⁴⁸See, e.g., Dissenting Statement of Commissioner Joshua D. Wright, In the Matter of Apple, Inc., FTC File No. 1123108 (Jan. 15, 2014), available at https://www.ftc.gov/sites/default/files/documents/cases/140115applestatementwright_0.pdf. See also Berin Szóka, *Josh Wright's Unfinished Legacy: Reforming FTC Consumer Protection Enforcement*, TRUTH ON THE MARKET (Aug. 26, 2015), <https://truthonthemarket.com/2015/08/26/josh-wrights-unfinished-legacy/>.

⁴⁹UPS, *supra* note 9.

so absurdly low under Section 5(b): “reason to believe that [a violation may have occurred]” and that “it shall appear to the Commission that [an enforcement action] would be to the interest of the public.”⁵⁰ The “preponderance of the evidence” standard is the same standard used in civil cases, simply requiring that civil plaintiffs provide evidence that their argument is “more likely than not” to get judgment against defendants. This standard is substantially less stringent than the “beyond a reasonable doubt” standard used in criminal cases, or the “clear and convincing” standard used in habeas petitions, so it should be suitable for the FTC’s unfairness work.

Why should the FTC have a higher burden (than it does today) at this intermediate stage in its enforcement process, when it brings a complaint? The FTC has significant pre-complaint powers of investigation at its disposal; it will have had considerable opportunity to perform discovery *before* bringing its complaint. Unlike private plaintiffs, who must first survive a *Twombly/Iqbal* motion to dismiss before they can compel discovery, typically at their own expense, the FTC can do so (through its civil investigative demand power)—and impose all of its costs on potential defendants—*before* ever alleging wrongdoing.

As we discuss in more detail below,⁵¹ in order to justify the massive expense of this pre-complaint discovery process, it is not enough that it enables the Commission to engage in fishing expeditions to “uncover” possible violations of the law. Rather, if it is to be justified, and if its use by the Commission is to be kept consistent with its consumer-welfare mission, it must tend to lead to enforcement only when complaints can be justified by the weight of the evidence uncovered. A heightened burden is more likely to ensure this fealty to the consumer interest and to reduce the inefficient imposition of discovery costs on the wrong enforcement targets.

It is also important to note that, although we disagree strongly with their claims,⁵² several FTC Commissioners and commentators have asserted that the set of consent orders entered into by the Commission with various enforcement targets constitute a *de facto* common law: “Technically, consent orders legally function as contracts rather than as binding precedent. Yet, in practice, the orders function much more broadly. . . .”⁵³ In making these claims, proponents, including the Commission’s current Chairwoman,⁵⁴ assert that “the trajectory and development [of FTC enforcement] has followed a predictable set of patterns . . . [that amount to] the functional equivalent of common law.”⁵⁵

For these claims to be true or worthy, it would seem necessary, *at a minimum*, that the Commission’s consumer protection complaints, which are virtually always coupled with consent orders upon their release (because *there is no statutory standard for settling FTC enforcement actions*), be tied to substantive standards that go beyond the mere exercise of three commissioners’ discretion. And yet the FTC and the courts have consistently argued that the FTC Act’s “reason to believe” standard for issuance of complaints requires nothing more than this minimal exercise of discretion. As former Commissioner Tom Rosch put it,

[t]he “reason to believe” standard, however, is not a summary judgment standard: it is a standard that simply asks whether there is a reason to believe that litigation may lead to a finding of liability. That is a low threshold. . . . [T]he

⁵⁰ 15 U.S.C. § 45(b).

⁵¹ See *infra* at 31.

⁵² See, e.g., Berin Szóka, *Indictments Do Not a Common Law Make: A Critical Look at the FTC’s Consumer Protection “Case Law,”* (2014 TPRC Conference Paper, Jul. 15, 2014), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2418572; Geoffrey A. Manne & Ben Sperry, *FTC Process and the Misguided Notion of an FTC “Common Law” of Data Security*, available at <http://masonlec.org/site/rte/uploads/files/manne%20%26%20sperry%20-%20ftc%20common%20law%20conference%20paper.pdf>.

⁵³ Daniel J. Solove & Woodrow Hartzog, *The FTC and the New Common Law of Privacy*, 114 COLUM. L. REV. 583, 607 (2014).

⁵⁴ Address by FTC Chairwoman Edith Ramirez, at 6, at the Competition Law Center at George Washington University School of Law (Aug. 13, 2015), available at https://www.ftc.gov/system/files/documents/public_statements/735411/150813section5speech.pdf (“As I have emphasized, I favor a common law approach to the development of Section 5 doctrine.”). The previous chairwoman held the same view. See Commissioner Julie Brill, *Privacy, Consumer Protection, and Competition*, speech given at 12th Annual Loyola Antitrust Colloquium (Apr. 27, 2012), available at http://www.ftc.gov/sites/default/files/documents/public_statements/privacy-consumer-protection-andcompetition/120427loyolasymposium.pdf (“Yet our privacy cases are also more generally informative about data collection and use practices that are acceptable, and those that cross the line, under Section 5 of the Federal Trade Commission Act creating what some have referred to as a common law of privacy in this country.”).

⁵⁵ Solove & Hartzog, *supra* note 53, at 608.

“reason to believe” standard is amorphous and can have an “I know it when I see it” feel.”⁵⁶

This creates a real problem for the claims that the Commission’s consent orders have any kind of precedential power:

In theory, the questions of whether to bring an enforcement action and whether a violation occurred are distinct; but in practice, when enforcement actions end in settlements (and when the two are often filed simultaneously), the two questions collapse into one. The FTC Act does not impose any additional requirement on the FTC to negotiate a settlement. . . . Thus, at best, the FTC’s decisions are roughly analogous not to court decisions on the merits, but to court decisions on motions to dismiss. . . . Or, perhaps even more precisely, the FTC’s decisions are analogous to reviews of warrants in criminal cases, as Commissioner Rosch has argued. It would be a strange criminal common law, indeed, that confused ultimate standards of guilt with the far lower standard of whether the police could properly open an investigation, yet this is essentially what the FTC’s “common law” of settlements does.⁵⁷

The incentives, discussed in more detail below,⁵⁸ that impel nearly every FTC consumer protection enforcement target to settle with the agency ensure that the only practical inflection point at which the entire enforcement process is subject to any kind of “review,” is when the Commissioners vote to authorize the issuance of a formal complaint and, simultaneously, approve an already-negotiated settlement. That such a determination may be based solely on the effectively unreviewable⁵⁹ discretion of the Commission that the complaint—not the consent order—meets the current, low threshold is troubling.

As former FTC Chairman Tim Muris observed, “Within very broad limits, the agency determines what shall be legal. Indeed, the agency has been ‘lawless’ in the sense that it has traditionally been beyond judicial control.”⁶⁰ If meaningful judicial review is ever to be brought to bear on the final agency decisions embodied in consent orders, it is crucial that the complaints that give rise to those settlements be subject to a more meaningful standard that imposes some evidentiary and logical burden on the Commission beyond the mere exercise of its discretion. While a preponderance of the evidence standard would hardly impose an insurmountable burden on the agency, it would at least impose a standard that is more than purely discretionary, and thus reviewable by courts and subject to recognizable standards upon which such review could proceed. Most importantly, enacting such a standard should, on the margin, embolden defendants to resist settling cases, thus producing more judicial decisions, which could in turn constrain the FTC’s discretion.

None of our proposed reforms to the FTC’s investigation process⁶¹ would in any way undermine the FTC’s ability to gather information prior to issuing a complaint. The FTC would still be able to contact parties and investigate them through its 6(b) powers and use civil investigative demands if necessary to compel disclosure. But it is necessary to heighten the FTC’s standard for finally bringing a complaint since it can do significant investigation beforehand. It is not unreasonable to think they should have enough evidence to determine a violation of the law by a preponderance of the evidence by the point of complaint, especially since this is where most enforcement actions end in settlement.

Deception & Materiality

No Bill Proposed

The FTC’s 1983 Deception Policy Statement forms one of the two pillars of its consumer protection work. As with Unfairness, the purpose of the Deception power is to protect consumers from injury. But unlike Unfairness, Deception does not require the FTC to prove injury. Instead, the FTC need prove only materiality—as an evidentiary proxy for injury:

⁵⁶ J. Thomas Rosch, Commissioner, Fed. Trade Comm’n, *Remarks at the American Bar Association Annual Meeting*, 3–4 (Aug. 5, 2010), available at https://www.ftc.gov/sites/default/files/documents/public_statements/so-i-serve-both-prosecutor-and-judge-whats-big-deal/100805abaspeech.pdf.

⁵⁷ Berin Szoka, *Indictments Do Not a Common Law Make: A Critical Look at the FTC’s Consumer Protection “Case Law”* 7–8, available at http://masonlec.org/site/rte_uploads/files/Szoka%20for%20GMU%20FTC%20Workshop%20%20May%202014.pdf.

⁵⁸ See *infra* at 31.

⁵⁹ See *FTC v. Standard Oil Co. of Cal.*, 449 U.S. 232 (1980).

⁶⁰ Muris, *supra* note 8, at 49.

⁶¹ See *infra* at 31.

[T]he representation, omission, or practice must be a “material” one. The basic question is whether the act or practice is likely to affect the consumer’s conduct or decision with regard to a product or service. If so, the practice is material, and consumer injury is likely, because consumers are likely to have chosen differently but for the deception. *In many instances, materiality, and hence injury, can be presumed from the nature of the practice. In other instances, evidence of materiality may be necessary.* Thus, the Commission will find deception if there is a representation, omission or practice that is likely to mislead the consumer acting reasonably in the circumstances, to the consumer’s detriment. . . .⁶²

A finding of materiality is also a finding that injury is likely to exist because of the representation, omission, sales practice, or marketing technique. Injury to consumers can take many forms. *Injury exists if consumers would have chosen differently but for the deception. If different choices are likely, the claim is material, and injury is likely as well. Thus, injury and materiality are different names for the same concept.*⁶³

Materiality is the *point* of the Deception Policy Statement. It is a shortcut by which the FTC can protect consumers from injury (*i.e.*, not getting the benefit of the bargain promised them) without having to establish injury (that failing to get this benefit actually harms them). A finding of materiality allows the FTC to presume injury because, in the traditional marketing context, a deceptive claim that is “material” enough to alter consumer behavior (which is the *point* of marketing, after all) may reasonably be presumed to do so in ways that a truthful claim wouldn’t (or else why bother making the misleading claim?).

Unfortunately, the FTC has effectively broken the logic of the materiality “short-cut” by extending a *second* set of presumptions: most notably, that all express statements are material. This presumption may make sense in the context of traditional marketing claims, but it breaks down with things like privacy policies and other non-marketing claims (like online help pages)—situations where deceptive statements certainly *may* alter consumer behavior, but in which such an effect can’t be presumed (because the company making the claim is not doing so in order to convince consumers to purchase the product).⁶⁴

The FTC has justified this presumption-on-top-of-a-presumption by pointing to this passage of the DPS (shown with the critical footnotes):

The Commission considers certain categories of information presumptively material.⁴⁷ First, the Commission presumes that express claims are material.⁴⁸ As the Supreme Court stated recently [in *Central Hudson Gas & Electric Co. v. PSC*], “[i]n the absence of factors that would distort the decision to advertise, we may assume that the willingness of a business to promote its products reflects a belief that consumers are interested in the advertising.”

⁴⁷The Commission will always consider relevant and competent evidence offered to rebut presumptions of materiality.

⁴⁸Because this presumption is absent for some implied claims, the Commission will take special caution to ensure materiality exists in such cases.⁶⁵

In effect, the first two sentences have come to swallow the rest of the paragraph, including the logic of the Supreme Court’s decision in *Central Hudson*, the single most important case of all time regarding the regulation of commercial speech.⁶⁶ In particular, the FTC ignores the “absence of factors that would distort the decision to advertise.”⁶⁷

When the Deception Policy Statement talked about “express claims,” it was obviously contemplating *marketing* claims, where the presumption of materiality makes sense: if a company buys an ad, anything it says in the ad is intended to convince the viewer to buy the product. The intention to advertise the product is simply the flipside of materiality—a way of inferring what reasonable buyers would think from

⁶²DPS *supra* note 10.

⁶³*Id.* at 6 (emphasis added).

⁶⁴Of course, even in the marketing context this presumption is one of administrative economy, not descriptive reality. While there is surely a correlation between statements intended to change consumer behavior and actual changes in consumer behavior, a causal assumption is not warranted. See generally Geoffrey A. Manne & E. Marcellus Williamson, *Hot Docs vs. Cold Economics: The Use and Misuse of Business Documents in Antitrust Enforcement and Adjudication*, 47 ARIZ. L. REV. 609 (2005).

⁶⁵*Id.* at 5.

⁶⁶Cent. Hudson Gas & Elec. Corp. v. Pub. Serv. Comm’n of NY, 447 U.S. 557 (1980).

⁶⁷*Id.* at 567–68.

what profit-maximizing sellers obviously intended. But this logic breaks down once we move beyond advertising claims.

We have written at length about this problem in the context of the FTC's 2015 settlement with Nomi, the maker of a technology that allowed stores to track users' movement on their premises, as well as a shopper's repeat visits, in order to deliver a better in-store shopping experience, placement of products, etc.⁶⁸

The FTC's complaint focused on a claim made in the privacy policy on Nomi's website that consumers could opt out on the website or at "any retailer using Nomi's technology." Nomi failed to provide an in-store mechanism for allowing consumers to opt out of the tracking program, but it did provide one on the website—right where the allegedly deceptive claim was made. That Nomi did not, in fact, offer an in-store opt-out mechanism in violation of its express promise to do so is clear. Whether, taken in context, that failure was *material*, however, is not clear.

For the FTC majority, even though the website portion of the promise was fulfilled, Nomi's failure to comply with the in-store portion amounted to an actionable deception. But the majority dodged the key question: whether the evidence that Nomi accurately promised a website opt-out, and that consumers could (and did) opt-out using the website, rebuts the presumption that the inaccurate, in-store opt-out portion of the statement was material, and sufficient to render the statement *as a whole* deceptive.

In other words, the majority assumed that Nomi's express claim, in the context of a privacy policy rather than a marketing statement, affected consumers' behavior. But given the very different purposes of a privacy policy and a marketing statement (and the immediate availability of the website opt-out in the very place that the claim was made), that presumption seems inappropriate. The majority did not discuss the reasonableness of the presumption given the different contexts, which *should* have been the primary issue. Instead it simply relied on a literal reading of the DPS, neglecting to consider whether its underlying logic merited a different approach.

The Commission failed to demonstrate that, *as a whole*, Nomi's failure to provide in-store opt out was deceptive, in clear contravention of the Deception Policy Statement's requirement that all statements be evaluated in context:

[T]he Commission will evaluate the entire advertisement, transaction, or course of dealing in determining how reasonable consumers are likely to respond. Thus, in advertising the Commission will examine "the entire mosaic, rather than each tile separately."⁶⁹

Moreover, despite the promise in the DPS that the Commission would "always consider relevant and competent evidence offered to rebut presumptions of materiality," the FTC failed to do so in *Nomi*. As Commissioner Wright noted in his dissent:

[T]he Commission failed to discharge its commitment to duly consider relevant and competent evidence that squarely rebuts the presumption that Nomi's failure to implement an additional, retail-level opt out was material to consumers. In other words, the Commission neglects to take into account evidence demonstrating consumers would not "have chosen differently" but for the allegedly deceptive representation.

Nomi represented that consumers could opt out on its website as well as in the store where the Listen service was being utilized. Nomi did offer a fully functional and operational global opt out from the Listen service on its website. Thus, the only remaining potential issue is whether Nomi's failure to offer the represented in-store opt out renders the statement in its privacy policy deceptive. The evidence strongly implies that specific representation was not material and therefore not deceptive. Nomi's "tracking" of users was widely publicized in a story that appeared on the front page of *The New York Times*, a publication with a daily reach of nearly 1.9 million readers. Most likely due to this publicity, Nomi's website received 3,840 unique visitors during the relevant time-frame and received 146 opt outs—an opt-out rate of 3.8 percent of site visitors. This opt-out rate is significantly higher than the opt-out rate for other online activities. This high rate, relative to website visitors, likely reflects the ease of

⁶⁸ See Geoffrey A. Manne, R. Ben Sperry & Berin Szóka, *In the Matter of Nomi Technologies, Inc.: The Dark Side of the FTC's Latest Feel-Good Case* (ICLE Antitrust & Consumer Protection Research Program White Paper 2015-1), available at http://laweconcenter.org/images/articles/icle-nomi_white_paper.pdf.

⁶⁹ *DPS supra* note 10, at 4 n.31 (quoting *Fed. Trade Comm'n v. Sterling Drug*, 317 F.2d 669, 674 (2d Cir. 1963)).

a mechanism that was immediately and quickly available to consumers at the time they may have been reading the privacy policy.

The Commission's reliance upon a presumption of materiality as to the additional representation of the availability of an in-store opt out is dubious in light of evidence of the opt-out rate for the webpage mechanism. Actual evidence of consumer behavior indicates that consumers that were interested in opting out of the Listen service took their first opportunity to do so. To presume the materiality of a representation in a privacy policy concerning the availability of an additional, in-store opt-out mechanism requires one to accept the proposition that the privacy-sensitive consumer would be more likely to bypass the easier and immediate route (the online opt out) in favor of waiting until she had the opportunity to opt out in a physical location. Here, we can easily dispense with shortcut presumptions meant to aid the analysis of consumer harm rather than substitute for it. The data allow us to know with an acceptable level of precision how many consumers—3.8 percent of them—reached the privacy policy, read it, and made the decision to opt out when presented with that immediate choice. The Commission's complaint instead adopts an approach that places legal form over substance, is inconsistent with the available data, and defies common sense.⁷⁰

The First Circuit's recent opinion in *Fanning v. FTC* compounds the FTC's error. First, it holds (we believe erroneously) that the DPS's presumptions aren't limited to the marketing milieu:

There is no requirement that a misrepresentation be contained in an advertisement. The FTC Act prohibits 'deceptive acts or practices,' and we have upheld the Commission when it imposed liability based on misstatements not contained in advertisements.⁷¹

In addition, the *Fanning* decision would allow the FTC to go even a step further. Citing the language from the Deception Policy Statement that "claims pertaining to a central characteristic of the product about 'which reasonable consumers would be concerned,'" are material, the First Circuit shifted the burden of proof to *Fanning* to prove that its promises were *not* material.

Of course, the DPS strongly suggests that this "central characteristic" language is also applicable only in the marketing context—in the context, that is, of claims made about a product's "central characteristics" in the service of *selling* that product—and that it is fact-dependent:

Depending on the facts, information pertaining to the central characteristics of the product or service will be presumed material. Information has been found material where it concerns the purpose, safety, efficacy, or cost, of the product or service. Information is also likely to be material if it concerns durability, performance, warranties or quality.⁷²

Much like *Nomi*, the effect of the First Circuit's decision could be far-reaching. If the FTC may simply assert that claims relate to the central characteristic of a product, receive a presumption of materiality on that basis, and then shift the burden the defendant to adduce evidence to the contrary, it may *never* need to offer any evidence of its own on materiality. Combined this with the reluctance of the FTC to actually consider evidence rebutting the presumption (as illustrated in *Nomi*), we could see cases where the FTC presumes materiality on the basis of mere allegation and ignores all evidence to the contrary offered in rebuttal, despite its promise to "always consider relevant and competent evidence offered to rebut presumptions of materiality."⁷³ This would lead to an outcome that the drafters of the Deception Policy Statement plainly did not intend: that effectively every erroneous or inaccurate word ever publicly disseminated by companies may be presumed to injure consumers and constitute an actionable violation of Section 5.

In short, if the courts will defer to the FTC even as it reads the materiality requirement out of the Deception Policy Statement, this is not a vindication of the

⁷⁰Dissenting Statement of Commissioner Joshua D. Wright, In the Matter of Nomi Technologies, Inc., at 3–4 (Apr. 23, 2015) (emphasis added), available at https://www.ftc.gov/system/files/documents/public_statements/638371/150423nomiwrightstatement.pdf.

⁷¹*Fanning v. Fed. Trade Comm'n*, No. 15–1520, slip op. at 13 (May 9, 2016), available at <https://www.ftc.gov/system/files/documents/cases/051816jerkopinon.pdf> (citing *Sunshine Art Studios, Inc. v. FTC*, 481 F.2d 1171, 1173–74 (1st Cir. 1973) (finding FTC Act violation based on company's practice of sending customers excess merchandise and using "a fictitious collection agency to coerce payment").

⁷²*DPS supra* note 10, at 5.

⁷³*Id.* at n.47.

FTC's reading; it is merely a reminder of the vastness of the deference paid to agencies in interpreting ambiguous statutes. And it should be a reminder to Congress that only through legislation can Congress ultimately reassert itself—if only to keep the FTC on the path the agency itself laid out decades ago.

Recommendation: Codify the 1983 Deception Policy Statement

Congress should codify the Deception Policy Statement in a new Section 5(o), just as it codified the core part of the Unfairness Policy Statement in 1994, and just as the SURE Act would codify the rest of the UPS today. Fully codifying both statements (all *three* statements, including the UMC Enforcement Policy Statement) is a good idea if only because the FTC is somewhat more likely to take them seriously if they are statutory mandates. But, as we have emphasized, codification alone will not do much to change the institutional structures and processes that are at the heart of the statements' relative ineffectiveness in guiding the FTC's discretion.

In codifying the DPS, Congress should be mindful of the problems we discuss above. It should also modify the DPS' operative language to mitigate the interpretative problems arising from its inevitable ambiguity. Without specifying precise language here, a few guidelines for drafting such language come readily to mind:

1. Defer to the DPS drafters: they could never have meant for the exceptions (presumptions) to subsume the rule (the materiality requirement), and the codified language should endeavor to reflect this.
2. Acknowledge that there are differences between marketing language and language used in other contexts, including, importantly, today's ubiquitous privacy policies and website terms of use—settings that weren't contemplated by the DPS drafters.
3. Clarify what evidentiary burden is required to demonstrate materiality in contexts where it shouldn't simply be inferred, and, after *Fanning*, clarify whether, and when, the burden should shift from the FTC to defendants.

Recommendation: Clarify that Legally Required Statements Cannot Be Presumptively Material

Particularly given the increasing importance of privacy policies in the FTC's deception enforcement practice, it is also important to clarify whether legally mandated language should be presumed material. We believe that the DPS' exception for "factors that would distort the decision to advertise" includes a legal mandate to say something, which unequivocally "distorts" the decision to proffer such language. Thus, in most cases, privacy policies—required by California law⁷⁴—ought not be treated as presumptively material. This would not preclude the FTC from proving that they *are* material, of course. It would simply require the Commission to *establish* their materiality in each particular case—which, again, was the point of the Deception Policy Statement in the first place.

Recommendation: Delegate Reconsideration of Other Materiality Presumptions

Unfortunately, it will be difficult for Congress to address the other aspects of the FTC's interpretation of materiality by statute, because each is highly fact-specific. But, ultimately, ensuring that the FTC's implementation of the Deception Policy Statement's requirement of a rigorous assessment of trade-offs doesn't require specification of outcomes; it requires some institutional rejiggering ensure that the Bureau of Consumer Protection is motivated to do so by some combination of the courts, the commissioners, and the Bureau of Economics.

Instead of trying to address these issues directly, Congress could, for example, direct the FTC to produce a Policy Statement on Materiality in which the Commission attempts to clarify these issues on its own. Thus, for example, the Commission could describe factors for determining whether and when an online help center should be considered a form of marketing that merits the presumption. Or, as we have previously proposed, Congress could delegate this and other key doctrinal questions to a Modernization Commission focused on high-tech consumer protection issues like privacy and data security, parallel to the Antitrust Modernization Commission.⁷⁵

⁷⁴ See CAL. BUS. & PROF. §22575, available at <http://www.leginfo.ca.gov/cgi-bin/displaycode?section=bpc&group=22001-23000&file=22575-22579>.

⁷⁵ Comments of TechFreedom & International Center for Law and Economics, In the Matter of Big Data and Consumer Privacy in the Internet Economy, Docket No. 140514424-4424-01, at 4 (Aug. 5, 2014), available at http://www.laweconcenter.org/images/articles/tf-icle_ntia_big_data_comments.pdf ("A Privacy Law Modernization Commission could do what Commerce on its own cannot, and what the FTC could probably do but has refused to do: carefully study where new legislation is needed and how best to write it. It can also do what no Executive or independent agency can: establish a consensus among a diverse array of experts that can be

Recommendation: Require Preponderance of the Evidence in Deception Cases

Above, we explain that among our top three priorities for additional reforms—indeed, for reforms overall—is adding a “preponderance of the evidence” standard for unfairness cases by expanding upon Section 5(n).⁷⁶ We urge Congress to include the same standard in a new Section 5(o) for non-fraud deception cases. Again, this standard should be easy for the FTC to satisfy.

Unfair Methods of Competition

No Bill Proposed

The Commission’s unanimous adoption last year of a “Statement of Enforcement Principles Regarding ‘Unfair Methods of Competition’” was a watershed moment for the agency.⁷⁷ The adoption of the Statement marked the first time in the Commission’s 100-year history that the FTC issued enforcement guidelines for cases brought under the Unfair Methods of Competition (“UMC”) provisions of Section 5 of the FTC Act.⁷⁸

Enforcement principles for UMC actions were in desperate need of clarification at the time of the Statement’s adoption. Without any UMC standards, the FTC had been essentially completely free to leverage its costly adjudication process into settlements (or short-term victories), and to leave businesses in the dark as to what sorts of conduct might trigger enforcement. Through a series of unadjudicated settlements, UMC unfairness doctrine (such as it is) has remained largely within the province of FTC discretion and without judicial oversight. As a result, and either by design or by accident, UMC never developed a body of law encompassing well-defined goals or principles like antitrust’s consumer-welfare standard. Several important cases had seemingly sought to take advantage of the absence of meaningful judicial constraints on UMC enforcement actions to bring standard antitrust cases under the provision.⁷⁹ And more than one recent Commissioner had explicitly extolled the virtue of the unfettered (and unprincipled) enforcement of antitrust cases the provision afforded the agency.⁸⁰ The new Statement makes it official FTC policy to reject this harmful dynamic.

The UMC Statement is deceptively simple in its framing:

In deciding whether to challenge an act or practice as an unfair method of competition in violation of Section 5 on a standalone basis, the Commission adheres to the following principles:

- the Commission will be guided by the public policy underlying the antitrust laws, namely, the promotion of consumer welfare;
- the act or practice will be evaluated under a framework similar to the rule of reason, that is, an act or practice challenged by the Commission must cause, or be likely to cause, harm to competition or the competitive process, taking into account any associated cognizable efficiencies and business justifications; and
- the Commission is less likely to challenge an act or practice as an unfair method of competition on a standalone basis if enforcement of the Sherman or Clay-

presented to Congress as, not merely yet another in a series of failed proposals, but one that has a unique degree of analytical rigor behind it and bipartisan endorsement. If any significant reform is ever going to be enacted by Congress, it is most likely to come as the result of such a commission’s recommendations.”).

⁷⁶See *supra* note 18.

⁷⁷Fed. Trade Comm’n, Statement of Enforcement Principles Regarding “Unfair Methods of Competition” Under Section 5 of the FTC Act (Aug. 13, 2015), available at https://www.ftc.gov/system/files/documents/public_statements/735201/150813section5enforcement.pdf.

⁷⁸It should be noted that the Statement represents a landmark victory for Commissioner Joshua Wright, who has been a tireless advocate for defining the scope of the Commission’s UMC authority since before his appointment to the FTC in 2013. See, e.g., Joshua D. Wright, *Abandoning Antitrust’s Chicago Obsession: The Case for Evidence-Based Antitrust*, 78 ANTITRUST L. J. 241 (2012).

⁷⁹For a succinct evaluation of these cases (including, e.g., *Intel* and *N-Data*), see Geoffrey A. Manne & Berin Szóka, *Section 5 of the FTC Act and monopolization cases: A brief primer*, TRUTH ON THE MARKET (Nov. 26, 2012), <https://truthonthemarket.com/2012/11/26/section-5-of-the-ftc-act-and-monopolization-cases-a-brief-primer/>.

⁸⁰See, e.g., Statement of Chairman Leibowitz and Commissioner Rosch, In the Matter of Intel Corp., Docket No. 9341, 1, available at https://www.ftc.gov/system/files/documents/public_statements/568601/091216intelchairstatement.pdf (“[I]t is more important than ever that the Commission actively consider whether it may be appropriate to exercise its full Congressional authority under Section 5.”).

ton Act is sufficient to address the competitive harm arising from the act or practice.⁸¹

Most importantly, the Statement espouses a preference for enforcement under the antitrust laws over UMC when both might apply, and brings the weight of consumer-welfare-oriented antitrust law and economics to bear on such cases.

Recommendation: Codify the Statement of Enforcement Principles Regarding “Unfair Methods of Competition” Under a New Section 5(p) of the FTC Act

As beneficial as the Statement is, it necessarily reflects compromise. In particular, the third prong is expressed merely as a *preference* for antitrust enforcement rather than an obligation. And, of course, such statements are not binding on the Commission, no matter how strongly worded they may be, and no matter how much “soft law” may be brought to bear on the Commissioners charged with following it.

For these reasons, Congress should codify the most important aspects of the Statement—much as it did with the Unfairness Policy Statement’s consumer-injury unfairness test—by adding the following language in a new Section 5(p):

The Commission *shall not* challenge an act or practice as an unfair method of competition on a standalone basis if the alleged competitive harm arising from the act or practice is subject to enforcement under the Sherman or Clayton Act.

An act or practice challenged by the Commission as an unfair method of competition must cause, or be likely to cause, harm to competition or the competitive process, taking into account any associated cognizable efficiencies and business justifications.

This language is taken directly from the UMC Statement, with the small tweak highlighted above *requiring* application of the antitrust laws instead of UMC in appropriate cases, rather than merely expressing a preference for doing so.

Such language would harmonize enforcement of all anticompetitive practices under the antitrust laws’ consumer-welfare standard, while still permitting the few cases not amenable to Sherman or Clayton Act jurisdiction (*e.g.*, invitations to collude) to be brought by the Commission. Importantly, language such as this, which would make enforcement under the antitrust laws *obligatory* where both UMC and antitrust could apply, would transform the Statement’s expression of agency preference into an enforceable statutory requirement.

Enforcement & Guidance

The FTC is commonly labeled a “law enforcement agency,” but in reality it is an administrative agency that regulates primarily through enforcement rather than rulemaking:

As an administrative agency, the FTC’s primary form of regulation involves administrative application of a set of general principles—a “law enforcement” style function that, practically speaking, operates as administrative regulation. . . .⁸²

This administrative enforcement model puts significant emphasis on the agency’s investigative power, and it is the investigatory aspect of its enforcement process that has become the agency’s most powerful—and least overseen—tool. As one commentator notes, “[t]he FTC possesses what are probably the broadest investigatory powers of any Federal regulatory agency.”⁸³

The Commission’s investigatory process is also the heart of the mechanism by which the agency largely bypasses judicial oversight:

[Not even] the courts have . . . been a significant factor in deterring FTC investigation. Indeed, the bulk of court cases appear to affirm the agency’s authority to obtain information pursuant to the Federal Trade Commission Act. Thus, any constraints placed upon the FTC’s ability to obtain information must lie elsewhere.⁸⁴

By overly compelling companies to settle enforcement actions when they are little more than investigations, the investigative process inevitably leads, on the margin, to less-well-targeted investigations, increased discovery burdens on (even blameless) potential defendants, inefficiently large compliance expenditures throughout the

⁸¹ Statement of UMC Enforcement Principles, *supra* note 77.

⁸² *Consumer Protection & Competition Regulation in a High-Tech World: Discussing the Future of the Federal Trade Commission*, *supra* note 4, at 12.

⁸³ Stephanie W. Kanwit, 1 Federal Trade Commission § 13:1 at 13–1 (West 2003).

⁸⁴ Darren Bush, *The Incentive and Ability of the Federal Trade Commission to Investigate Real Estate Markets: An Exercise in Political Economy*, 20–21, available at <http://www.antitrustinstitute.org/files/517c.pdf>.

economy, under-experimentation and innovation by firms, doctrinally questionable consent orders, and a relative scarcity of judicial review of Commission enforcement decisions.

More than any other aspect of the FTC Act or the FTC's operations, it is here that reinvigorated congressional oversight is needed. Even Chris Hoofnagle, who has long advocated that the FTC be far more aggressive on privacy and data security, warns, in his new treatise on privacy regulation at the agency, that

the FTC's investigatory power is very broad and is akin to an inquisitorial body. On its own initiative, it can investigate a broad range of businesses without any indication of a predicate offense having occurred.⁸⁵

In competition cases, the entire Commission must vote to authorize CIDs in each matter and also vote to close investigations once compulsory process is issued. But in the consumer protection context, the Commission issues standing orders—"omnibus resolutions" (ORs)—authorizing extremely broad, industry-wide investigations that authorize the subsequent issuance of CIDs with the consent of only a single Commissioner. For instance, there is a standing Commission order authorizing staff to investigate telemarketing fraud cases.⁸⁶ Thus, if staff wants to issue a CID to investigate a specific telemarketer or any of a wide range of companies that may be supporting telemarketers, it need seek approval for the CID from only a single Commissioner. These requests are frequent (to the best of our knowledge amounting to many dozens *per week*), and routinely granted.

The staff's ability to rely upon Omnibus Resolutions in this manner bypasses an important aspect of how the FTC's enforcement approach is structured on paper. The FTC Operating Manual draws a clear line between initial phase investigations (initiated and run by the staff at their own discretion for up to 100 hours in consumer protection cases) and full investigations. The decision to upgrade an investigation can be made by the Bureau Director on delegated authority, but at least this creates some potential for involvement of other Commissioners. It also requires written analysis by the staff⁸⁷—something other Commissioners could ask to see. But most relevant to the immediate discussion is the Commission's policy that

Compulsory procedures are not ordinarily utilized in the initial phase of investigations; therefore, facts and data which cannot be obtained from existing sources must be developed through the use of voluntary procedures.⁸⁸

Relying on ORs, however, the staff may make use of compulsory process even when it would not otherwise be appropriate to do so.

At the same time, the Commission may (if it so chooses) bring its Section 5 cases (those relatively few that don't settle) in its own administrative tribunal, whose decisions are appealed to the Commission itself. Only after the Commission's review (or denial of review) may a party bring its case before an Article III court. Needless to say, this adds an extremely costly layer of administrative process to enforcement, as former Commissioner Wright explains:

[T]he key to understanding the threat of Section 5 is the interaction between its lack of boundaries and the FTC's administrative process advantages. . . . Consider the following empirical observation that demonstrates at the very least that the institutional framework that has evolved around the application of Section 5 cases in administrative adjudication is quite different than that faced by Article III judges in Federal court in the United States. The FTC has voted out a number of complaints in administrative adjudication that have been tried by administrative law judges ("ALJs") in the past nearly twenty years. In each of those cases, after the administrative decision was appealed to the Commission, the Commission ruled in favor of FTC staff. In other words, *in 100 percent of cases where the ALJ ruled in favor of the FTC, the Commission affirmed; and in 100 percent of the cases in which the ALJ ruled against the FTC, the Commission reversed.* By way of contrast, when the antitrust decisions of Federal district court judges are appealed to the Federal courts of appeal, plaintiffs

⁸⁵ HOOFNAGLE, FEDERAL TRADE COMMISSION PRIVACY LAW & POLICY, *supra* note 3, at 102.

⁸⁶ Resolution No. 0123145, "Resolution Directing the Use of Compulsory Process in a Non-public Investigation of Telemarketers, Sellers, Suppliers, and Others" Technically the Telemarketing Resolution expired in April 2016. But it authorizes continuing investigation subject to already-issued CIDs as long as necessary. Although no further CIDs will be issued, the investigation continues.

⁸⁷ Federal Trade Commission, *Operating Manual*, 3.5.1.2 [hereinafter *Operating Manual*].

⁸⁸ *Id.* at 3.2.3.2.

do not come anywhere close to a 100 percent success rate. Indeed, the win rate is much closer to 50 percent.⁸⁹

The net effect of these procedural circumstances is stark. Wright continues:

The combination of institutional and procedural advantages with the vague nature of the Commission's Section 5 authority gives the agency the ability, in some cases, to elicit a settlement even though the conduct in question very likely may not [violate any law or regulation]. This is because firms typically prefer to settle a Section 5 claim rather than going through lengthy and costly administrative litigation in which they are both shooting at a moving target and have the chips stacked against them. Significantly, such settlements also perpetuate the uncertainty that exists as a result of the ambiguity associated with the Commission's [Section 5] authority by *encouraging a process by which the contours of Section 5 are drawn without any meaningful adversarial proceeding or substantive analysis of the Commission's authority.*⁹⁰

Further, the Commission currently enjoys a nearly insurmountable presumption that its omnibus resolutions are proper—a fact that places subjects of investigations at a severe disadvantage when trying to challenge the Commission's often intrusive investigative process.

Whether issued under an Omnibus Resolution or otherwise, the Commission's CIDs allow the agency to impose enormous costs on potential defendants before even a single Commissioner—let alone the entire Commission or a court of law—determines that there is even a “reason to believe” that the party being investigated has violated any law.

The direct costs of compliance with these extremely broad CIDs can be enormous. Unlike discovery requests in private litigation, reimbursement of costs associated with CID compliance is not available, even if a defendant prevails. Among other things, CID recipients will be required to incur the expense of performing electronic and offline searches for copious amounts of information (which may require the hiring of outside vendors), interviewing employees, the business costs of lost employee and management time, and attorneys' fees. Moreover, there may be several CIDs issued to a single company. And, sometimes of greatest importance, in many cases publicly traded companies will be required to disclose receipt of a CID in its SEC filings. This can have significant immediate effects on a company's share price and do lasting damage to its reputation among consumers.

The experience of Wyndham Hotels is illustrative. The company became the first to challenge an FTC data security enforcement action following more than twelve years of FTC data security settlements. Even before it finally had recourse to an Article III court, Wyndham had already incurred enormous costs, as we noted in our amicus brief in support of Wyndham's 2013 motion to dismiss:

Burdensome as settlements can be, *not* settling can be even costlier. Wyndham, for example, has already received 47 document requests in this case and spent \$5 million responding to these requests. The FTC's compulsory investigative discovery process and administrative litigation both consume the most valuable resource of any firm: the time and attention of management and key personnel.⁹¹

And it is difficult for CID recipients to challenge a CID on the basis of cost. As the Commission notes in a ruling denying one such request:

WAM [West Asset Management] has not satisfied its burden of demonstrating compliance with the CID would be unduly burdensome. . . . WAM has not cited, and the Commission is unaware of, any cases to support WAM's minimize-disruption standard. “Thus courts have refused to modify investigative subpoenas unless compliance threatens to unduly disrupt or seriously hinder normal operations of a business.” As in *Texaco* the breadth of the CID is a reflection of the comprehensiveness of the inquiry being undertaken and the magnitude of WAM's business operations.⁹²

⁸⁹ Joshua Wright, *Recalibrating Section 5: A Response to the CPI Symposium*, CPI ANTITRUST CHRONICLE (Nov. 2013 (2)), at 4 (emphasis added), available at https://www.ftc.gov/sites/default/files/documents/public_statements/recalibrating-section-5-response-cpi-symposium/1311section5.pdf.

⁹⁰ *Id.* at 5 (emphasis added).

⁹¹ Amici Curiae Brief Of TechFreedom, International Center for Law and Economics & Consumer Protection Scholars, Fed. Trade Comm'n v. Wyndham Worldwide Corp., No. 2:13-cv-01887 (3d Cir. 2013) at 13.

⁹² Request for Review of Denial of Petition to Limit Civil Investigative Demand, File No. 0723006 (Jul. 2, 2008), available at <https://www.ftc.gov/sites/default/files/documents/peti->

High costs, as long as they don't threaten a company's viability, will be insufficient to quash or even minimize the scope of a CID. But even expenses that don't threaten viability can be extremely large and extremely burdensome. And, of course, broader costs (*e.g.*, on stock price and market reputation) are extremely difficult to measure and unaccounted for in the FTC's assessment of a CID's burden.

It should be noted that, unlike complaints (before adjudication) and consent orders, CIDs are directly reviewed by courts at times. For better or worse, however, courts are prone to give the Commission an extreme degree of deference when reviewing CIDs. "The standard for judging relevancy in an investigatory proceeding is more relaxed than in an adjudicatory one . . . The requested material, therefore, need only be relevant to the investigation—the boundary of which may be defined quite generally."⁹³ Thus, the Commission has "extreme breadth' in conducting . . . investigations."⁹⁴

But high *direct* costs aren't even the most troubling part. The indirect, societal cost of overly broad CIDs is the increased propensity of companies to settle to avoid them. For reasons we also discuss elsewhere, an excessive tendency toward settlements imposes costs throughout the economy. Among other things:

- It reduces the salutary influence of judicial review of agency enforcement actions;
- It reduces the stock of judicial decisions from which companies, courts and the FTC would otherwise receive essential guidance regarding appropriate enforcement theories and the propriety of ambiguous conduct;
- It induces companies that haven't violated the statute to be saddled with remedies nonetheless, and thereby induces other, similarly-situated companies to incur inefficient costs to avoid the same fate;
- It incentivizes the FTC to impose remedies via consent order that a court might not sustain; and
- It may induce companies that would be found by a court not to have violated the statute to admit liability.

These largely hidden, underappreciated effects are, collectively, enormously distorting. And they feedback into the process, reinforcing the institutional dynamics that lead to such outcomes in the first place. In short, the FTC's discovery process greatly magnifies its already vast discretion to make substantive decisions about the evolution of Section 5 doctrine (or quasi-doctrine).

At the same time, there is reason to believe that the rate of CID issuance, and the scope of CIDs issued, are (far) greater than optimal.

In order to issue a CID pursuant to an OR, staff need not present the authorizing Commissioner with a theory of the case or anything approaching "probable cause" for the CID; rather, the OR effectively takes care of that (although without anything like the specificity required of, say, a subpoena), and staff need only assert that the CID is in furtherance of an OR. The other Commissioners do not have an opportunity to vote on the issuance of the CID and would not likely even know about the investigation. Even if dissenting staff members attempt to notify Commissioners,⁹⁵ it may be difficult, at this early stage, for Commissioners to recognize the doctrinal or practical significance of the cases the staff is attempting to bring, and thus to provide any meaningful check upon the discretion of the staff to use the discovery process to coerce settlements.

Thus, because of omnibus resolutions, a great number of investigations—encompassing a great number of costly CIDs—are not presented to the other Commissioners to determine whether the investigation is an appropriate use of the agency's resources or whether the legal basis for the case is sound. In many cases, the other Commissioners may not even see the case until a settlement has been negotiated as a *fait accompli*.

tions-quash/west-asset-management-inc./080702westasset.pdf (citing Fed. Trade Comm'n v. Texaco, Inc., 555 F.2d 862, 882 (D.C. Cir. 1977)).

⁹³ Invention Submission, 965 F.2d at 1090 (emphasis in original, internal citations omitted) (citing Fed. Trade Comm'n v. Carter, 636 F.2d 781, 787–88 (D.C. Cir. 1980), and *Texaco*, 555 F.2d at 874 & n.26).

⁹⁴ *Re: LabMD, Inc.'s Petition to Limit or Quash the Civil Investigative Demand; and Michael J. Daugherty's Petition to Limit or Quash the Civil Investigative Demand* (Apr. 20, 2012), 5, available at <https://www.ftc.gov/sites/default/files/documents/petitions-quash/labmd-inc./102-3099-lab-md-letter-ruling-04202012.pdf>.

⁹⁵ Operating Manual §3.5.1.1 ("Dissenting staff recommendations regarding compulsory process, compliance, consent agreements, proposed trade regulation rules or proposed industrywide investigations should be submitted to the Commission by the originating offices, upon the request of the staff member.").

The bar for issuing CIDs pursuant to an omnibus resolution is extremely low. Nominally the CID request must fall within the agency's authority and be relevant to the investigation that authorizes it. But the FTC has enormous discretion in determining whether a specific compulsory demand is relevant to an investigation, and it need not have "a justifiable belief that wrongdoing has actually occurred."⁹⁶

For example, the Commission's telemarketing resolution authorized compulsory process

[t]o determine whether unnamed telemarketers, sellers, or others assisting them have engaged in or are engaging in: (1) unfair or deceptive acts or practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act; and/or (2) deceptive or abusive telemarketing acts or practices in violation of the Commission's Telemarketing Sales Rule, including but not limited to the provision of substantial assistance or support—such as mailing lists, scripts, merchant accounts, and other information, products, or services—to telemarketers engaged in unlawful practices. The investigation is also to determine whether Commission action to obtain redress for injury to consumers or others would be in the public interest.⁹⁷

Pursuant to this OR, the Commission issued a CID to Western Union. Western Union challenged the CID on the grounds that it was unrelated to the OR (among other things). The FTC, in denying the motion to quash, claimed that "[t]he resolution . . . includes investigations of telemarketers or sellers as well as entities such as Western Union who may be providing substantial assistance or support to telemarketers or sellers." While the OR does mention "assistance or support," it doesn't specify any companies by name and doesn't specify that payment processors provide the sort of support it contemplates. In fact, it is fairly clear from even the impressively broad characterization of these in the OR—"mailing lists, scripts, merchant accounts, and other information, products, or services"—that the ancillary processing of payment transactions by legitimate companies was not really contemplated.

Nevertheless, the standard of review for the relevance of CIDs—in the rare instance that they are challenged at all—is extremely generous to the agency. As the Commission notes in its *Western Union* decision:

In the context of an administrative CID, "relevance" is defined broadly and with deference to an administrative agency's determination. An administrative agency is to be accorded "extreme breadth" in conducting an investigation. As the D.C. Circuit has stated, the standard for judging relevance in an administrative investigation is "more relaxed" than in an adjudicatory proceeding. As a result, the agency is entitled to the documents unless the CID recipient can show that the agency's determination is "obviously wrong" or the documents are "plainly irrelevant" to the investigation's purpose. We find that Western Union has not met this burden.⁹⁸

Finally, administrative challenges to CIDs are public proceedings, which itself presents a substantial bar to their review. Companies subject to investigations by the FTC are, not surprisingly, reluctant to reveal the existence of such an investigation publicly. While the immense breadth and vagueness of the ORs authorizing compulsory process in an investigation, the ease with which CIDs are issued, and the lack of a "belief of wrongdoing" requirement certainly mean that no wrongdoing *should* be inferred from the existence of an investigation or a CID, unfortunately public perception may not track these nuances. In the case of some publicly traded companies, the mere issuance of a CID may require disclosure.⁹⁹ But for other publicly traded companies and for all private companies such disclosure is not required. This means that, for these companies, there is an added deterrent to challenging

⁹⁶ *United States v. Morton Salt Co.*, 338 U.S. 632, 642 (1950).

⁹⁷ *Resolution Directing Use of Compulsory Process in a Nonpublic Investigation of Telemarketers, Sellers, Suppliers, or Others*, File No. 0123145 (Apr. 11, 2011), quoted in *In the Matter of December 12, 2012 Civil Investigative Demand Issue to the Western Union Company*, File No. 012 3145 (Mar. 4, 2013), available at <https://www.ftc.gov/sites/default/files/documents/petitions-quash/unnamed-telemarketers-others/130404westernunionpetition.pdf> (Citations omitted).

⁹⁸ *In the Matter of December 12, 2012 Civil Investigative Demand Issue to the Western Union Company* at 8. (Citing cases).

⁹⁹ See, e.g., Deborah S. Birnbach, *Do You Have to Disclose a Government Investigation?*, HARVARD LAW SCHOOL FORUM ON CORPORATE GOVERNANCE AND FINANCIAL REGULATION (May 21, 2016), <https://corpgov.law.harvard.edu/2016/04/09/do-you-have-to-disclose-a-government-investigation/>.

a CID because doing so will cause it to be disclosed publicly when it otherwise would not be.

The combination of an exceedingly deferential standard of review, the need to exhaust administrative process before the very agency that issued the OR and CID before gaining access to an independent Article III tribunal, the risk of reputational harms, and the massive compliance costs combine to ensure that very few CIDs are ever challenged. This only reinforces FTC staff's incentives to issue CIDs, and to do so with an increasingly tenuous relationship to the Commission-approved resolution authorizing them.

The absence of effective oversight on this process creates a further problem. FTC staff have the power to issue Voluntary Access Letters requesting the same documents as a CID without *any* Commissioner involvement—or even (at least on paper) the possibility that a dissenting staff member can notify a Commissioner of her objections.¹⁰⁰ While these requests are nominally voluntary, the omnipresent threat of compelled discovery means that recipients virtually always comply with these requests, although they do often initiate a discussion between staff and recipients that may result in a narrowing of the requests' scope. Voluntary Access Letters are subject to even less scrutiny than CIDs, and there is virtually no way for any of the FTC's oversight bodies (Congress, the courts, the public, the executive branch, etc.) to monitor their use.

Investigations and Reporting on Investigations

The Clarifying Legality & Enforcement Action Reasoning (CLEAR) Act

While identifying the problems with the Commission's investigation and CID process is fairly straightforward, identifying solutions is not so straightforward. A critical first step, however, would be imposing greater transparency requirements on the Commission's investigation practices.

Rep. Brett Guthrie's (R-KY) proposed CLEAR Act (H.R. 5109)¹⁰¹ would require the FTC to report annually to Congress on the status of its investigations, including the legal analysis supporting the FTC's decision to close some investigations without action. This requirement would not require the Commission to identify its targets, thus preserving the anonymity of the firms in question.

Value of the Bill: Better Reporting of FTC Enforcement Trends

The FTC used to provide somewhat clearer data on the number of enforcement actions it took every year, classifying each by product and "type of matter."¹⁰² The FTC's recent "Annual Highlights" reports do not include even this level of data on its enforcement actions.¹⁰³ But neither includes the basic data required by the CLEAR Act on the number of investigations commenced, closed, settled or litigated. Without hard data on this, it is difficult to assess how the FTC's enforcement approach works, the relationship between the agency's investigations and enforcement actions, and how these has changed over time. While the bill does not specifically mention consent decrees among the items that must be reported to Congress, it does require that the report include "the disposition of such investigations, if such investigations have concluded and resulted in official agency action," which would include consent decrees.

Recommendation: Add Discovery Tools to the Required Reporting

The bill omits, however, one of the most important aspects of the FTC's operations, which is very easily quantifiable: the FTC's use of its various discovery tools. The FTC should, in addition, have to produce aggregate statistics on its use of discovery tools, excluding the specific identity of the target, but including, for example:

- The source of the investigation (e.g., Omnibus Resolution, consumer complaint, etc.);
- The volume of discovery requested;
- The volume of discovery produced;

¹⁰⁰Again, Operating Manual Section 3.3.5.1.1 requires that "[d]issenting staff recommendations . . . be submitted to the Commission by the originating offices, upon the request of the staff member," but does not include voluntary assistance letters in the list of covered subjects, only "compulsory process."

¹⁰¹The Clarifying Legality and Enforcement Action Reasoning Act, H.R. 5109, 114th Cong. (2016) [hereinafter CLEAR Act] available at <https://www.congress.gov/bills/114th-congress/house-bill/5109/text>.

¹⁰²See, e.g., 1995 Annual Report at 49, https://www.ftc.gov/sites/default/files/documents/reports-annual/annual-report-1995/ar1995_0.pdf.

¹⁰³Fed. Trade Comm'n, FTC Annual Reports, <https://www.ftc.gov/policy/reports/policy-reports/ftc-annual-reports>.

- The time elapsed between the initiation of the investigation and the request(s);
- The time elapsed between the request(s) and production;
- Estimated cost of compliance (as volunteered by the target);
- The specific tool(s) used to authorize the investigation and production request(s) (*e.g.*, Omnibus Resolution, CID, Voluntary Access Letter, etc.);
- Who approved the investigation and production request(s) (*e.g.*, a single Commissioner, the full Commission, the Bureau Director, the staff itself, etc.);
- The approximate size (number of employees) and annual revenues of the target business (to measure effects on small businesses); and
- The general nature of the issue(s) connected to the investigation and production request(s).

This reporting could be largely automated from the FTC database used to log investigations, discovery requests and resulting production of documents. And, of course, the FTC should have such a flexible and usable database if it does not already. Once created, it should be relatively easy to make the data public, as it will require little more than obscuring the identity of the target, putting the size of the company in ranges, and ensuring that the metadata identifying the relevant issues is sufficiently high level (*e.g.*, “data security” rather than “PED skimming”).

Value of the Bill: What is Not Prohibited Is a Crucial Form of Guidance

Clarity as to what the law does *not* prohibit may be a more important hallmark of the Evolutionary Model (the *true* common law), than is specificity as to what the law does prohibit.

The FTC used to issue closing letters regularly but stopped providing meaningful guidance at least since the start of this Administration. The FTC Operating Manual already requires staff to produce a memo justifying closure of any investigation that has gone beyond the initial stage, thus requiring the approval of the Bureau Directors to expand into a full investigation, that “summarize[s] the results of the investigation, discuss[es] the methodology used in the investigation, and explain[s] the rationale for the closing.”¹⁰⁴

In other words, the staff already, in theory, does the analysis that would be required by the bill (at least for cases that merit being continued beyond the 100 hours allowed for initial phase consumer protection investigations);¹⁰⁵ they simply do not share it. Thus, at most, the bill would require (i) greater rigor in the memoranda that staff already writes, (ii) that some version of memoranda be included in the annual report, edited to obscure the company’s identity, and (iii) that *some* analysis be written for initial phase cases that may be closed without any internal memoranda. And this last requirement should not be difficult for the staff to satisfy, since cases that did not merit full investigations ought to raise simpler legal issues.

For example, in 2007, the FTC issued a no-action letter closing its investigation into Dollar Tree Stores that offers a fair amount of background on the issue: “PED skimming,” the tampering with of payment card PIN entry devices (PEDs) used at checkout that allowed hackers to steal customers’ card information and thus make fraudulent purchases.¹⁰⁶ The FTC explained its decision to close the Dollar Tree Stores investigation at length, listing the factors considered by the FTC:

the extent to which the risk at issue was reasonable foreseeable at the time of the compromise; the nature and magnitude of the risk relative to other risks; the benefits relative to the costs of protecting against the risk; Dollar Tree’s overall data security practices, the duration and scope of the compromise; the level of consumer injury; and Dollar Tree’s prompt response to the incident.¹⁰⁷

The letter went on to note:

We continue to emphasize that data security is an ongoing process, and that as risks, technologies, and circumstances change over time, companies must adjust their information security programs accordingly. The staff notes that, in recent months, the risk of PED skimming at retail locations has been increasingly identified by security experts and discussed in a variety of public and business contexts. We also understand that some businesses have now taken steps to improve physical security to deter PED skimming, such as locking or

¹⁰⁴ Operating Manual § 3.2.4.1.1 (consumer protection) & § 3.2.4.1.2 (competition)

¹⁰⁵ Operating Manual § 3.2.2.1.

¹⁰⁶ Letter from Joel Winston, Associate Director of Fed. Trade Comm’n to Michael E. Burke, Esq., Counsel to Dollar Tree Stores, Inc. (June 5, 2001) available at http://www.ftc.gov/sites/default/files/documents/closing_letters/dollar-tree-stores-inc./070605doltree.pdf.

¹⁰⁷ *Id.* at 2.

otherwise securing PERs in checkout lanes; installing security cameras or other monitoring devices; performing regular PED inspections to detect tampering, theft, or other misuse; and/or replacing older PEDs with newer tamper-resistant and tamper-evident models. We hope and expect that all businesses using PEDs in their stores will consider implementing these and/or other reasonable and appropriate safeguards to secure their systems.¹⁰⁸

The FTC has issued only one closing letter in standard data security cases since its 2007 letter in *Dollar Tree Stores*—and, apparently, about the same issue. In 2011, the FTC issued a letter closing its investigation of the Michaels art supply store chain.¹⁰⁹ The letter offers essentially no information about the investigation or analysis of the issues involved—in marked contrast to the *Dollar Tree Stores* letter. But based on press reports from 2011, the issue appears to have been the same as in *Dollar Tree Stores*: “crooks [had] tampered with PIN pads in the Michaels checkout lanes, allowing them to capture customers’ debit card and PIN numbers.”¹¹⁰

Once again, the FTC has become increasingly unwilling to constrain its own discretion, even in the issuance of closing letters that do not bar the FTC from taking future enforcement actions. This underscores not only the value of the CLEAR Act, but also of the challenge in getting the FTC to take seriously the bill’s requirement that annual reports include, “for each such investigation that was closed with no official agency action, a description sufficient to indicate the legal analysis supporting the Commission’s decision not to continue such investigation, and the industry sectors of the entities subject to each such investigation.”¹¹¹

Recommendation: Require the Bureau of Economics to Be Involved

Wherever possible, Congress should specify that the Bureau of Economics be involved in the making of important decisions, and in the production of important guidance materials. Absent that instruction, the FTC, especially the Bureau of Consumer Protection, will likely resist fully involving the Bureau of Economics in its processes. The simplest way to make this change is as follows:

For each such investigation that was closed with no official agency action, a description sufficient to indicate the legal *and economic* analysis supporting the Commission’s decision not to continue such investigation, and the industry sectors of the entities subject to each such investigation.

Of course, there will be many cases where the economists have essentially nothing to say. The point is not that each case merits detailed economic analysis. Rather, the recommendation is intended to ensure that, at the very least, the *opportunity* to produce and disseminate a basic economic analysis by the BE is built into the enforcement process.

Moreover, if an economic analysis is deemed appropriate, the determination of what constitutes an appropriate *level* of analysis should be made by the Bureau of Economics alone. For example, in the *Dollar Tree Stores* letter quoted above, it would have been helpful if the letter had provided *some* quantitative analysis as to the factors mentioned in the letter. To illustrate this point, one might ask the following questions about the factors identified in *Dollar Tree Stores*:

- “the extent to which the risk at issue was reasonably foreseeable at the time of the compromise” and “the nature and magnitude of the risk relative to other risks”—*How widely known was the vulnerability generally at that time? How fast was awareness spreading among similarly situated companies? How likely was the vulnerability to occur?*
- “the benefits relative to the costs of protecting against the risk”—*Given the impossibility of completely eradicating risk, how much ex ante “protection” would have been sufficient? Given the ex ante uncertainty of any particular risk occurring, how much would it have cost to mitigate against all such risks, not just the one that actually materialized?*

¹⁰⁸ *Id.*

¹⁰⁹ Letter from Maneesha Mithal, Associate Director of Fed. Trade Comm’n to Lisa J. Sotto, Counsel to Michael’s Stores, Inc. (June 5, 2011) available at http://www.ftc.gov/sites/default/files/documents/closing_letters/michaels-stores-inc./120706michaelsstorescltr.pdf.

¹¹⁰ Elisabeth Leamy, *Debit Card Fraud Investigation Involving Michaels Craft Stores PIN Pads Spreads to 20 U.S. States*, ABC NEWS (May 13, 2011) available at <http://abcnews.go.com/Business/ConsumerNews/debit-card-fraud-michaels-crafts-customers-info-captured/story?id=13593607>.

¹¹¹ CLEAR Act, *supra* note 101.

- “Dollar Tree’s overall data security practices”—*How much did the company spend? How else do its practices compare to its peers? How can good data security be quantified?*
- “the duration and scope of the compromise”—*How long? How many users?*
- “the level of consumer injury”—*Can this be quantified specifically to this case? Or can injury be extrapolated from reliably representative samples of similar injury?*
- “Dollar Tree’s prompt response to the incident”—*Just how prompt was it, in absolute terms? And relative to comparable industry practice?*

Given the general scope of the FTC’s investigations, it likely already collects the kind of data that could allow it to answer some, if not all, of these questions (and others as well). It may even have performed some of the requisite analysis. Why should the Commission’s economists not have a seat at the table in writing the closing analysis? This could be perhaps the greatest opportunity to begin bringing the analytical rigor of law and economics to consumer protection.

Of course, the Commission may be (quite understandably) reluctant to include this data in company-specific closing letters—for the same reasons that investigations are supposed to remain confidential. But therein lies one of the chief virtues of the CLEAR Act: Instead of writing company-specific letters, the FTC could aggregate the information, obscure the identity of the company at issue in each specific case, and thus speak more freely about the details of its situation. Although the tension between the goals of providing analytical clarity and maintaining confidentiality for the subjects of investigation is obvious, it is not an insurmountable conflict, and thus no reason not to require more analysis and disclosure, in principle.

Finally, it is worth noting that if BE is to be competent in its participation in these investigations and the associated reports, it will need a larger staff of economists. Thus, as we discuss below, Congress should devote additional resources to the Commission that are specifically earmarked for hiring additional BE staff.¹¹²

Recommendation: Attempt to Make the FTC Take the Analysis Requirement Seriously

We recommend that Congress emphasize *why* such reporting is important with something like the following language, added either to Congressional findings or made clear in the legislative history around the bill:

- Guidance from the Commission as to what is *not* illegal may be the most important form of guidance the Commission can offer; and
- To be truly useful, such guidance should hew closely the FTC’s applicable Policy Statements.

We further recommend that Congress carefully scrutinize the FTC’s annual reports issued under the CLEAR Act in oral discussions at hearings and in written questions for the record. Indeed, *not* doing so will indicate to the FTC that Congress is not really serious about demanding greater analytical rigor.

Recommendation: Ensure that the Commission Organizes These Reports in a Useful Manner

The legal analysis section of the bill is markedly different from the other three sections. The first two sections require simple counts of investigations commenced and closed with no action. The third section (“disposition of such investigations, if such investigations have concluded and resulted in official agency action”) can be satisfied with a brief sentence for each (or less). But the fourth section requires long-form analysis, which could run many pages for each case.

At a minimum, the FTC should do more than it does today to make it easy to identify which closing letters are relevant. Today, the Commission’s web interface for closing letters is essentially useless. Letters are listed in reverse chronological order with no information provided other than the name, title and corporate affiliation of the person to whom the letter is addressed. There is no metadata to indicate what the letter is about (*e.g.*, privacy, data security, advertising, product design) or what doctrinal issues (*e.g.*, unfairness, deception, material omissions, substantiation) the letter confronts. Key word searches for, say, “privacy” or “data security” produce zero results.

The CLEAR Act offers Congress a chance to demand better of the Commission. Congress should communicate what a *useful* discussion of closing decisions might look like—whether by including specific instructions in legislation, by addressing

¹¹²See *infra* note 123.

the issue in legislative history, or simply (and probably least effectively in the long term) by raising the issue regularly with the FTC at hearings. For instance, the text in the FTC's reports to Congress could be made publicly available in an online database tagged with metadata to make it easier for users to search for and find relevant closing letters.

Ideally, this database would be accessed through the same interface envisioned above for transparency into the FTC's discovery process, and would include the same metadata and search tools. Thus, a user might be able to search for FTC enforcement actions and discovery inquiries regarding, say, data security practices in small businesses, in order to get a better sense of how the FTC operates in that area.

Recommendation: Require the FTC to Synthesize Closing Decisions and Enforcement Decisions into Doctrinal Guidelines

When the FTC submitted the Unfairness Policy Statement to Congress, it noted, in its cover letter:

In response to your inquiry we have therefore undertaken a review of the decided cases and rules and have synthesized from them the most important principles of general applicability. Rather than merely reciting the law, we have attempted to provide the Committee with a concrete indication of the manner in which the Commission has enforced, and will continue to enforce, its unfairness mandate. In so doing we intend to address the concerns that have been raised about the meaning of consumer unfairness, and thereby attempt to provide a greater sense of certainty about what the Commission would regard as an unfair act or practice under Section 5.¹¹³

This synthesis is what the FTC needs to do now—and could get close to doing, in part, through better organized reporting on its closing decisions—only on a more specific level of the component elements of each of its Policy Statements. This is essentially what the various Antitrust Guidelines issued jointly by the DOJ and the FTC's Bureau of Competition do. These are masterpieces of thematic organization. Consider, for example, from the 2000 Antitrust Guidelines for Collaborations Among Competitors, this sample of the table of contents:

- 3.34 Factors Relevant to the Ability and Incentive of the Participants and the Collaboration to Compete
 - 3.34(a) Exclusivity
 - 3.34(b) Control over Assets
 - 3.34(c) Financial Interests in the Collaboration or in Other Participants
 - 3.34(d) Control of the Collaboration's Competitively Significant Decision Making
 - 3.34(e) Likelihood of Anticompetitive Information Sharing
 - 3.34(f) Duration of the Collaboration
- 3.35 Entry
- 3.36 Identifying Procompetitive Benefits of the Collaboration
 - 3.36(a) Cognizable Efficiencies Must Be Verifiable and Potentially Procompetitive
 - 3.36(b) Reasonable Necessity and Less Restrictive Alternatives
- 3.37 Overall Competitive Effect¹¹⁴

The guidelines are rich with examples that illustrate the way the agencies will apply their doctrine. As noted in the introduction, these guidelines are one level down the Doctrinal Pyramid: They explain how the kind of concepts articulated at the high conceptual level of, say, the FTC's UDAP policy statements, can actually be applied to real world circumstances.¹¹⁵

One obvious challenge is that the antitrust guidelines synthesize litigated cases, of which the FTC has precious few on UDAP matters. This makes it difficult, if not impossible, for the FTC to do *precisely* the same thing on UDAP matters as the anti-

¹¹³UPS, *supra* note 9.

¹¹⁴FED. TRADE COMM'N & DEP'T OF JUSTICE, ANTITRUST GUIDELINES FOR COLLABORATIONS AMONG COMPETITORS ii (Apr. 2000), available at https://www.ftc.gov/sites/default/files/documents/public_events/joint-venture-hearings-antitrust-guidelines-collaboration-among-competitors/ftcdojguidelines-2.pdf.

¹¹⁵See *supra* note 12.

trust guidelines do. But that does not mean the FTC could not benefit from writing “lessons learned” retrospectives on its past enforcement efforts and closing letters.

Importantly, publication of these guidelines would not actually be a constraint upon the FTC’s discretion; it would merely require the Commission to better explain the rationale for what it has done in the past, connecting that arc across time. Like policy statements and consent decrees, guidelines are not technically binding upon the agency. Yet, in practice, they would steer the Commission in a far more rigorous way than its vague “common law of consent decrees [or of congressional testimony or blog posts].” It would allow the FTC to build doctrine in an analytically rigorous way as a second-best alternative to judicial decision-making—and, of course, as a supplement to judicial decisions, to the extent they happen.

Recommendation: Ensure that Defendants Can Quash Subpoenas Confidentially

Among the biggest deterrents to litigation today is companies’ reluctance to make public investigations aimed at them. But a company wishing to challenge the FTC’s overly broad investigative demands effectively must accede to public disclosure because the FTC has the discretion to make such fights public.

Specifically, FTC enforcement rules currently allow parties seeking to quash a subpoena to ask for confidential treatment for their motions to quash, but the rules also appear to set public disclosure as the default:

(d) *Public disclosure.* All petitions to limit or quash Commission compulsory process and all Commission orders in response to those petitions shall become part of the public records of the Commission, except for information granted confidential treatment under § 4.9(c) of this chapter.¹¹⁶

The referenced general rule on confidentiality gives the FTC’s General Counsel broad discretion in matters of confidentiality:

(c) *Confidentiality and in camera material.*

(1) Persons submitting material to the Commission described in this section may designate that material or portions of it confidential and request that it be withheld from the public record. All requests for confidential treatment shall be supported by a showing of justification in light of applicable statutes, rules, orders of the Commission or its administrative law judges, orders of the courts, or other relevant authority. *The General Counsel or the General Counsel’s designee will act upon such request with due regard for legal constraints and the public interest.*¹¹⁷

Setting the default to public disclosure for such disputes is flatly inconsistent with the FTC’s general policy of keeping investigations nonpublic:

While investigations are generally nonpublic, Commission staff may disclose the existence of an investigation to potential witnesses or other third parties to the extent necessary to advance the investigation.¹¹⁸

This is the right balance: Commission staff should *sometimes* be able to disclose aspects of an investigation. It should *not* be able to coerce a company into settling, or complying with additional discovery, in order to avoid bad press. Even if a company calculates that bad press is inevitable, if the FTC seems determined to extract a settlement, disclosing the investigation earlier can increase the direct expenses and reputational costs incurred by the company by stretching out the total length of the fight with the Commission for months or years longer.

We propose that the default be switched, so that motions to quash are generally kept under seal except in exceptional circumstances.

¹¹⁶ 16 C.F.R. § 2.10(d).

¹¹⁷ 16 C.F.R. § 4.9(c)(1).

¹¹⁸ 16 C.F.R. § 2.6; *See also* Federal Trade Commission, *Operating Manual*, Section 3.3.1 (To promote orderly investigative procedures and to protect individuals or business entities under investigation from premature adverse publicity, the Commission treats the fact that a particular proposed respondent is under investigation and the documents and information submitted to or developed by staff in connection with the investigation as confidential information that can be released only in the manner and to the extent authorized by law and by the Commission. In general, even if a proposed respondent in a nonpublic investigation makes a public disclosure that an investigation is being conducted, Commission personnel may not acknowledge the existence of the investigation, or discuss its purpose and scope or the nature of the suspected violation.)

Economic Analysis of Investigations, Complaints, and Consent Decrees

No Bill Proposed

The Federal Trade Commission's Bureau of Economics' (BE) role as an independent and expert analyst is one of the most critical features of the FTC's organizational structure in terms of enhancing its performance, expanding its substantive capabilities, and increasing the critical reputational capital the agency has available to promote its missions.¹¹⁹

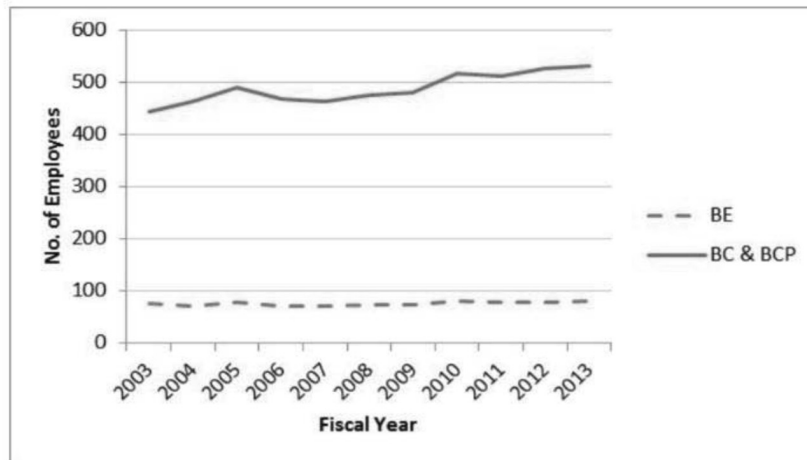
Former FTC Commissioner Joshua Wright, 2015

Commissioner Wright wrote as a veteran of both the Bureau of Economics and the Bureau of Competition. He was only the fourth economist to serve as FTC Commissioner (following Jim Miller, George Douglas and Dennis Yao) and the first JD/PhD. His 2015 speech, "On the FTC's Bureau of Economics, Independence, and Agency Performance," marked the beginning of an effort to bolster the role of the Bureau of Economics in the FTC's decision-making, especially in consumer protection matters. Wright warned, pointedly, that the FTC has "too many lawyers, too few economists," calling this "a potential threat to independence and agency performance."¹²⁰

Unfortunately, this was only a beginning: shortly after delivering this speech, Wright resigned from the Commission to return to teaching law and economics. For now, at least, the task of bolstering economic analysis at the Commission falls to Congress.

The RECS Act's proposal that BE be involved in any recommendation for new legislation or regulatory action is an important step towards this goal, but it is too narrow.¹²¹ It does not address the need to bolster the FTC's role in the institutional structure of the agency, or its role in enforcement decisions. The following chart (from Wright's speech) ably captures the first of these problems:

NUMBER OF ATTORNEYS TO ECONOMISTS AT THE FTC FROM 2003 TO 2013¹²²

*Recommendation: Hire More Economists*

Wright recommends:

Hiring more full-time economists is one obvious fix to the ratio problem. There are many benefits to expanding the economic capabilities of the agency. Many cases simply cannot be adequately staffed with one or two staff economists. *Doubling the current size of BE* would be a good start towards aligning the in-

¹¹⁹ Statement of Commissioner Joshua D. Wright, On the FTC's Bureau of Economics, Independence, and Agency Performance, at 1 (Aug. 6, 2015), available at https://www.ftc.gov/system/files/documents/public_statements/695241/150806bestmtwright.pdf.

¹²⁰ *Id.* at 5.

¹²¹ See *infra* at 54.

¹²² Statement of Commissioner Joshua D. Wright, On the FTC's Bureau of Economics, Independence, and Agency Performance, *supra* note 119, at 6.

Doubling the current size of BE would be a good start towards aligning the incentives of the Commission and BE staff with respect to case recommendations. While too quickly increasing the size of BE staff might dilute quality, a gradual increase in staffing coupled with a pay increase and a commitment to research time should help to keep quality levels at least constant.¹²³

We wholeheartedly endorse former Commissioner Wright's recommendation.

Recommendation: Require BE to Comment Separately on Complaints and Consent Orders

In the case of complaints and consent orders issued by the Commission, we recommend that Congress require the Commission to amend its Rules of Practice to require that the Bureau of Economics provide a *separate* economic assessment of the complaint or consent order in conjunction with each. This proposal is consistent with former Commissioner Wright's similar recommendation:

I suggest the FTC consider interpreting or amending FTC Rule of Practice 2.34 to mandate that BE publish, in matters involving consent decrees, and as part of the already required "explanation of the provisions of the order and the relief to be obtained," a separate explanation of the economic analysis of the Commission's action. The documents associated with this rule are critical for communicating the role that economic analysis plays in Commission decision-making in cases. In many cases, public facing documents surrounding consents in competition cases simply do not describe well or at all the economic analysis conducted by staff or upon which BE recommended the consent.¹²⁴

In order to perform its desired function, this "separate explanation" would be authored and issued by the Bureau of Economics, and not subject to approval by the Commission. The document would express BE's independent assessment (approval or rejection) of the Commission's proposed complaint or consent order, provide a high-level description of the specific economic analyses and evidence relied upon in its own recommendation or rejection of the proposed consent order, and offer a more general economic rationale for its recommendation.

Requiring BE to make public its economic rationale for supporting or rejecting a complaint or consent decree voted out by the Commission would offer a number of benefits. In general, such an analysis would both inform the public and demand rigor of the Commission. As former Commissioner Wright noted,

First, it offers BE a public avenue to communicate its findings to the public. Second, it reinforces the independent nature of the recommendation that BE offers. Third, it breaks the agency monopoly the FTC lawyers currently enjoy in terms of framing a particular matter to the public. The internal leverage BE gains by the ability to publish such a document . . . will also provide BE a greater role in the consent process and a mechanism to discipline consents that are not supported by sound economics . . ., minimizing the "compromise" recommendation that is most problematic in matters involving consent decrees.¹²⁵

Wright explains this "compromise recommendation" problem in detail that bears extensive quotation and emphasis here:

Both BC attorneys and BE staff are responsible for producing a recommendation memo. The asymmetry is at least partially a natural result of the different nature of the work that lawyers and economists do. But it is important to note that one consequence of this asymmetry, whatever its cause, is that it creates the potential to weaken BE's independence. BE maintains a high level of integrity and independence over core economic tasks—*e.g.*, economic modeling and framing, statistical analyses, and assessments of outside economic work—yet when it comes to the actual policy recommendation, *I think it is fair to raise the question whether the Commission always receives unfiltered recommendations when BE dissents from the recommendation of BC or BCP staff.*

One example of this phenomenon is the so-called "compromise recommendation," that is, a BE staff economist might recommend the FTC accept a consent decree rather than litigate or challenge a proposed merger when the underlying economic analysis reveals very little actual economic support for liability. In my experience, *it is not uncommon for a BE staff analysis to convincingly demonstrate that competitive harm is possible but unlikely, but for BE staff to rec-*

¹²³Statement of Commissioner Joshua D. Wright, On the FTC's Bureau of Economics, Independence, and Agency Performance, *supra* note 119, at 11.

¹²⁴*Id.* at 11–12.

¹²⁵*Id.* at 11.

ommend against litigation on those grounds, but in favor of a consent order. The problem with this compromise approach is, of course, that a recommendation to enter into a consent order must also require economic evidence sufficient to give the Commission reason to believe that competitive harm is likely. This type of “compromise” recommendation in some ways reflects the reality of BE staff incentives. Engaging in a prolonged struggle over the issue of liability with BC and BC management is exceedingly difficult when the economist is simply outmanned. It also ties up already scarce BE resources on a matter that the parties are apparently “willing” to settle.¹²⁶

The ability of BC or BCP staff to dilute the analysis of BE staffers in a combined compromise recommendation renders moot this provision of the operating manual:

Dissenting staff recommendations regarding compulsory process, compliance, consent agreements, proposed trade regulation rules or proposed industrywide investigations should be submitted to the Commission by the originating offices, upon the request of the staff member.¹²⁷

For this provision to have any effect, there must be a separate dissenting staff recommendation that can be seen by Commissioners—and, ideally, also made public.

Recommendation: Require BE to Comment on Upgrading Investigations

Similarly, we recommend enhancing BE’s role earlier in the investigation process: at the point where the Bureau Director decides whether to upgrade an initial (Phase I) investigation to a full investigation. This is a critical inflection point in the FTC’s investigative process for three reasons:

1. In principle, the staff is not supposed to negotiate consent decrees during the initial investigation phase;
2. In principle, the staff is not supposed to use compulsory discovery process during the initial investigation phase, meaning a target company’s cooperation until this point is at least theoretically voluntary; and
3. Either the decision to open a formal investigation or the subsequent issuance of CIDs may trigger a public company’s duty to disclose the investigation in its quarterly securities filings.

It is also likely the point at which the staff determines (or at least begins to seriously consider) whether or not the Commission is likely to approve a staff recommendation to issue a complaint against any of the specific targets of the investigation.

For all these reasons, converting an initial investigation to a full investigation gives the staff enormous power to coerce a settlement. This decision deserves far more rigorous analysis than it currently seems to receive.

When the BC or BCP staff proposes to their Bureau director that an initial investigation be expanded into a full investigation, the FTC Operating Manual requires a (confidential) memorandum justifying a decision, but does *not* formally require the Bureau of Economics, or require that the analysis performed by any FTC staff correspond to two of the three requirements of Section 5(n) or the materiality requirement of the Deception Policy Statement:

3.5.1.4 Transmittal Memorandum

The memorandum requesting approval for full investigation should clearly and succinctly explain the need for approval of the full investigation, including a discussion of relevant factors among the following:

- (1) A description of the practices and their impact on consumers and/or on the marketplace;
- (2) Marketing area and volume of business of the proposed respondent and the overall size of the market;
- (3) Extent of consumer injury inflicted by the practices to be investigated, the benefits to be achieved by the Commission action and/or the extent of competitive injury;
- (4) When applicable, an explanation of how the proposed investigation meets objectives and, where adopted, case selection criteria or the program to which it has been assigned;

¹²⁶ *Id.* at 7–8.

¹²⁷ Operating Manual § 3.3.5.1.1.

(5) When applicable, responses to the policy protocol questions (see OM Ch. 2);¹²⁸

We recommend modifying this in two ways. First, while approving a complaint or a consent decree should absolutely require a separate recommendation from the Bureau of Economics, requiring such a recommendation merely to convert an initial investigation to a full investigation might well pose too great a burden on BE's already over-taxed resources. But that is no reason why the FTC rules should not at least give BE the *opportunity* to write a separate memorandum if it so desires. Having this written recommendation shared with Commissioners would serve as an early warning system, alerting them to potentially problematic cases being investigated by BCP or BC staff *before* the staff has extracted a consent decree—something that regularly has effectively happened by the time the Commission votes on whether to authorize a complaint. Thus, giving BE the opportunity to be involved at this early stage may be critical to scrutinizing the FTC's use of consent decrees.

Second, there is no reason that the memorandum prepared by either BC or BCP staff should not correspond to the doctrinal requirements of the relevant authority. The Operating Manual falls well short of this by merely requiring some analysis of the “[e]xtent of consumer injury.” Why not countervailing benefit and reasonable avoidability, too, for Unfairness cases? And materiality in Deception cases? And the various other factors subsumed in the consumer welfare standard of the rule of reason, for Unfair Methods of Competition Cases?

That this would be only an *initial* analysis that will remain confidential under the Commission's rules is all the more reason it should not be a problem for the Staff to produce.

Economic Analysis in Reports & “Recommendations”

The Revealing Economic Conclusions for Suggestions (RECS) Act

Rep. Mike Pompeo's (R-KS) bill (H.R. 5136)¹²⁹ would require the FTC to include, in “any recommendations for legislative or regulatory action,” analysis from the Bureau of Economics including:

[T]he rationale for the Commission's determination that private markets or public institutions could not adequately address the issue, and that its recommended legislative or regulatory action is based on a reasoned determination that the benefits of the recommended action outweigh its costs.

Valuable as this is, the bill should be expanded to encompass other Commission pronouncements that aren't, strictly, “recommendations for legislative or regulatory action.”

Value of the Bill: Bringing Rigor to FTC Reports, Testimony, etc.

The lack of economic analysis in support of “recommendations for legislative or regulatory action” has grown more acute with time—not only in the FTC's reports but also in its testimony to Congress.

Section 6(b) of the FTC Act gives the Commission the authority “to conduct wide-ranging economic studies that do not have a specific law enforcement purpose” and to require the filing of “annual or special . . . reports or answers in writing to specific questions” for the purpose of obtaining information about “the organization, business, conduct, practices, management, and relation to other corporations, partnerships, and individuals” of any company over which the FTC has jurisdiction, except insurance companies. This section is a useful tool for better understanding business practices, particularly those undergoing rapid technological change. But it is only as valuable as the quality of the analyses these 6(b) reports contain. And typically they are fairly short on economic analysis, especially concerning consumer protection matters.

The FTC has consistently failed to include any apparent, meaningful role for the Bureau of Economics in its consumer protection workshops or in the drafting of the subsequent reports. Nor has the FTC explored the adequacy of existing legal tools to address concerns raised by its reports. For example, the FTC's 2014 workshop, “Big Data: A Tool for Inclusion or Exclusion?,” included not a single PhD economist

¹²⁸ Operating Manual § 3.3.5.1.4 (emphasis added).

¹²⁹ The Revealing Economic Conclusions for Suggestions Act, H.R. 5136, 114th Cong. (2016) [hereinafter RECS Act] available at <https://www.congress.gov/bill/114th-congress/house-bill/5136/text>.

or BE staffer.¹³⁰ The resulting 2016 report includes essentially just two footnotes on economics.¹³¹ Commissioner Ohlhausen dissented, noting that

Concerns about the effects of inaccurate data are certainly legitimate, but policymakers must evaluate such concerns in the larger context of the market and economic forces companies face. Businesses have strong incentives to seek accurate information about consumers, whatever the tool. Indeed, businesses use big data specifically to increase accuracy. Our competition expertise tells us that if one company draws incorrect conclusions and misses opportunities, competitors with better analysis will strive to fill the gap. . . .

To understand the benefits and risks of tools like big data analytics, we must also consider the powerful forces of economics and free-market competition. If we give undue credence to hypothetical harms, we risk distracting ourselves from genuine harms and discouraging the development of the very tools that promise new benefits to low income, disadvantaged, and vulnerable individuals. Today's report enriches the conversation about big data. My hope is that future participants in this conversation will test hypothetical harms with economic reasoning and empirical evidence.¹³²

The Commission's 2016 PrivacyCon conference did include several economists on a panel devoted to the "Economics of Privacy & Security."¹³³ But, as one of the event's discussants, Geoffrey Manne, noted:

One of the things I would say is that it's a little bit unfortunate we don't have more economists and engineers talking to each other. As you might have gathered from the last panel, an economist will tell you that merely identifying a problem isn't a sufficient basis for regulating to solve it, nor does the existence of a possible solution mean that that solution should be mandated. And you really need to identify real harms rather than just inferring them, as James Cooper pointed out earlier. And we need to give some thought to self-help and reputation and competition as solutions before we start to intervene. . . .

So we've talked all day about privacy risks, biases in data, bad outcomes, problems, but we haven't talked enough about beneficial uses that these things may enable. So deriving policy prescriptions from these sort of lopsided discussions is really perilous.

Now, there's an additional problem that we have in this forum as well, which is that the FTC has a tendency to find justification for enforcement decisions in things that are mentioned at workshops just like these. So that makes it doubly risky to be talking [] about these things without pointing out that there are important benefits here, and that the costs may not be as dramatic as it seems [just] because we're presenting these papers describing them.¹³⁴

As Manne notes, as a practical matter, these workshops and reports are often used by the Commission either to make legislative recommendations or to define FTC enforcement policy by recommending industry best practices (which the agency will effectively enforce). But, again, because they lack much in the way of economically rigorous analysis, these recommendations may not be as well-founded as they may be presumed to be.

In its 2000 Report to Congress, for example, the FTC called for comprehensive baseline legislation on privacy and data security.¹³⁵ Congress has not passed such legislation, but the FTC repeated the recommendation in its 2012 Privacy Report.¹³⁶

¹³⁰ Fed. Trade Comm'n, Public Workshop: Big Data: A Tool for Inclusion or Exclusion? (Sep. 15, 2014), available at <https://www.ftc.gov/news-events/events-calendar/2014/09/big-data-tool-inclusion-or-exclusion>.

¹³¹ FED. TRADE COMM'N, BIG DATA: A TOOL FOR INCLUSION OR EXCLUSION? UNDERSTANDING THE ISSUES FTC REPORT (2016), available at <https://www.ftc.gov/system/files/documents/reports/big-data-tool-inclusion-or-exclusion-understanding-issues/160106big-data-rpt.pdf>

¹³² *Id.* at A-1 to A-2.

¹³³ Fed. Trade Comm'n, Conference: PrivacyCon (Jan. 14, 2016), available at <https://www.ftc.gov/news-events/events-calendar/2016/01/privacycon>.

¹³⁴ Fed. Trade Comm'n, Transcript of the Remarks of Geoffrey A. Manne, 19 (Jan. 14, 2016), available at https://www.ftc.gov/system/files/documents/videos/privacycon-part-5/ftc_privacycon-transcript-segment-5.pdf#page=18.

¹³⁵ FED. TRADE COMM'N, PRIVACY ONLINE: FAIR INFORMATION PRACTICES IN THE ELECTRONIC MARKETPLACE (2000), available at <https://www.ftc.gov/sites/default/files/documents/reports/privacy-online-fair-information-practices-electronic-marketplace-federal-trade-commission-report/privacy2000text.pdf>.

¹³⁶ FED. TRADE COMM'N, PROTECTING CONSUMER PRIVACY IN AN ERA OF RAPID CHANGE: RECOMMENDATIONS FOR BUSINESS AND POLICYMAKERS (2012), available at <https://www.ftc.gov/>

While that Report called for significantly stricter legislation, less tied to consumer harm, it did *not* include any economic analysis by the FTC's Bureau of Economics. Indeed, by rejecting the harms-based model of the 2000 Report,¹³⁷ the 2012 report essentially dismisses the *relevance* of economic analysis, either in the report itself or in case-by-case adjudication.

In his dissent, Commissioner Rosch warned about the Report's reliance on unfairness rather than deception, noting that "'Unfairness' is an elastic and elusive concept. What is 'unfair' is in the eye of the beholder. . . ." ¹³⁸ In effect, Rosch, despite his long-standing hostility to economic analysis,¹³⁹ was really saying that the Commission had failed to justify its *analysis* of unfairness. Rosch objected to the Commission's invocation of unfairness against harms that have not been clearly analyzed:

That is not how the Commission itself has traditionally proceeded. To the contrary, the Commission represented in its 1980, and 1982 [sic], Statements to Congress that, absent deception, it will not generally enforce Section 5 against alleged intangible harm. In other contexts, the Commission has tried, through its advocacy, to convince others that our policy judgments are sensible and ought to be adopted.¹⁴⁰

Rosch contrasted the Report's reliance on unfairness with the Commission's Unfair Methods of Competition doctrine, which he called "self-limiting" because it was tied to analysis of market power.¹⁴¹ Rosch lamented that,

There does not appear to be any such limiting principle applicable to many of the recommendations of the Report. If implemented as written, many of the Report's recommendations would instead apply to almost all firms and to most information collection practices. It would install "Big Brother" as the watchdog over these practices not only in the online world but in the offline world. That is not only paternalistic, but it goes well beyond what the Commission said in the early 1980s that it would do, and well beyond what Congress has permitted the Commission to do under Section 5(n). I would instead stand by what we have said and challenge information collection practices, including behavioral tracking, only when these practices are deceptive, "unfair" within the strictures of Section 5(n) and our commitments to Congress, or employed by a firm with market power and therefore challengeable on a stand-alone basis under Section 5's prohibition of unfair methods of competition.¹⁴²

The proposed bill would help to correct these defects, and to ensure that FTC Reports, at least those containing legislative or rulemaking recommendations, are based on the rigorous analysis that should be expected of an expert investigative agency's policymaking—especially one that has arguably the greatest pool of economic talent found anywhere in government in America.

Recommendation: Require Analysis of Recommended Industry Best Practices

In this regard the proposed bill would be enormously beneficial, but it could, and should, do significantly more.

First and foremost, the term "recommendations for legislative or regulatory action" would not encompass the most significant FTC recommendations: those included in "industry best practices" publications and reports produced by the Commission. These documents purport to offer expert suggestions for businesses to follow in order to help them to protect consumer welfare and to better comply with the relevant laws and regulations. But the FTC increasingly treats these recommendations as soft law, not merely helpful guidance, in at least two senses:

[sites/default/files/documents/reports/federal-trade-commission-report-protecting-consumer-privacy-era-rapid-change-recommendations/120326privacyreport.pdf](https://www.ftc.gov/sites/default/files/documents/reports/federal-trade-commission-report-protecting-consumer-privacy-era-rapid-change-recommendations/120326privacyreport.pdf).

¹³⁷PRIVACY ONLINE: FAIR INFORMATION PRACTICES IN THE ELECTRONIC MARKETPLACE, *supra* note 135.

¹³⁸PROTECTING CONSUMER PRIVACY IN AN ERA OF RAPID CHANGE, *supra* note 136, at C-3.

¹³⁹See e.g., J. Thomas Rosch, *Litigating Merger Challenges: Lessons Learned* (June 2, 2008), available at <https://www.ftc.gov/sites/default/files/documents/public-statements/litigating-merger-challenges-lessons-learned/080602litigatingmerger.pdf> ("any kind of economic analyses that require the use of mathematical formulae are of little persuasive value in the courtroom setting;" "when I see an economic formula my eyes start to glaze over."); See generally Joshua Wright, *Commissioner Rosch v. Economics, Again*, TRUTH ON THE MARKET (Oct. 7, 2008), available at <https://truthonthemarket.com/2008/10/07/commissioner-rosch-v-economics-again/>.

¹⁴⁰PROTECTING CONSUMER PRIVACY IN AN ERA OF RAPID CHANGE, *supra* note 136, at C-4.

¹⁴¹*Id.* at C-5.

¹⁴²*Id.*

1. The FTC uses these recommendations as the basis for writing its 20-year consent-decree requirements, including ones unrelated, or only loosely related, to the conduct at issue in an enforcement action; and
2. The FTC uses these recommendations as the substantive basis for enforcement actions—for example, by pointing to a company’s failure to do something the FTC recommended as evidence of the unreasonableness of its practices.

Former Chairman Tim Muris notes this about the “voluntary” guidelines issued by the FTC in 2009 in conjunction with three other Federal agencies, comparing them to the FTC’s efforts to ban advertising to children:

The FTC has been down this road before. Prodded by consumer activists in the late 1970s, the Commission sought to stop advertising to children. . . .

One difference between the current proposal and the old rulemaking—called Kid Vid—is that this time the agencies are suggesting that the standards be adopted “voluntarily” by industry. Yet can standards suggested by a government claiming the power to regulate truly be “voluntary”? Moreover, at the same workshop that the standards were announced, a representative of one of the same activist organizations that inspired the 1970s efforts speculated that a failure to comply with the new proposal would provoke calls for rules or legislation.¹⁴³

Regulation by leering glare is still regulation.

Informed by the trauma of its near-fatal confrontation with Congress at the end of the Carter administration, the FTC was long skittish about making recommendations for businesses in its reports, beyond high level calls for attention to issues like data security. That changed in 2009, however. The FTC has since issued a flurry of reports recommending best practices like “privacy by design” and “security by design,” first generally, and then across a variety of areas, from Big Data to facial recognition.¹⁴⁴

The FTC’s recommendations to industry in its 2005 report on file-sharing were admirably circumspect:

Industry should decrease risks to consumers through technological innovation and development, industry self-regulation (including risk disclosures), and consumer education.¹⁴⁵

This is not to say that the FTC could not or should not have done more to address the very real problem of inadvertent online file-sharing. Indeed, one of the authors of this report has lauded the (Democratic-led) FTC for bringing its 2011 enforcement action against Frostwire¹⁴⁶ for designing its peer-to-peer file-sharing software in a way that deceived users into unwittingly sharing files.¹⁴⁷ Rather, it is simply to say that the FTC, in 2005, understood that a report was not a substitute for a rule-making—*i.e.*, not an appropriate place to make “recommendations” for the private sector that would have any force of law.

By 2012 the FTC had lost any such scruples. Its Privacy Report, issued that year, is entitled “Recommendations for Businesses and Policymakers.” The title says it all: The FTC directed its sweeping recommendations for “privacy by design” to both the companies it regulates and the elected representatives the FTC supposedly serves:

The final privacy framework is intended to articulate best practices for companies that collect and use consumer data. These best practices can be useful to companies as they develop and maintain processes and systems to operationalize privacy and data security practices within their businesses. The

¹⁴³ *Statement of Timothy J. Muris, supra* note 14, at 11–13.

¹⁴⁴ BIG DATA: A TOOL FOR INCLUSION OR EXCLUSION, *supra* note 131; FED TRADE COMM’N, FACING FACTS: BEST PRACTICES FOR COMMON USES OF FACIAL RECOGNITION TECHNOLOGIES (2012), available at <https://www.ftc.gov/sites/default/files/documents/reports/facing-facts-best-practices-common-uses-facial-recognition-technologies/121022faciatechrpt.pdf>.

¹⁴⁵ FED. TRADE COMM’N, PEER-TO-PEER FILE-SHARING TECHNOLOGY: CONSUMER PROTECTION AND COMPETITION ISSUES (2005), available at <https://www.ftc.gov/sites/default/files/documents/reports/peer-peer-file-sharing-technology-consumer-protection-and-competition-issues/050623p2prpt.pdf>.

¹⁴⁶ Fed. Trade Comm’n v. Frostwire LLC, FTC File No. 112 3041, <https://www.ftc.gov/enforcement/cases-proceedings/112-3041/frostwire-llc-angel-leon> (2011).

¹⁴⁷ *Prepared Statement of Berin Szóka, President of TechFreedom: Hearing Before the H. Energy & Commerce Comm. 112th Cong.* (2012), 23, available at https://techliberation.com/wp-content/uploads/2012/11/Testimony_CMT_03.29.12_Szoka.pdf.

final privacy framework contained in this report is also intended to assist Congress as it considers privacy legislation.¹⁴⁸

Of course, the FTC added:

To the extent the framework goes beyond existing legal requirements, the framework is not intended to serve as a template for law enforcement actions or regulations under laws currently enforced by the FTC.¹⁴⁹

Also noteworthy is the contrast between the two reports in their analytical rigor. The file sharing report noted:

The workshop panelists and public comments did not provide a sufficient basis to conclude whether the degree of risk associated with P2P file-sharing programs is greater than, equal to, or less than the degree of risk when using other Internet technologies.¹⁵⁰

The 2012 report shows no such modesty, as Commissioner Rosch lamented in his dissent (“There does not appear to be any such limiting principle applicable to many of the recommendations of the Report.”).¹⁵¹

In 2015, Commissioner Wright expressed dismay at this same problem in his dissent from the staff report on the Internet of Things Workshop:

I dissent from the Commission’s decision to authorize the publication of staff’s report on its Internet of Things workshop (“Workshop Report”) because the Workshop Report includes a lengthy discussion of industry best practices and recommendations for broad-based privacy legislation without analytical support to establish the likelihood that those practices and recommendations, if adopted, would improve consumer welfare. . . .

First . . ., merely holding a workshop—without more—should rarely be the sole or even the primary basis for setting forth specific best practices or legislative recommendations. . . .

Second, the Commission and our staff must actually engage in a rigorous cost-benefit analysis prior to disseminating best practices or legislative recommendations, given the real world consequences for the consumers we are obligated to protect. . . .

*The most significant drawback of the concepts of “security by design” and other privacy-related catchphrases is that they do not appear to contain any meaningful analytical content. . . . An economic and evidence-based approach sensitive to [] tradeoffs is much more likely to result in consumer-welfare enhancing consumer protection regulation. To the extent concepts such as security by design or data minimization are endorsed at any cost—or without regard to whether the marginal cost of a particular decision exceeds its marginal benefits—then application of these principles will result in greater compliance costs without countervailing benefit. Such costs will be passed on to consumers in the form of higher prices or less useful products, as well as potentially deter competition and innovation among firms participating in the Internet of Things.*¹⁵²

The point illustrated by comparing these examples is the difficulty inherent in trying to require greater rigor from the FTC in recommendations to businesses when those recommendations can be either high level and commonsensical (as in 2005) or sweeping and effectively regulatory (as in 2012 and 2015). Thus, we recommend the following simple amendment to the proposed bill:

[The FTC] shall not submit any *proposed industry best practices, industry guidance or recommendations* for legislative or regulatory action without [analysis]. . . .

This wording would not apply to the kind of “recommendation” that the FTC made occasionally before 2009, as exemplified by the 2005 report. In any event, the bill’s requirement is easily satisfied: essentially the FTC need only give the Bureau of Economics a role in drafting the report. Because this recommendation would not

¹⁴⁸ Protecting Consumer Privacy in an Era of Rapid Change, *supra* note 136, at iii.

¹⁴⁹ *Id.* at vii.

¹⁵⁰ PEER-TO-PEER FILE-SHARING TECHNOLOGY, *supra* note 145, at 12.

¹⁵¹ PROTECTING CONSUMER PRIVACY IN AN ERA OF RAPID CHANGE, *supra* note 136, at C–5.

¹⁵² Dissenting Statement of Commissioner Joshua D. Wright, *Issuance of The Internet of Things: Privacy and Security in a Connected World Staff Report* (Jan. 27, 2015) (emphasis added), available at https://www.ftc.gov/system/files/documents/public_statements/620701/150127iotjdwtmt.pdf.

hamstring the FTC's enforcement actions, nor tie the FTC up in court, it should not be controversial, even if applied to proposed industry best practices and guidance.

Our proposed amendment would be simpler than attempting to broaden the definition of "regulatory action" beyond just rulemakings (which is how the FTC would likely limit its interpretation of the bill as drafted now) to include the kind of "regulatory action" that matters most: its use of reports to indicate how it will regulate through case by case enforcement, *i.e.*, its "common law of consent decrees."

Recommendation: Clarify the Bill's Language to Ensure It Applies to All FTC Reports

Another important difference between the 2000 and 2012 privacy reports is that the 2000 report is labelled "A Report to Congress," while the 2012 report is not and, indeed, barely mentions Congress. This reflects a little-noticed aspect of the way Section 6(f) is currently written, with subsection numbers added for clarity:

(f) Publication of information; reports

To [i] make public from time to time such portions of the information obtained by it hereunder as are in the public interest; and to [ii] make annual and special reports to the Congress and to submit therewith recommendations for additional legislation; and to [iii] provide for the publication of its reports and decisions in such form and manner as may be best adapted for public information and use.¹⁵³

In other words, the Commission has shifted from relying upon 6(f)(ii) to 6(f)(i) and (iii). This distinction may seem unimportant, but it may cause the bill as drafted to be rendered meaningless, because the way it is worded could be read to apply only to 6(f)(ii). The bill would amend the existing proviso in Section 6(f) as follows:

Provided [t]hat the Commission shall not submit any recommendations for legislative or regulatory action without an economic analysis by the Bureau of Economics. . .

The use of the words "submit" and "recommendations" clearly tie this proviso to 6(f)(ii). Thus, the FTC could claim that it need not include the analysis required by the bill unless it is specifically submitting recommendations to Congress, which it simply does not do anymore.

Instead we propose the following slight tweak to the bill's wording, to ensure that it would apply to the entirety of Section 6(f):

Provided [t]hat the Commission shall not *make* any recommendations for legislative or regulatory action without an economic analysis by the Bureau of Economics. . .

This would require the participation of the Bureau of Economics in *all* FTC reports (that make qualifying recommendations), whatever their form. It would also require BE's participation in at least two other contexts where such recommendations are likely to be made: (i) Congressional testimony and (ii) the competition advocacy filings the Commission makes with state and local regulatory and legislative bodies, and with other Federal regulatory agencies. This is a feature, not a bug: participation by BE is not something to be minimized; it should be woven into the fabric of *all* of the FTC's activities. As we have noted previously:

The most important, most welfare-enhancing reform the FTC could undertake is to better incorporate sound economic- and evidence-based analysis in both its substantive decisions as well as in its process. While the FTC has a strong tradition of economics in its antitrust decision-making, its record in using economics in other areas is mixed.¹⁵⁴

Because the bill does not in any way create a cause of action against the FTC for failing to comply with the requirement, it will not hamstring the FTC if the agency fails to take the bill's requirements seriously. That, if anything, is a weakness of the bill, but it is largely inevitable. It will always be up to the discretion of the Commission itself (subject, of course, to congressional oversight) to decide how much "economic analysis" is "sufficient" under the bill.

¹⁵³ 15 U.S.C. § 46(f)

¹⁵⁴ Geoffrey A. Manne, *Humility, Institutional Constraints and Economic Rigor: Limiting the FTC's Discretion*, ICLE White Paper 2014-1 (Feb. 28, 2014) at 4, available at <http://docs.house.gov/meetings/IF/IF17/20140228/101812/HHRG-113-IF17-Wstate-ManneG-20140228-SD002.pdf>.

Recommendation: Require a Supermajority of Commissioners to Decide What Analysis is “Sufficient”

As written, the bill might do little more than shame the Chairman into involving the Bureau of Economics somewhat more in the writing of reports and the workshops that lead to them—if only because the bill might embolden a single Commissioner to object to the FTC’s lack of analysis, as Commissioner Wright objected to the FTC’s Internet of Things report.¹⁵⁵ This change in incentives for the Chairman and other commissioners, alone, may not significantly improve the analytical quality of the FTC’s reports, given the hostility of the Bureau of Consumer Protection to economic analysis, although having *any* involvement by BE would certainly be an improvement.

Again, the question of “sufficiency” is inherently something that will be left to the Commission’s discretion, but there is no principled reason that it has to be resolved through simple majority votes. On the other hand, giving a single Commissioner the right to veto an FTC “recommendation” as lacking a “sufficient” analytical basis might go too far.

We recommend striking a balance by requiring a supermajority (majority plus one, except in the case of a three-member Commission) of Commissioners to approve of the sufficiency of the analysis—essentially that this vote be taken, or at least recorded, separately from the vote on the issuance of the report itself. (The “sufficiency” vote would not stop the FTC from issuing a report.) At the same time, we recommend that the outcome of the “sufficiency” vote be disclosed on the first page of all reports or other documents containing recommendations.

Such a mechanism would effectively expand the set of options for which Commissioners could vote, enabling them to express subtler degrees of preference without constraining them, as now, into making the binary choice between approving or rejecting a recommendation *in toto*. In other words, while the cost of expressing disapproval today, in the form of a dissent from a report, may be too high in some cases (especially for Commissioners in the majority party), the cost of expressing disapproval for the sufficiency of analysis without vetoing an entire report would be much lower. Allowing such a vote, and publishing its results, would offer important information to the public. It would also increase the leverage of commissioners most concerned with ensuring that FTC recommendations are supported by sufficient rigor to influence the content and conclusions of FTC reports and similar documents.

In cases where the three-member majority feels the two-member minority’s objections to analytical rigor are merely a pretense for objections to the recommendations themselves, the bill as we envision it would do nothing to stop the majority from issuing its recommendations anyway, of course; the “sufficiency” vote in this sense may sometimes be merely an expression of preference. Nonetheless, the majority Commissioners would likely be compelled to do more to explain why they believe the analysis included in support of a recommendation is sufficient, and why the minority is conflating its own policy views with the question of analytical sufficiency. These would also be valuable additions to the public’s understanding of the basis for Commission recommendations.

The virtue of our proposed approach is that it would further lower the bar for the Commission to do something it ought to do anyway: involve the Bureau of Economics in its decision-making.

Recommendation: Codify Congress’s Commitment to Competition Advocacy

As we propose amending the RECS Act, consistent with the spirit with which we believe the bill is intended, BE would also have to be involved in any competition advocacy filings made by the FTC. Again, we believe this is all for the good. But it might, on the margin, discourage the FTC from issuing such filings in the first place—something we believe the FTC already does not do enough of. Thus, as discussed below, we recommend that Congress do more to encourage competition advocacy filings by the FTC.¹⁵⁶ At minimum, this means amending Section 6 to provide specific statutory authority for competition advocacy, something the FTC only vaguely divines from the Section today. As the text stands today, this authority is far from apparent, especially because the current Section 6 makes reference to “recommendations” only with respect to *Congress* in what we above refer to as Section 6(f)(ii).

¹⁵⁵ See *Issuance of The Internet of Things: Privacy and Security in a Connected World Staff Report*, *supra* note 152, at 4.

¹⁵⁶ See *infra* note 87.

Other Sources of Enforcement Authority (Guidelines, etc.)

The Solidifying Habitual & Institutional Explanations of Liability & Defenses (SHIELD) Act

Rep. Mike Pompeo's (R-KS) bill (H.R. 5118)¹⁵⁷ clarifies what is already black letter law: agency guidelines do not create any binding legal obligations, either upon regulated companies or the FTC. This means the FTC can bring enforcement actions outside the bounds of its Unfairness and Deception Policy Statements, its Unfair Methods of Competition Enforcement Policy Statement, and its regulations promulgated under other statutes enforced by the Commission (*e.g.*, the "Safeguards Rule," promulgated under the Gramm-Leach-Bliley Act)¹⁵⁸ unless Congress codifies the Statements in the statute. The only substantively operative provision of the bill is section (B), which provides that:

Compliance with any guidelines, general statement of policy, or similar guidance issued by the Commission may be used as evidence of compliance with the provision of law under which the guidelines, general statement of policy, or guidance was issued.

This does not create a formal safe harbor; it merely allows companies targeted by the FTC to cite FTC's past guidance in their defense. This should be uncontroversial.

Value of the Bill: Increasing Legal Certainty and Decreasing the Coercive Regulatory Effect of the FTC's Soft Law

The bill would accomplish two primary goals. First, it would formally bar the FTC from doing something it has likely been doing in practice for some time: treating its own informal guidance as quasi-regulatory. To the extent that the Commission actually does so, it would effectively be circumventing the safeguards Congress imposed in 1980 upon the FTC's Section 5 rulemaking powers by amending the FTC Improvement Act of 1975 (commonly called "Magnuson-Moss"),¹⁵⁹ But of course, for exactly this reason, the Commission would never *admit* that this is what it is doing when its enforcement agenda just happens to line up with its previous recommendations.

More clear and more troubling is that, in the *LabMD* case, the Commission argued that the company, a small cancer testing lab, had committed an unfair trade practice sometime between 2006 and 2008 by failing to take "reasonable" measures to prevent the installation and operation of peer-to-peer file-sharing software on its network, which made patient billing information accessible to Tiversa, a company with specialized tools capable of scouring P2P networks for sensitive information. Crucial to the FTC's Complaint was its allegation that:

Since at least 2005, security professionals and others (including the Commission) have warned that P2P applications present a risk that users will inadvertently share files on P2P networks.¹⁶⁰

The Commission was referring, obliquely, to its 2005 report,¹⁶¹ which offered this rather unhelpful suggestion to affected companies:

Industry should decrease risks to consumers through technological innovation and development, industry self-regulation (including risk disclosures), and consumer education.

Not until January 2010 did the FTC issue "Peer-to-Peer File Sharing: A Guide for Business"¹⁶²—about the same time, it appears, that the FTC undertook its in-

¹⁵⁷ Solidifying Habitual and Institutional Explanations of Liability and Defenses Act, H.R. 5118, 114th Cong. (2016) [hereinafter SHIELD Act], available at <https://www.congress.gov/bill/114th-congress/house-bill/5118/text>.

¹⁵⁸ Standards for Safeguarding Customer Information, 16 C.F.R. § 314.

¹⁵⁹ The term Magnuson-Moss is inapt for two reasons. First, as former Chairman Muris explains, "Although within the Commission these procedures are uniformly referred to as 'Magnuson Moss,' in fact, the procedures are contained within Title II of the Magnuson Moss Warranty—Federal Trade Commission Improvement Act of 1975. Only Title I involved the Magnuson Moss Warranty Act. . . ." *Statement of Timothy J. Muris, supra* note 14, at 22, n. 44. Second, the safeguards at issue were adopted in 1980, not 1975, when "Mag-Moss" was passed.

¹⁶⁰ Complaint, In the Matter of LabMD, Inc., Docket No. 9357 at 4, available at <https://www.ftc.gov/sites/default/files/documents/cases/2013/08/130829labmdpart3.pdf>.

¹⁶¹ PEER-TO-PEER FILE-SHARING TECHNOLOGY, *supra* note 145.

¹⁶² Fed. Trade, Comm'n, *Peer-to-Peer File Sharing: A Guide for Business* (Jan. 2010), available at <https://www.ftc.gov/tips-advice/business-center/guidance/peer-peer-file-sharing-guide-business>.

investigation of LabMD. The SHIELD Act would clearly bar the FTC from pointing to its own past guidance as creating a legal trigger for liability. The Commission's assessment of "reasonableness" would have to be proven through other factors; indeed, since "reasonable" is found nowhere in Section 5 or even in the Unfairness Policy Statement, the Commission would have to prove the underlying elements of unfairness, without shortcutting this analysis by oblique reference to its own past reports.

A related concern is the Commission's application of rules promulgated in one context, in which they have binding authority, to other contexts in which they do not. The most striking example of this practice is the Commission's use of the Safeguards Rule, which "applies to the handling of customer information by all financial institutions over which the [FTC] has jurisdiction,"¹⁶³ to define unfair data security practices, and the remedies applied by the FTC in consent decrees, outside the financial sector. Although the Safeguards Rule has regulatory authority for financial institutions, its authority is no different than informal guidance (or recommended "best practices") the Commission offers for everyone else. Nevertheless, the Commission has imposed remedies virtually identical to the Safeguards Rule in nearly every data security consent order into which it has entered.

[T]he majority of the FTC's [data security] cases, regardless of cause of action or facts, impose the same remedy: the set of security standards laid out in the FTC's Safeguards Rule. Most notably, this is true regardless of whether the respondents were financial institutions (to which the Safeguards Rule directly applies) or not (to which the Rule has no direct application), and regardless of whether the claim is generally one of deception or unfairness.¹⁶⁴

Second, the SHIELD Act would allow companies to raise their compliance with FTC guidance as part of their defense. This would, at a minimum, help encourage companies to resist settling legally questionable or analytically unsupported enforcement actions.

Recommendation: Clarify that Consent Decrees, Reports, and FTC Best Practices are not Binding

We propose expanding the bill's language slightly to ensure that it achieves its intended goal:

No guidelines, general statements of policy, *consent decrees*, *settlements*, *reports*, *recommended best practices*, or similar guidance issued by the Commission shall confer any right.

As should be clear by now, these other forms of soft law are the most important aspects of the FTC's discretionary model, especially given the paucity of policy statements (building upon the three major ones, such as on materiality, for example) or issue-specific "Guides."

Specifically, the Commission regularly applies its recommended best practices (grouped under catchphrases like "privacy by design" and "security by design") as mandatory company-specific regulations in consent decrees that are themselves applied, in cookie-cutter fashion, across enforcement actions brought against companies that differ greatly in their circumstances, and regardless of the nature or extent of the injury or the specific facts of their case.

Second, the *LabMD* case provides at least one clear example wherein the FTC has treated its own previous reports, making vague recommendations about the need for better industry data security practices (regarding peer-to-peer file-sharing), as a critical part of the trigger for legal liability.¹⁶⁵ We suspect this is the tip of the iceberg—that the FTC in fact does this kind of thing quite often, but usually does not have to admit it, because it is able to settle cases without revealing its legal arguments. Only in the *LabMD* case (one of the first (of two) data security cases to be litigated after more than a decade of FTC consent decrees in this area) did the Commission have to make the connection between its previous "recommendations" and its application of Section 5. Even here, in its *LabMD* Complaint, it should be noted, the Commission did not specifically cite its 2005 P2P file-sharing report, but instead vaguely alluded to it—suggesting that even FTC staff were wary of revealing this connection.

¹⁶³ 16 C.F.R. § 314.1(b).

¹⁶⁴ Manne & Sperry, *supra* note 52, at 20.

¹⁶⁵ See *supra* note 66 and note 161.

Recommendation: Specify When a Defendant May Raise Evidence of Its Compliance with FTC Guidance

The bill does not currently specify *when* in the enforcement process evidence of compliance may be cited. It is important that a defendant be able to raise a compliance defense as early as possible. Without such an opportunity, the Commission can drag out an investigation that should have been terminated early, as when the subject of the investigation acted in good faith reliance upon the Commission's own statements. Ideally, this would occur during motions to quash CIDs.

Further, it would help if the FTC amended its rule on such motions, 16 C.F.R. § 2.10, to specify that this defense could be raised at part of a motion to quash. And, as we noted above,¹⁶⁶ it is critical that these challenges be permitted to remain confidential, as many companies may choose to avoid the risk the public exposure that comes with challenging CIDs.

At a minimum, the defendant should be able to raise this defense in a way that is communicated to Commissioners *before* the Commission's vote on whether to issue a complaint.

Recommendation: Encourage the FTC to Issue More Policy Statements & Guides

As the proposed SHIELD Act reflects, while there is some risk of ossification from over-reliance on *ex ante* guidelines and policy statements, the absence of such guidance documents can leave consumers and economic actors with insufficient notice of FTC enforcement principles and practices. Absent meaningful constraints on the Commission's discretionary authority, the costs of over-enforcement may be as great or greater than the costs of over-regulation. For these reasons, the bill should require the FTC to issue substantive guidelines, allow private parties to petition the FTC to issue guidelines, or allow a single Commissioner to force the issue.

A good place to start would be privacy regulation, where the Commission has issued no meaningful guides.¹⁶⁷ The Commission has done better on data security, with guides, for example, on photocopier data security (2010),¹⁶⁸ P2P software (2010),¹⁶⁹ and mobile app security (2013).¹⁷⁰ But none of these, and even the particularly thorough "Start with Security: A Guide for Business" (2015),¹⁷¹ does the kind of thing the various antitrust guidelines do: expand upon the *analytical framework* by which the Commission determines how much security is enough. This must be grounded in the component elements of Section 5, not the Commission's policy agenda or technical expertise.

More important than issue-specific guides would be guidance one step up the Doctrinal Pyramid, explaining how concepts like materiality, weighing injury with benefits, and measuring reasonable avoidability will be measured.¹⁷² Such a document would greatly enhance the value of issue-specific guides by allowing regulated companies to understand not just what the Commission might demand in the future, but the doctrinal legal basis for doing so.

Remedies

Appropriate Tailoring of Remedies

No Bill Proposed

The FTC has, perhaps predictably, also pushed the envelope with regard to the sorts of remedies it seeks against a broader category of targets. Initially, the Commission was given authority to pursue permanent injunctions under Section 13(b) as part of its ongoing mission to curb outright fraud.¹⁷³ Over time, however, the FTC has expanded its use of Section 13(b) in order to target companies that engage

¹⁶⁶ See *supra* at 46.

¹⁶⁷ See, e.g., Fed. Trade Comm'n, *Federal Trade Commission Enforcement of the U.S.-EU and U.S.-Swiss Safe Harbor Frameworks* (Dec. 2012), available at <https://www.ftc.gov/tips-advice/business-center/guidance/federal-trade-commission-enforcement-us-eu-us-swiss-safe-harbor>

¹⁶⁸ Fed. Trade Comm'n, *Copier Data Security: A Guide for Businesses* (Nov. 2010), available at <https://www.ftc.gov/tips-advice/business-center/guidance/copier-data-security-guide-businesses>

¹⁶⁹ *Peer-to-Peer File Sharing: A Guide for Business*, *supra* note 162.

¹⁷⁰ Fed. Trade Comm'n, *Mobile App Developers: Start with Security* (Feb. 2013), available at <https://www.ftc.gov/tips-advice/business-center/guidance/mobile-app-developers-start-security>

¹⁷¹ Fed. Trade Comm'n, *Start with Security: A Guide for Business* (Jun. 2015), available at <https://www.ftc.gov/tips-advice/business-center/guidance/start-security-guide-business>

¹⁷² See *supra* note 12.

¹⁷³ See generally Beales & Muris, *supra* note 21.

in conduct that implicates issues from substantiation claims to product design—all far from fraudulent territory.¹⁷⁴

For instance, Apple, Google, and Amazon have all been targets of the Commission for issues related to the design and function of their respective mobile app stores.¹⁷⁵ Amazon, one of the rare parties to proceed to full litigation on a Section 5 unfairness case, recently lost a summary judgment motion on a claim that its in-app purchasing system permitted children to make in-app purchases without parental “informed consent,” thus engaging in an “unfair practice.”¹⁷⁶ As part of its case the Commission sought a permanent injunction under Section 13(b) against Amazon on the basis of the Commission’s claim that it was “likely to continue to injure consumers, reap unjust enrichment, and harm the public interest.”¹⁷⁷

This practice, called “fencing-in,”¹⁷⁸ may be appropriate for the inveterate fraudsters—against whom it is authorized under Section 19 of the Act:

If the Commission satisfies the court that the act or practice to which the cease and desist order relates is *one which a reasonable man would have known under the circumstances was dishonest or fraudulent*, the court may grant . . . such relief as the court finds necessary.¹⁷⁹

The FTC—in the past—indeed viewed Section 13(b) as a tool to police clearly fraudulent practices. “Consistent with the limitations in Section 19, the agency used Section 13(b) for a narrow class of cases involving fraud, near fraud, or worthless products.”¹⁸⁰ Meanwhile, courts, for their part, “blessed this limited expansion of FTC authority,” and still see the appropriate scope of Section 13(b) as a limited one.

But the argument for extending fencing-in beyond the fraud context is extremely weak. Nevertheless, the FTC has more recently, as in the *Amazon* case, sought to use 13(b) against legitimate companies, dramatically expanding its scope—and its *in terrorem* effect.¹⁸¹

Such broad “fencing in” relief (imposition of behavioral requirements that are more extensive than required [in order] to avoid future violations) goes well beyond prior FTC practice and may be aimed at “encouraging” other firms in similar industries to adopt costly new testing.¹⁸²

Effectively, from the Commission’s perspective, Aman—with its app store that satisfied the needs of a huge number of consumers—was legally equivalent to “defendants engaged in continuous, fraudulent practices [who] were deemed likely to re-offend based on the ‘systemic nature’ of their misrepresentations.”¹⁸³ This could not have been what Congress intended.

The courts, when they are presented with the opportunity to review this approach (as they sometimes are in Deception cases and as they virtually never are in Unfairness cases, given the lack of litigation) have been less than receptive. Although Amazon lost its motion for summary judgment, it prevailed on the question of whether Section 13(b) presented an appropriate remedy for its alleged infractions.

While permanent injunctions are often awarded in cases where liability under the FTC Act is determined, Amazon correctly distinguishes those cases from the facts of this case . . . [C]ases in which a permanent injunction has been entered involved deceptive, ongoing practices.¹⁸⁴

¹⁷⁴ *Id.* at 4.

¹⁷⁵ See Geoffrey A. Manne, *Federal Intrusion: Too Many Apps for That*, WALL STR. J. (Sep. 16, 2014), <http://www.wsj.com/articles/geoffrey-manne-federal-intrusion-too-many-apps-for-that-1410908397>.

¹⁷⁶ Fed. Trade Comm’n v. Amazon.com, Inc., Case No. C14–1038–JCC, slip op. at 10 (W.D. Wash. 2016), available at https://www.ftc.gov/system/files/documents/cases/16042amazon_order.pdf.

¹⁷⁷ *Id.* at 10.

¹⁷⁸ See, e.g., Federal Trade Commission V. RCA Credit Services, LLC, Case No. 8:08–CV–2062–T–27AEP. (M.D. Fla. Jul 21, 2010) at 20 (“Courts also have discretion to include ‘fencing-in’ provisions that extend beyond the specific violations at issue in the case to prevent Defendants from engaging in similar deceptive practices in the future.”).

¹⁷⁹ 15 U.S.C. § 57(b)-(a)(2) and -(b).

¹⁸⁰ Beales & Muris, *supra* note 21, at 22.

¹⁸¹ *Id.* at 4 (“The FTC now threatens to expand the use of the Section 13(b) program beyond fraud cases, suggesting that it may use Section 13(b) to seek consumer redress even against legitimate companies.”).

¹⁸² Alden Abbott, *Time to Reform FTC Advertising Regulation*, Heritage Foundation Legal Memorandum #140 on Regulation (Oct. 29, 2014), available at http://www.heritage.org/research/reports/2014/10/time-to-reform-ftc-advertising-regulation#_ftnref21.

¹⁸³ Amazon case at 11.

¹⁸⁴ Amazon case at 11.

The court properly noted that it was incumbent upon the Commission to “establish, with evidence, a cognizable danger of a recurring violation.”¹⁸⁵

Similarly, in *FTC v. RCA Credit* (a Deception case), the court rejected the FTC’s use of 13(b)—in that case, accepting the permanent injunction but questioning the expansion of its scope:

The undisputed facts demonstrate that this is a proper case for permanent injunctive relief. However, the Court will defer ruling on the appropriate scope of an injunction (including whether, as the FTC requests, the injunction should include a broad fencing-in provision enjoining misrepresentations of material fact in connection with the sale of any goods and services) until after hearing evidence on the issue.¹⁸⁶

The reluctance of some courts to abet the FTC’s expansion of its use of fencing-in remedies to reach legitimate companies is reassuring—and affirms our belief as to what Congress intended in Section 13(b). Unfortunately, however, most parties do not proceed to ruinously expensive litigation with the Commission, and will accede to the demands of a consent order. This creates undue costs of both the first order (companies agreeing to remedies that are larger or more invasive than what a court would impose) and the second order (the systemic cost of companies settling cases they might otherwise litigate, all regulated entities losing the benefit of litigation, and the FTC having to do less rigorous analysis).

The FTC’s ability to threaten a permanent injunction, or to dramatically extend its scope beyond the practices at issue in a case, gives parties an inefficiently large incentive to settle in order to avoid the risk of the more draconian remedy. But, in doing so, parties end up opting in to consent orders that allow the FTC to evade any judicially enforced limits on the remedies it imposes, which is what the Commission *really* wants. Whatever the benefits to the agency from permanent injunctions, it arguably receives even more benefit from the ability to impose more detailed behavioral remedies than a court might permit (and to do so in the context of a consent order, the violation of which is subject to the lower burden of proving contempt rather than an initial violation).

The Commission’s general resistance to constraints upon its remedial discretion was aptly illustrated by its abrupt revocation, in 2012,¹⁸⁷ of its 2003 Policy Statement On Monetary Equitable Remedies in Competition Cases (commonly called the Disgorgement Policy Statement).¹⁸⁸ As Commissioner Ohlhausen noted in her dissent from the withdrawal of the policy:

Rescinding the bipartisan Policy Statement signals that the Commission will be seeking disgorgement in circumstances in which the three-part test heretofore utilized under the Statement is not met, such as where the alleged antitrust violation is not clear or where other remedies would be sufficient to address the violation.¹⁸⁹

Not only does this mean that parties in general are more likely to settle, but it also means that parties that are facing novel, untested antitrust theories are more likely to settle. This allows the Commission to expand its antitrust enforcement authority beyond judicially recognized conduct without risk of reversal by the courts.

Section 13(b) and the Commission’s disgorgement powers represent tremendous weapons to wield over the heads of investigative targets. Their expanding use to impose expansive or draconian remedies in cases involving non-fraudulent, legitimate companies and questionable legal theories is extremely troubling. Not only is this bad policy, it is also inconsistent with the spirit of the FTC Act, which was designed to find and punish actively fraudulent conduct, and to deter anticompetitive behavior that is not countervailed by pro-consumer benefits. But most of all, this gives the FTC greater ability to coerce companies that might otherwise litigate into settle-

¹⁸⁵ *Id.* at 11.

¹⁸⁶ *RCA Credit* case at 24.

¹⁸⁷ Fed. Trade Comm’n, *FTC Withdraws Agency’s Policy Statement on Monetary Remedies in Competition Cases; Will Rely on Existing Law* (Jul. 31, 2012), available at <https://www.ftc.gov/news-events/press-releases/2012/07/ftc-withdraws-agencys-policy-statement-monetary-remedies>.

¹⁸⁸ Fed. Trade Comm’n, Policy Statement On Monetary Equitable Remedies—Including in Particular Disgorgement and Restitution, in FEDERAL TRADE COMMISSION COMPETITION CASES ADDRESSING VIOLATIONS OF THE FTC ACT, THE CLAYTON ACT, OR THE HART-SCOTT-RODINO ACT (2003), available at <https://www.ftc.gov/public-statements/2003/07/policy-statement-monetary-equitable-remedies-including-particular>.

¹⁸⁹ Dissenting Statement of Commissioner Maureen K. Ohlhausen, *Commission’s Decision to Withdraw its Policy Statement on Monetary Equitable Remedies in Competition Cases* (Jul. 31, 2012), available at https://www.ftc.gov/sites/default/files/documents/public_statements/statement-commissioner-maureen-k.ohlhausen/120731ohlhausenstatement.pdf.

ments, pushing us further away from the Evolutionary Model and towards the Discretionary Model.

To correct these problems, at least two things should be done:

Recommendation: Limit Injunctions to the “Proper Cases” Intended by Congress

First, the Commission’s use of Section 13(b) remedies should be reevaluated in light of the law’s original purpose:

[O]ne class of cases clearly improper for awarding redress under Section 13(b): traditional substantiation cases, which typically involve established businesses selling products with substantial value beyond the claims at issue and disputes over scientific details with well-regarded experts on both sides of the issue. In such cases, the defendant would not have known *ex ante* that its conduct was “dishonest or fraudulent.” Limiting the availability of consumer redress under Section 13(b) to cases consistent with the Section 19 standard strikes the balance Congress thought necessary and ensures that the FTC’s actions benefit those that it is their mission to protect: the general public.¹⁹⁰

This same logic applies to a host of other types of cases, as well, including the Commission’s recent product design cases.¹⁹¹ Thus the tailoring of the Commission’s Section 13(b) powers should not stop merely with substantiation cases, but should extend, as a general principle, to any party that had not intentionally or recklessly engaged in conduct it should have known was dishonest or fraudulent. As Josh Wright noted in his dissent in the *Apple* product design case:

The economic consequences of the allegedly unfair act or practice in this case—a product design decision that benefits some consumers and harms others—also differ significantly from those in the Commission’s previous unfairness cases.

The Commission commonly brings unfairness cases alleging failure to obtain express informed consent. These cases invariably involve conduct where the defendant has intentionally obscured the fact that consumers would be billed. Many of these cases involve unauthorized billing or cramming—the outright fraudulent use of payment information. Other cases involve conduct just shy of complete fraud—the consumer may have agreed to one transaction but the defendant charges the consumer for additional, improperly disclosed items. Under this scenario, the allegedly unfair act or practice injures consumers and does not provide economic value to consumers or competition. In such cases, the requirement to provide adequate disclosure itself does not cause significant harmful effects and can be satisfied at low cost.

However, the particular facts of this case differ in several respects from the above scenario.¹⁹²

The same logic that undergirds former Commissioner Wright’s objection to the majority’s aggressive application of the UPS in *Apple* applies equally to the aggressive 13(b) remedies sought in similar cases.

Recommendation: Narrow Overly Broad “Fencing-in” Remedies

Similarly, the imposition of unreasonable behavioral demands—“fencing-in” of conduct beyond that at issue in the case—upon parties subject to FTC enforcement is problematic.

For instance, in *Fanning v. FTC*, the Commission imposed upon defendant John Fanning a requirement that the First Circuit characterized as “not reasonably related to [the alleged] violation.”¹⁹³ In 2009, Fanning founded *jerk.com*, a social networking website that controversially enabled users to nominate certain persons to

¹⁹⁰ Beales & Muris, *Striking the Proper Balance*, *supra* note 21, at 6.

¹⁹¹ 15 U.S.C. § 57(b)-(a)(2) and -(b).

¹⁹⁰ Beales & Muris, *Striking the Proper Balance*, *supra* note 21, at 6–7.

¹⁹¹ Fed. Trade Comm’n, *FTC Alleges Amazon Unlawfully Billed Parents for Millions of Dollars in Children’s Unauthorized In-App Charges* (Jul. 10, 2014), available at <https://www.ftc.gov/news-events/press-releases/2014/07/ftc-alleges-amazon-unlawfully-billed-parents-millions-dollars>; In the Matter of Apple Inc., FTC File No 112 3108, <https://www.ftc.gov/enforcement/cases-proceedings/112-3108/apple-inc> (2014); Fed. Trade Comm’n, *Google to Refund Consumers at Least \$19 Million to Settle FTC Complaint It Unlawfully Billed Parents for Children’s Unauthorized In-App Charges* (Sept. 4, 2014), available at <https://www.ftc.gov/news-events/press-releases/2014/09/google-refund-consumers-least-19-million-settle-ftc-complaint-it>.

¹⁹² Dissenting Statement of Commissioner Joshua D. Wright, In the Matter of Apple, Inc., FTC File No. 1123108, at 3 (Jan. 15, 2014), available at <https://goo.gl/ORCC9E>.

¹⁹³ *Fanning v. Fed. Trade Comm’n*, FTC File No. 15–1520, slip op. at 13 (May 9, 2016), available at <https://www.ftc.gov/system/files/documents/cases/051816jerkopinion.pdf>.

be “jerks.”¹⁹⁴ In issuing a variety of challenges to jerk.com’s business practices—including an alleged failure of the site to facilitate paid customers’ removal of negative information—the Commission additionally applied a “compliance monitoring” provision aimed directly at Fanning.¹⁹⁵ This provision required that Fanning “notify the Commission of . . . his affiliation with any new business or employment,” and submit information including the new business’s “address and telephone number and a description of the nature of the business” for a period of ten years.¹⁹⁶ Under the Commission’s cease and desist order, it did not matter whether Fanning engaged in reputation work, or started social media sites, or not—the requirement applied regardless of what type of work Fanning did and for whom he did it.¹⁹⁷

The First Circuit rebuked the Commission on this point:

When asked at oral argument, the Commission conceded that this provision would ostensibly require Fanning to report if he was a waiter at a restaurant. The only explanation offered by the Commission for this breadth is that it has traditionally required such reporting.¹⁹⁸

Moreover, the Commission cited a string of district court cases upholding similar provisions which the court characterized as “almost entirely bereft of analysis that might explain the rationale for such a requirement.”¹⁹⁹ While it is encouraging that the First Circuit saw fit to rein in the Commission, it is also apparent that the FTC frequently receives an extraordinary degree of deference from district courts, even when creating punitive provisions that bear little or no connection to challenged subject matter.

In order to deter the Commission from taking advantage of this frequent judicial deference by imposing such disconnected “fencing-in” remedies in non-fraud cases—which, of course, is compounded by the fact that most cases are never reviewed by courts at all—Congress should consider imposing some sort of minimal requirement that provisions in proposed orders and consent decrees be (i) reasonably related to challenged behavior, and (ii) no more onerous than necessary to correct or prevent the challenged violation.

This reform is also important to minimizing the daisy-chaining of consent decrees discussed in the next Section.²⁰⁰ As we note there, the ability of the Commission to bring a second enforcement action not premised on Section 5, but rather on the terms of a consent decree that is vaguely related to the challenged conduct creates several problems. The Commission’s ability to do this is magnified if the initial consent order already contains provisions that reach a broad range of conduct or that include a host of difficult conduct remedies that the company may even inadvertently violate.

Recommendation: Revive the 2003 Disgorgement Policy

Second, Congress should consider requiring the Commission to return to its previous disgorgement policy, or to propose targeted amendments to it. At a minimum, the Commission should be required to perform *some* process to examine the issue and take public comment on it. As Commissioner Ohlhausen noted in her dissent, objecting to the vote to rescind the Policy Statement:

I am troubled by the seeming lack of deliberation that has accompanied the withdrawal of the Policy Statement. Notably, the Commission sought public comment on a draft of the Policy Statement before it was adopted. That public comment process was not pursued in connection with the withdrawal of the statement. I believe there should have been more internal deliberation and likely public input before the Commission withdrew a policy statement that appears to have served this agency well over the past nine years.²⁰¹

¹⁹⁴ *Id.* at 2–3.

¹⁹⁵ *Id.* at 21–22.

¹⁹⁶ *Id.* at 22.

¹⁹⁷ Final Order, *Fanning v. Fed. Trade Comm’n*, FTC File No. 15–1520 (March 13, 2015), available at <https://www.ftc.gov/system/files/documents/cases/150325jerkorder.pdf>

¹⁹⁸ *Id.* at 23–24.

¹⁹⁹ *Id.* at 24.

²⁰⁰ *See infra* at 76.

²⁰¹ *Id.* at 2.

Consent Decree Duration & Scope

The Technological Innovation through Modernizing Enforcement (TIME) Act

Subcommittee Chairman Rep. Michael C. Burgess, M.D.'s (R-TX) bill (H.R. 5093)²⁰² would, in non-fraud cases, limit FTC consent orders to eight years—instead of the 20 years the FTC usually imposes. If the term runs five years or more, the FTC must reassess the de-cree after five years under the same factors required for setting the length of the consent decree from the outset:

1. The impact of technological progress on the continuing relevance of the consent order.
2. Whether there is reason to believe that the entity would engage in activities that violate this section without the consent order 8 years after the consent order is entered into by the Commission.

Shortening the length of consent decrees will do much to address the abuse of consent decrees, but it will not fix the underlying problems, as we discuss below.

Value of the Bill: Reducing the Abuse of Consent Decrees as De Facto Regulations

This reform is critical to reducing the FTC's use of consent decrees as effectively regulatory tools. It is entire commonplace for the FTC to impose the same twenty-year consent decree term and the same conditions (drawn from its quasi-regulatory reports) on every company, regardless of the facts of the case, the size of the company etc. Limiting the duration of consent decrees would not entirely stop abuse of consent decrees as a way to circumvent Section 5 rulemaking safeguards (because each consent decree is effectively a mini-rulemaking, which implements the FTC's pre-determined policy agenda), but it would at least limit the damage, and clear overly broad consent decrees more quickly.

The bill would also make it less likely that the FTC could daisy-chain additional enforcement actions—that is, bring a second enforcement action not premised on Section 5 (and therefore not even paying lip service to its requirements) but on the terms of a consent decree that is only vaguely related to the subsequent conduct. Such daisy-chaining has allowed enormous leverage in forcing settlements, since the FTC Act gives the Commission civil penalty authority only for violations of consent decrees (and rules), not Section 5 itself. Thus, the FTC gains the sledgehammer of potentially substantial monetary fines the second time around. It also allows the FTC to further extend the term of the consent decree beyond the initial 20 years—and potentially keep a company operating under a consent decree forever.

This is essentially what the FTC did to Google. First, in 2011, the FTC and Google settled charges that Google had committed an unfair trade practice in 2010 in by opting Gmail users into certain features of its new (and later discontinued) Buzz social network.²⁰³ A year later, the FTC imposed a \$22.5 million penalty against Google in settling charges that Google had violated the 2011 consent decree by misleading consumers by, essentially, failing to update an online help page that told users of Apple's Safari browser that they did not need to take further action to avoid being tracked, after a technical change made by *Apple* had rendered this statement untrue.²⁰⁴ The FTC's Press Release boasted "Privacy Settlement is the Largest FTC Penalty Ever for Violation of a Commission Order."²⁰⁵ The case raised major questions about the way the FTC understood its deception authority,²⁰⁶ none of which were dismissed because (a) Google, already being under the FTC's thumb and facing a potentially even-larger monetary penalty, was eager to settle the case, and (b) the FTC technically did not have to prove the normal elements of deception, such as the materiality of a help page seen by a tiny number of users, because it was enforcing the consent decree, not Section 5.

²⁰²The Technological Innovation through Modernizing Enforcement Act, H.R. 5118, 114th Cong. (2016) [hereinafter TIME Act], available at <https://www.congress.gov/bill/114th-congress/house-bill/5093/text>.

²⁰³Fed. Trade Comm'n, *FTC Charges Deceptive Privacy Practices in Googles Rollout of Its Buzz Social Network* (Mar. 30, 2011), available at <https://www.ftc.gov/news-events/press-releases/2011/03/ftc-charges-deceptive-privacy-practices-googles-rollout-its-buzz>.

²⁰⁴Fed. Trade Comm'n, *Google Will Pay \$22.5 Million to Settle FTC Charges it Misrepresented Privacy Assurances to Users of Apple's Safari Internet Browser* (Aug. 9, 2012) available at <https://www.ftc.gov/news-events/press-releases/2012/08/google-will-pay-225-million-settle-ftc-charges-it-misrepresented>.

²⁰⁵*Id.*

²⁰⁶See, e.g., *FTC's Google Settlement a Pyrrhic Victory for Privacy and the Rule of Law*, International Center for Law & Economics (Aug. 9, 2012), available at <http://www.laweconcenter.org/component/content/article/84-ftcs-google-settlement-a-pyrrhic-victory-for-privacy-and-the-rule-of-law.html>.

Perhaps most disconcertingly, the Commission's 2012 action against Google had precious little to do with the conduct that gave rise to its 2011 consent order. To be sure, the 2011 order was written in the broadest possible terms, arguably covering nearly every conceivable aspect of Google's business. But this just underscores the regulation-like nature of the Commission's consent orders, as well as the FTC's propensity to treat cases with dissimilar facts and dissimilar circumstances essentially the same. While that kind of result might be expected of a regulatory regime, it is inconsistent with the idea of case-by-case adjudication, which also puts paid to the idea that of a "common law of data security consent decrees":

In this sense the FTC's data security settlements aren't an evolving common law—they are a static statement of "reasonable" practices, repeated about 55 times over the years and applied to a wide enough array of circumstances that it is reasonable to assume that they apply to *all* circumstances. This is consistency. But it isn't the common law. The common law requires consistency of application—a consistent theory of liability, which, given different circumstances, means *inconsistent* results. Instead, here we have consistent results which, given inconsistent facts, means [] inconsistency of application.²⁰⁷

Recommendation: Allow Petitions for Appeal of Mooted Consent Decrees

Noticeably *not* addressed by this bill is the situation in which the FTC has found a company in violation of Section 5 for some practice (and imposed a consent decree for the violation), then lost in court on essentially the same doctrinal point. At a minimum, part of the reassessment of any consent decree should include assessing whether court decisions have called into question whether the original allegation actually violated Section 5. Ideally, the bill should also include a procedure by which the company subject to a consent decree could petition for review of its consent decree on these grounds.

Such an amendment should not be controversial, given that the FTC so rarely (if ever) litigates its consumer protection cases.

Other Process Issues

Open Investigations

The Start Taking Action on Lingering Liabilities (STALL) Act

Rep. Susan Brooks' (R-IN) bill (H.R. 5097)²⁰⁸ would automatically terminate investigations six months after the last communication from the FTC. Commission staff can keep an investigation alive either by sending a new communication to the target or the Commissioners can vote to keep the investigation open (without alerting the target). Current FTC rules allow the staff to inform targets that their investigation has ended, but does *not* require them to do so.²⁰⁹

Value of the Bill: Good Housekeeping, Reduces In Terrorem Effects of Lingering Investigations

This should be among the least controversial of the pending bills. It is simply a good house-keeping measure, ensuring that companies will not be left hanging in limbo after initial investigation-related communications from the FTC.

Closing open investigations could have several benefits.

First, in some circumstances, publicly traded companies may conclude that they are required to disclose the FTC's inquiry in their SEC filings.²¹⁰ That, in turn, can spark a media frenzy that could be as damaging to the company as whatever terms the FTC might impose in a consent decree—or at least seem to be less costly to managers who are more incentivized to care about the immediate performance of the company than the hassle of being subject to an FTC consent decree for the next

²⁰⁷ Manne & Sperry, *supra* note 52, at 13.

²⁰⁸ Start Taking Action on Lingering Liabilities Act, H.R. 5097, 114th Cong. (2016) [hereinafter STALL Act], available at <https://www.congress.gov/bills/114th-congress/house-bill/5097/text>.

²⁰⁹ Fed. Trade Comm'n, *Operating Manual: Chapter 3: Investigations*, 46 (last visited May 20, 2016), available at https://www.ftc.gov/sites/default/files/attachments/ftc-administrative-staff-manuals/ch03investigations_0.pdf (providing, in .3.7.4.5, that "[i]n investigations which have been approved by Bureau Directors, closing letters are ordinarily sent to both the applicant and the proposed respondent, with copies to their attorneys, if any[,] but not requiring such letters in any case).

²¹⁰ See, e.g., Deborah S. Birnbach, *Do You Have to Disclose a Government Investigation?*, *supra* note 99.

20 years.²¹¹ Making such disclosures can be particularly problematic if management intends to shop the company around for acquisition.

Presumably, a company that feels compelled to disclose an investigation in an SEC filing would, today, *eventually* feel justified in modifying the disclosure to indicate its belief that the investigation has concluded, given a long enough period of silence from the Commission. But this could take years, during which time the “lingering liability” could continue to damage the company. The bill (if it includes our proposed amendment, below) would give companies a clear indication whether or not they can modify their quarterly disclosures and inform shareholders and the general public that an investigation has concluded.

Second, giving subject companies repose after six months of silence from the FTC would allow management to focus on running their businesses. This could be especially critical for small companies.

Third, giving companies greater certainty in this way would reduce the leverage that staff may have to coerce companies into settling cases that might otherwise not be brought at all, or that companies might litigate. That means, in the first instance, moving closer to the optimal number of cases settled and, in the second instance, increasing the potential for litigation where it is warranted, which benefits everyone by allowing “the underlying criteria [of Section 5] to evolve and develop over time” through “judicial review,” as the Unfairness Policy Statement explicitly intends.²¹²

Fourth, holding target companies *in terrorem* may have other indirect costs besides driving companies to settle questionable cases. The longer an investigation lingers, or the longer it *could* linger (before the company can safely assume it is over), the more likely the company is to treat the FTC’s “recommended” best practices as effectively mandatory, regulatory requirements. This regulation-by-terror is impossible to quantify, but it is a very real concern. To the extent it happens, it contributes to transforming the FTC’s “inquisitorial powers” into a tool by which the FTC may treat its workshops and reports as de facto rulemakings, thus at least partially circumventing the Section 5 rulemaking safeguards.

Finally, the bill makes it harder for FTC staff to circumvent Bureau Director oversight—and thus avoid any possibility of alerting Commissioners. Current FTC rules allow an Initial Phase Investigation to be conducted for up to 100 hours of staff time, after which Staff must draft a memo and obtain approval from the Bureau Director to continue the investigation.²¹³ Today, the staff may be able to shoe-horn a new investigation into an old investigation for which they have already received Director approval, thus avoiding or forestalling having to seek new approval from the Bureau Director. One can imagine that this would be particularly appealing if the Commission’s majority—and thus also its Bureau Directors, who are appointed by the Chairman—has switched parties. This shoe-horning may be very easy to do given the breadth of the FTC’s investigations: one inquiry about questionable data security could very easily morph into another, potentially years later. The proposed bill would reduce this possibility by reducing the menu of available investigations from which staff could pick and choose. In other words, it would help to draw lines between old investigations and new ones. While this should not be a significant burden for the Staff, it should help to ensure that other internal decision-making safeguards are respected.

Recommendation: Bar Secret Votes as a Means of Evading the Bill

As drafted, the bill would allow the Commission to take a (non-public) vote to keep an investigation alive without the subject receiving additional communications. We can think of no reason to permit the Commission to hide the existence of a continuing investigation from its subject, however. In fact, although doing so requires a small price (an affirmative vote of the Commission), the price is so small that it is reasonable to expect that the exception would subsume the rule, and permit the Commission to evade the overall benefits of the proposed bill. Thus, we suggest amending section (2)(B) of the proposed bill, which authorizes an investigation to continue if “the Commission votes to extend the covered investigation before the ex-

²¹¹Notably, this also includes the potential for the FTC to bring additional enforcement actions premised on violating the terms of the consent decree, however attenuated the subsequent enforcement action might be, which is even easier than bringing an enforcement action premised directly on Section 5 (in that the FTC need not even purport to satisfy the requirements of Section 5). See *e.g.*, *United States v. Google, Inc.*, Case 5:12-cv-04177-HRL (N.D.Ca. 2012), available at <https://www.ftc.gov/news-events/press-releases/2012/08/google-will-pay-225-million-settle-ftc-charges-it-misrepresented>.

²¹²UPS, *supra* note 9.

²¹³Operating Manual at 9, § 3.2.1.1.

piration of such period,”²¹⁴ to also require the Commission to send a communication to the subject informing it of the vote. This would add no appreciable cost to the Commission’s ability to extend an investigation, but, unlike a non-public vote, it ensures that the subject is made aware of the extension.

This amendment would have the benefit of allowing the subject’s management to take *true* repose, knowing that an investigation had truly ended. Only then, for instance, would many managers feel comfortable revising a public securities disclosure about the company’s lingering potential liability. In short, this would allow companies to clear their good names and get on with the business of serving consumers.

Commissioner Meetings

The Freeing Responsible & Effective Exchanges (FREE) Act

Rep. Pete Olson’s (R–TX) bill (HR 5116)²¹⁵ would allow a bipartisan quorum of FTC Commissioners to meet confidentially under certain circumstances: no vote or agency action may be taken, the meeting must be FTC staff only, with a lawyer from the Office of General Counsel present, and the meeting must be disclosed publicly online. This would greatly empower other Commissioners by allowing them to meet with each other and with Commission staff—potentially without the Chairman, or without the Chairman having organized the meeting.

The bill does essentially the same thing as the FCC Process Reform Act of 2015 (H.R. 2583), which was so uncontroversial that it passed the House on a voice vote in November 2015.²¹⁶ Both bills would, for the affected agency, undo an unintended consequence of the Government in the Sunshine Act of 1976. That well-intentioned effort to bring transparency to agency decision-making in the aftermath of the Watergate scandal has had the perverse result of undermining the very purpose of multi-member commissions.

Value of the Bill: Restoring the Collegiality of the FTC

The Sunshine Act calls multi-member commissions “collegial bod[ies],”²¹⁷ but the effect of the law has been to greatly contribute to the rise of the Imperial Chairmanship, because the law not only requires that “disposing of” (*i.e.*, voting on) major items (*e.g.*, rulemakings or enforcement actions) be conducted in public meetings (organized by the Chairman), it also bars Commissioners from “jointly conduct[ing] . . . agency business” except under the Act’s tight rules. In effect, this makes it difficult for other Commissioners to coordinate without the Chairman.

The bill would continue to require that any “vote or any other agency action” be taken at meetings held under the Sunshine Act. This would ensure that the FTC generally continues to operate in full public view and according to valid process.

But the bill would allow Commissioners to meet privately, potentially without the Chairman present.

The benefits of such meetings are self-evident. They would encourage collegiality and facilitate bipartisan discussions, leading to a more open and inclusive process. They would also provide opportunities for minority commissioners to be apprised earlier in the process when the Commission is considering various actions, from investigations to issuing consent decrees.

The fact that the Energy & Commerce Committee has already vetted these reforms for the FCC, and that the full House has already voted for them as part of a larger FCC reform package, should make passage of this bill straightforward.

Recommendation: Ensure that Two of Three Commissioners Can Meet

As amended by the bill, 15 U.S.C. § 552b(d)(2)(A) would require that the group consist of at least three or more Commissioners. This would have the perverse result of rendering the bill useless at present, when the Commission has only three Commissioners—because all three would have to be present for a meeting. We recommend simply striking this subsection, so that, on a three-member commission, the Democrat and Republican commissioners can meet without the Chairman.

Part III Litigation

Numerous commentators have raised serious questions about the FTC’s use of adjudication under Part III of the FTC’s Rules. Commissioner Wright put it best in a 2015 speech:

²¹⁴ STALL Act, *supra* note 208.

²¹⁵ The Freeing Responsible and Effective Exchanges Act, H.R. 5116, 114th Cong. (2016) [hereinafter FREE Act], available at <https://www.congress.gov/bill/114th-congress/house-bill/5116/text>.

²¹⁶ Federal Communications Commission Process Reform Act of 2015, H.R. 2583, 114th Cong. (2016), available at <https://www.congress.gov/bill/114th-congress/house-bill/2583/actions>

²¹⁷ 5 U.S.C. § 552b(a)(1) & (3).

Perhaps the most obvious evidence of abuse of process is the fact that over the past two decades, the Commission has almost exclusively ruled in favor of FTC staff. That is, when the ALJ agrees with FTC staff in their role as Complaint Counsel, the Commission affirms liability essentially without fail; when the administrative law judge dares to disagree with FTC staff, the Commission almost universally reverses and finds liability. Justice Potter Stewart's observation that the only consistency in Section 7 of the Clayton Act in the 1960s was that "the Government always wins" applies with even greater force to modern FTC administrative adjudication.

Occasionally, there are attempts to defend the FTC's perfect win rate in administrative adjudication by attributing the Commission's superior expertise at choosing winning cases. And don't get me wrong—I agree the agency is pretty good at picking cases. But *a 100 percent win rate is not pretty good; Michael Jordan was better than pretty good and made about 83.5 percent of his free throws during his career, and that was with nobody defending him. One hundred percent isn't Michael Jordan good; it is Michael Jordan in the cartoon movie "Space Jam" dunking from half-court good.* Besides being a facially implausible defense—the data also show appeals courts reverse Commission decisions at four times the rate of federal district court judges in antitrust cases suggests otherwise. This is difficult to square with the case-selection theory of the FTC's record in administrative adjudication.²¹⁸

Former FTC Chairman Terry Calvani provides an apt summary of empirical research on the FTC's perfect win rate.²¹⁹ He notes FTC practitioner David Balto's study of eighteen years of FTC litigation, in which "the FTC has never found for the respondent and has reversed all ALJ decisions finding for the respondent."²²⁰ Balto concluded "there appears to be a lack of impartiality by the Commission that really undermines the credibility of the process, and I think that makes it more difficult for the FTC to effectively litigate tough cases and get the court of appeals to support [its] decisions going forward."²²¹

We recommend that Congress consider one of two structural reforms.

Recommendation: Separate the FTC's Enforcement & Adjudicatory Functions

Former Chairman Calvani proposes that

the FTC be reorganized to separate the prosecutorial and adjudicatory functions. The former would be vested in a director of enforcement appointed by and serving at the pleasure of the president. Commissioners would hear the cases brought before the agency. This model is not alien to American administrative law and independent agencies. Labor complaints are evaluated and issued by National Labor Relations Board ("NLRB") regional directors. Administrative hearings are held before ALJs, and appeals from the ALJs are vested in the NLRB. Similarly, the Securities and Exchange Commission's ("SEC's") prosecutorial functions are vested in the Division of Enforcement while administrative hearings are held before ALJs and appeals are vested in the SEC.

This change in organization would eliminate the existence or perception of unfairness associated with the same commissioners participating in both the decision to initiate a case and in its ultimate resolution. It would also make the decision to prosecute more transparent. One person would be responsible for the agency's enforcement agenda.²²²

Calvani notes that this would not significantly alter the responsibility of the powers of Commissioners, since "the power of a commissioner is relatively slight. The only real power of a commissioner is a negative one: blocking an enforcement initiative."²²³ But it would "rather dramatically, [the responsibilities] of the chair."²²⁴ In our view, this is a bug, not a feature.

²¹⁸ Joshua D. Wright, Commissioner, Fed. Trade Comm'n, *Remarks at the Global Antitrust Institute Invitational Moot Court Competition*, 16–17 (Feb. 21, 2015) (emphasis added), available at https://www.ftc.gov/system/files/documents/public_statements/626231/150221judgingantitrust-1.pdf.

²¹⁹ Terry Calvani & Angela M. Diveley, *The FTC At 100: A Modest Proposal for Change*, 21 GEO. MASON L. REV. 1169, 1178–82 (2014).

²²⁰ *Id.* at 1179 (quoting David A. Balto, *The FTC at a Crossroads: Can It Be Both Prosecutor and Judge?*, LEGAL BACKGROUNDER (Wash. Legal Found.) (Apr. 23, 2013), 1).

²²¹ Wash. Lgl Found., *FTC's Administrative Litigation Process: Should the Commission Be Both Prosecutor and Judge?*, YOUTUBE (Mar. 11, 2014), <http://youtu.be/a9zvyDr4a-Y>, at 9:24.

²²² Calvani & Diveley, *supra* note 219, at 1184.

²²³ *Id.* at 1185.

²²⁴ *Id.* at 1184.

Recommendation: Abolish or Limit Part III to Settlements

More fundamentally, Congress should re-examine the continued need for Part III as an alternative to litigation in Federal court. There are important differences between adjudications that originate in Part III proceedings as opposed to those that originate in Article III proceedings. Foremost, the selection of venue is an important determinant of the FTC's likelihood of success as well as the level of deference it will enjoy. Defendants will likewise see major differences between litigation in the different fora: from the range of discovery options available to the range and sort of materials considered by the tribunal (*e.g.*, through amicus briefs). And, perhaps most important, the different venues each will create different legal norms and rules binding upon parties to future proceedings.

There is also a question regarding to what extent Part III proceedings are more than a mere formality. On the one hand, the FTC's Administrative Law Judge takes his job seriously, and has reversed the Commission in, most notably, two recent consumer protection decisions.²²⁵ However, on the other hand, the Commission *always* reverses decisions of the ALJ that find against it.²²⁶ Which leads to an important question: if the Commission is simply going to reverse its ALJ anyway what is the point of having an ALJ?

Even the threat of Part III litigation has a significant effect in coercing defendants to settle with the FTC during the investigation stage—not merely because of the direct financial costs of two additional rounds of litigation (first before the ALJ and then before the full Commission) prior to facing an independent Article III tribunal, but also because the Part III process drags out the other, less tangible but potentially far greater costs to the company in reputation and lost management attention. The threat of suffering two rounds of bad press before going to Federal court (or at least one, if the ALJ rules for a defendant but the Commission reverses) may persuade some defendants who wouldn't otherwise to settle. Thus, the current operation of Part III rarely, if ever, serves to actually advance the interests of a fair hearing on disputed issues, and is more a tool to coerce settlements.

Congress could end this dynamic by requiring the FTC to litigate in Federal court while potentially still preserving Part III for the supervision of the settlement process and discovery. This is not a novel idea, nor would it be disruptive to the FTC as the Commission has had independent litigating authority since the 1970s.²²⁷ The Smarter Act (H.R. 2745) effectively abolishes Part III with respect to merger cases, by requiring the FTC to bring Clayton Act Section 7 cases (for preliminary injunctions to stop mergers) in Federal court under the same procedures as the Department of Justice.²²⁸ This bill passed by a vote of 230 to 170.²²⁹

Finally, those who might object that abolishing Part III would hamstring the agency should take comfort in the fact that the FTC uses Part III so rarely anyway. Abolishing Part III will not bury the FTC in an avalanche of litigation in Federal court. At most it would marginally increase the willingness of companies to resist the siren song of settlement, thus resulting in slightly more litigation (and perhaps also slightly more cases simply abandoned by staff, if they do not think they could win). But this is a trivial price to pay in comparison with the benefit of getting more judicial review and consistent enforcement standards and judicial standards of review. The difference between essentially no litigation and *some* litigation is the key difference between the Discretionary and Evolutionary Models.

Recommendation: Allow Commissioners to Limit the Use Part III

The least draconian reform would be to empower one or two Commissioners to insist that the Commission bring a particular complaint in Federal court. This would allow them to steer cases out of Part III either because they are doctrinally significant or because the Commissioners fear that, unless the case goes to Federal court, the defendant will simply settle, thus denying the entire legal system the benefits of litigation in building the FTC's doctrines. In particular, it would be a way for Commissioners to act on the dissenting recommendations of staff, particularly the

²²⁵ In the Matter of LabMD, Inc., FTC File No. 102 3099 (May 16, 2016), available at <https://www.ftc.gov/enforcement/cases-proceedings/102-3099/labmd-inc-matter>; POM Wonderful LLC v. FTC, 777 F.3d 478 (D.C. Cir. 2015).

²²⁶ Joshua D. Wright, *Recalibrating Section 5: A Response to the CPI Symposium*, CPI ANTI-TRUST CHRONICLE, 4 (2012).

²²⁷ Elliott Karr, *Essay: Independent Litigation Authority and Calls for the Views of the Solicitor General*, 77 GEO. WASH. L. REV. 1080, 1090–91 (2009).

²²⁸ Standard Merger and Acquisition Reviews Through Equal Rules Act of 2015, H.R. 2745, 114th Cong. (2015), available at <https://www.congress.gov/bills/114th-congress/house-bill/2745> [hereinafter SMARTER Act].

²²⁹ U.S. House of Rep., *Final Vote Results For Roll Call 137* (Mar. 23, 2016) available at <http://clerk.house.gov/evs/2016/roll137.xml>

Bureau of Economics, about cases that are problematic from either a legal or policy perspective.

Standard for Settling Cases

No Bill Proposed

Recommendation: Set a Standard for Settling Cases Higher than for Bringing Complaints

Currently there is no standard for settling cases. The Commission simply applies the “reason to believe” standard set forth in Section 5(b)—and very often combines the vote as to whether to bring the complaint with the vote on whether to settle the matter, when the staff has already negotiated the settlement during the investigation process (because of the enormous leverage it has in this process, as we explain above). As Commissioner Wright has noted, “[w]hile the Act does not set forth a separate standard for accepting a consent decree, I believe that threshold should be at least as high as for bringing the initial complaint.”²³⁰ Reform in this area is especially critical if Congress chooses not to enact the “preponderance of the evidence” standard for issuing complaints.²³¹

While it would certainly be an improvement to adopt even a “preponderance of the evidence” standard for the approval of consent decrees (relative to the status quo), we believe that this should be the standard for the approval of *complaints*, and that approval of *consent decrees* should be even higher (although, as we emphasize above, the “preponderance of the evidence” is not a particularly high standard).²³² The standard and process required by the Tunney Act for antitrust settlements would be a good place to begin. That act requires the FTC to file antitrust consent decrees with a Federal court, and requires the court make the following determination:

Before entering any consent judgment proposed by the United States under this section, the court shall determine that the entry of such judgment is in the public interest. For the purpose of such determination, the court shall consider:

(A) the competitive impact of such judgment, including termination of alleged violations, provisions for enforcement and modification, duration of relief sought, anticipated effects of alternative remedies actually considered, whether its terms are ambiguous, and any other competitive considerations bearing upon the adequacy of such judgment that the court deems necessary to a determination of whether the consent judgment is in the public interest; and

(B) the impact of entry of such judgment upon competition in the relevant market or markets, upon the public generally and individuals alleging specific injury from the violations set forth in the complaint including consideration of the public benefit, if any, to be derived from a determination of the issues at trial.²³³

If anything, a standard for settlements should require *more* analysis than this, as the Tunney Act has been relatively ineffective. In particular, any approach based on the Tunney act should allow third parties to intervene to challenge the FTC’s assertions about the public interest.²³⁴ This reform could go a long way toward inspiring the agency to perform more rigorous analysis.

Competition Advocacy

The FTC occupies a unique position in its role as the Federal government’s competition scold. Despite the absence of direct legal authority over federal, state and local actors (which limits the efficacy of competition advocacy efforts), some have argued that “the commitment of significant Commission resources to advocacy is nonetheless warranted by the past contributions of competition authorities to the reevaluation of regulatory barriers to rivalry, and by the magnitude and durability of anticompetitive effects caused by public restraints on competition.”²³⁵

²³⁰ Dissenting Statement of Commissioner Joshua D. Wright, In the Matter of Nomi Technologies, Inc., FTC. File No. 132 3251 (Sept. 3, 2015), 2, available at https://www.ftc.gov/system/files/documents/public_statements/638371/150423nomiwrightstatement.pdf.

²³¹ See, *supra*, at 18.

²³² See *infra* at 18.

²³³ 15 U.S.C. § 16(b)(1).

²³⁴ The act currently provides that “Nothing in this section shall be construed to require the court to conduct an evidentiary hearing or to require the court to permit anyone to intervene.” 15 U.S.C. § 16(b)(2).

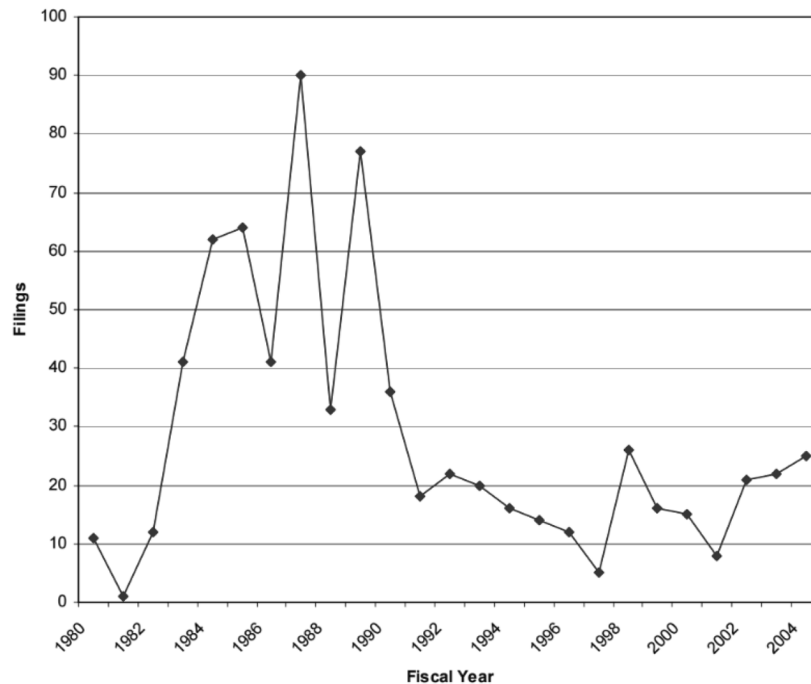
²³⁵ Ernest Gellhorn, & William E. Kovacic, *Analytical Approaches and Institutional Processes for Implementing Competition Policy Reforms by the Federal Trade Commission* (Dec. 12, 1995),

The FTC performs two different, but related, kinds of “competition advocacy”:

1. *Competition advocacy litigation*: The Bureau of Competition occasionally brings antitrust cases against nominally public bodies that the FTC believes are ineligible for state action immunity, either because they are effectively operating as marketplace participants (e.g., state-run hospitals) or because state-created regulatory boards have been so completely coopted by private actors that they operate as private cartels, lacking sufficiently clear statement of legislative intent to maintain their state action immunity.
2. *Competition advocacy filings*: The Office of Policy Planning files comments with state, local, tribal and Federal lawmakers and regulators as to the impact of proposed (or existing) legislation or regulation upon consumers and competition.

In 2004, James Cooper, Paul Pautler and Todd Zywicki (all FTC veterans) provided an empirical basis for comparing the FTC’s level of activity on competition advocacy filings.²³⁶ Their analysis included this chart:

FTC Advocacy Filings, 1980 to 2004²³⁷



Since 2009, the FTC has averaged just nineteen competition advocacy filings per year.²³⁸ On high-tech matters, the Commission has been particularly inactive, making just four filings on ride-sharing,²³⁹ four on direct sale of cars to consumers (i.e., online),²⁴⁰ and none on house-sharing. It has also made few other broadly tech-relevant filings. See https://www.ftc.gov/system/files/documents/public_statements/418071/951212compolicy.pdf.

²³⁶James C. Cooper, Paul A. Pautler & Todd J. Zywicki, *Theory and Practice of Competition Advocacy at the FTC* at 3, available at https://www.ftc.gov/sites/default/files/documents/public_events/FTC%2090th%20Anniversary%20Symposium/040910zywicki.pdf.

²³⁷*Id.*

²³⁸A search of the FTC’s Advocacy Filings reveals that between January 2009 and January 2016, 115 separate documents have been filed. See Fed Trade Comm’n, *Advocacy Filings* available at <https://www.ftc.gov/policy/advocacy/advocacy-filings>.

²³⁹Fed Trade Comm’n, “Transportation” Advocacy Filings, available at https://www.ftc.gov/policy/advocacy/advocacy-filings?combine=&field_matter_number_value=&field_advocacy_docu

Continued

online),²⁴⁰ and none on house-sharing. It has also made few other broadly tech-related miscellaneous filings to other Federal agencies on privacy and data security, vehicle-to-vehicle communications, mobile financial services, and the National Broadband Plan.

The FTC held a workshop on the sharing economy in June 2015,²⁴¹ but has since missed the opportunity to do significant competition advocacy work in the area, despite growing protectionist state and local regulation aimed at upstarts like Uber, Lyft, Airbnb and others. Recent legislation in Austin, Texas, is sadly illustrative. An Austin City Council ordinance,²⁴² essentially regulating ride-sharing services out of existence, was approved by (the few) voters who showed up to vote in a referendum.²⁴³ This type of overly broad law regulating innovative technology is exactly the sort of thing the FTC should be taking initiative to advocate against, and it is unfortunate that, in the face of it, the FTC's competition advocacy has receded.

By contrast, in the early 2000s, OPP's State Action Task Force and Internet Task Force made a concerted effort to challenge anticompetitive state and local regulations that hindered online commerce through litigation, testimony and comments. The FTC started several campaigns, including one challenging rules making it harder to participate in e-commerce. Unlike the current Commission's stunted approach, the early 2000s FTC started with a workshop,²⁴⁴ released reports explaining the problem the FTC's planned approach,²⁴⁵ and then went on to systematically challenge e-commerce-related regulations (among other things) inconsistent with consumer welfare. Filings included:

- Comment on Ohio legislation to allow direct shipment of wine to Ohio consumers;²⁴⁶ and on similar New York legislation;²⁴⁷
- Congressional Testimony regarding online wine sales;²⁴⁸
- Comment on Arkansas legislation regarding online contact sales;²⁴⁹ and
- Comment on Connecticut regulation of contact sales.²⁵⁰

ment terms tid=5283&field date value%5Bmin%5D%5Bdate%5D=January%2C+2009&field date value%5Bmax%5D%5Bdate%5D=January%2C+2016&items per page=100.

²⁴⁰ Fed Trade Comm'n, "Automobiles" Advocacy Filings, available at <https://goo.gl/lq9ACP>.

²⁴¹ Fed. Trade Comm'n, The "Sharing" Economy: Issues Facing Platforms, Participants, and Regulators (Jun. 9, 2015), available at <https://www.ftc.gov/news-events/events-calendar/2015/06/sharing-economy-issues-facing-platforms-participants-regulators>

²⁴² Austin, Texas, Ordinance No. 20151217-075 (2015), available at <http://www.austintexas.gov/edims/document.cfm%3Fid=245769>.

²⁴³ Jared Meyer, *The Reverse of Progress. Austin's new rules strangle Uber, Lyft—and the ride-sharing economy*, U.S. NEWS & WORLD REPORT (May 18, 2016), available at <http://www.usnews.com/opinion/articles/2016-05-18/austins-very-un-progressive-example-on-uber-and-lyft>.

²⁴⁴ Fed. Trade Comm'n Workshop, Possible Anticompetitive Efforts to Restrict Competition on the Internet, Oct. 8–10, 2002, available at <https://www.ftc.gov/news-events/events-calendar/2002/10/possible-anticompetitive-efforts-restrict-competition-internet>.

²⁴⁵ FED. TRADE COMM'N, REPORT OF THE STATE ACTION TASK FORCE (2003), available at https://www.ftc.gov/sites/default/files/documents/advocacy_documents/report-state-action-task-force/stateactionreport.pdf; FED. TRADE COMM'N, POSSIBLE ANTICOMPETITIVE BARRIERS TO E-COMMERCE: WINE (2003), 3 available at https://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-staff-report-concerning-possible-anticompetitive-barriers-e-commerce-wine/winereport2.pdf; FED. TRADE COMM'N, POSSIBLE BARRIERS TO E-COMMERCE: CONTACT LENSES: A REPORT FROM THE STAFF OF THE FEDERAL TRADE COMMISSION (Mar. 29, 2004), available at https://www.ftc.gov/sites/default/files/documents/advocacy_documents/possible-anticompetitive-barriers-e-commerce-contact-lenses-report-staff-ftc/040329clreportfinal.pdf.

²⁴⁶ Comment on Proposed Direct Shipment Legislation of the Federal Trade Commission to the Ohio State Senate (2006), available at https://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-staff-comment-honorable-eric-d.fingerhut-concerning-ohio-s.b.179-allow-direct-shipment-wine-ohio-consumers/v060010commentreohiosb179directshipmentofwine.pdf

²⁴⁷ *Letter of the Federal Trade Commission regarding Assembly bill 9560-A, Senate bills 6060-A and 1192 to the New York State legislature (2004)*, https://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-staff-comment-honorable-william-magee-et-al.concerning-new-york.b.9560-s.b.606-and-s.b.1192-allow-out-state-vendors-ship-wine-directly-new-york-consumers/v040012.pdf

²⁴⁸ Prepared Statement of Todd Zywicki, Fed. Trade Comm'n, before the Subcommittee on Commerce, Trade, and Consumer Protection, Committee on Energy and Commerce United States House of Representatives (Oct. 13, 2003), available at https://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-statement-u.s.house-representatives-energy-and-commerce-concerning-e-commerce-wine-sales-and-direct-shipment/031030ecommercewine.pdf

²⁴⁹ *Letter of the Federal Trade Commission regarding Arkansas HB 2286 to the Arkansas House of Representatives (2015)*, available at https://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-staff-comment-honorable-doug-matayo-concerning-arkansas-h.b.2286-and-fairness-contact-lens-consumers-act-and-contact-lens-rule/041008matayocomment.pdf

²⁵⁰ Comments of the Staff of the Federal Trade Commission In Re: Declaratory Ruling Proceeding on the Interpretation and Applicability of Various Statutes and Regulations Concerning

The current FTC has many ripe targets for public interest advocacy around the Nation as incumbents are, predictably, using regulation to try to stop Internet- and app-based competition, especially disruptive new “sharing economy” business models.

Value of the Idea: Competition Advocacy Is the Most Cost-Effective Way to Serve Consumers

As Cooper, Pautler & Zywicki explain:

The economic theory of regulation (“ETR”) posits that because of relatively high organizational and transaction costs, consumers will be disadvantaged relative to businesses in securing favorable regulation. This situation tends to result in regulations—such as unauthorized practice of law rules or per se prohibitions on sales-below-cost—that protect certain industries from competition at the expense of consumers. Competition advocacy helps solve consumers’ collective action problem by acting within the political system to advocate for regulations that do not restrict competition unless there is a compelling consumer protection rationale for imposing such costs on citizens. Furthermore, advocacy can be the most efficient means to pursue the FTC’s mission, and when antitrust immunities are likely to render the FTC impotent to wage ex post challenges to anticompetitive conduct, advocacy may be the only tool to carry out the FTC’s mission.²⁵¹

Competition advocacy is probably the most cost-effective way the FTC can promote consumer welfare. Anticompetitive practices and agreements backed up by the power of the state are much less likely to be corrected by the power of competition than those that exist in the marketplace, and antitrust law cannot be used to remove such barriers to competition. The only way for the FTC to even get at such conduct is through its competition advocacy arm.

Recommendation: Clarify Section 6(f) & the FTC May File Unsolicited Comments

The FTC currently relies on Sections 6(a) (information gathering) and 6(f) (issuance of reports) as the basis for its competition advocacy filings.²⁵² But as discussed above,²⁵³ Section 6(f) could be read to allow the FTC to make recommendations for legislation only to Congress, not to states or local governments. This is the kind of small discontinuity between the statute’s plain meaning and the agency’s practice (on an issue that enjoys broad bipartisan support) that should be addressed by Congress in regular reauthorization.

In the same vein, we gather that, if only by standing convention, the FTC does not file comments with state and local lawmakers or regulators unless invited to do so by someone on the relevant body. This is undoubtedly well-intentioned, perhaps grounded in some kind of sense of federalism, but it may have the perverse result of denying consumers the benefit of the FTC’s competition-advocacy work where it is most needed: when state regulators are so captured by incumbents, or otherwise blinded to the benefits of new technologies, that they will resent the FTC’s comment as an intrusion upon their decision-making.

We urge Congress to kill two birds with one stone by amending Section 6(f) to add the following bolded text (and, for clarity’s sake, roman numeral subsection numbers):

To (i) make public from time to time such portions of the information obtained by it hereunder as are in the public interest; and to (ii) make annual and special reports to the Congress and to submit therewith recommendations for additional legislation; **and to (iii) file recommendations for legislation or regulatory action with state, local, tribal and Federal bodies;** and to (iv) provide for the publication of its reports and decisions in such form and manner as may be best adapted for public information and use.

the Sale of Contact Lenses (2002), available at https://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-staff-comment-connecticut-board-examiners-opticians-intervenore-declaratory-ruling-proceeding/v020007.pdf

²⁵¹ Cooper, Pautler & Zywicki, *Theory and Practice of Competition Advocacy at the FTC* *supra* note 236, at 2.

²⁵² See, e.g., *id.* at 1, n.3:

The legal authority for competition advocacy is found in Section 6 of the FTC Act, which allows the FTC to “gather and compile information” that concerns persons subject to the FTC Act, and “to make public such portions of the information obtained” that are “in the public interest.”

(Quoting 15 U.S.C. § 46(a), (f) (2005)).

²⁵³ See *supra* 61.

Recommendation: Create an Office of Bureau of Competition Advocacy with Dedicated Funding

The FTC's Competition advocacy *filing* function has languished, in part, because while competition advocacy *litigation* resides inside the Bureau of Competition, the filings are primarily the responsibility of the Office of Policy Planning (OPP), a relatively tiny organization attached to the Chairman's office, which has a staff of just over a dozen compared to 285 for the Bureau of Competition, 331 for the Bureau of Consumer Protection, and 114 for the Bureau of Economics.²⁵⁴

Congress should seriously consider creating an independent office of Competition Advocacy, which would manage competition-advocacy filings, and share joint responsibility for competition-advocacy litigation with the Bureau of Competition. In particular, this would mean giving this new Bureau a line item in the FTC's budget.

Recommendation: In the Alternative, Reconstitute the Task Force

As noted above, the Internet Task Force, which was spun off from the broader State Action Task Force, had considerable effect through its research, reports, and associated filings. A standing Task Force of this nature could provide dividends by picking up where the Sharing Economy Workshop left off and studying the effects of regulation on the sharing economy around the Nation. A well-done report could then be followed by strategic litigation, amicus briefs, and other filings in order to promote sound public policy and combat the Internet-age protectionism that is slowing down innovation and competition and the attendant benefit to consumers.

Expanding FTC Jurisdiction

Section 5 of the FTC Act empowers the Commission to prevent unfair and deceptive acts and practices by nearly all American businesses (and business people). The exceptions are few: "banks, savings and loan institutions . . . , Federal credit unions . . . , common carriers subject to the Acts to regulate commerce, air carriers and [certain meat packers and stock-yards]. . . ." One important limitation is that the FTC Act does not expressly give the Commission jurisdiction over nonprofit organizations. Nevertheless, courts have held that nonprofit status is not in itself sufficient to exempt an organization from FTC jurisdiction.²⁵⁵ In *Cal Dental Ass'n v. FTC*, the Supreme Court noted that the FTC has jurisdiction over both "an entity organized to carry on business for its own profit" . . . [as well as] one that carries on business for the profit 'of its members.'²⁵⁶ Thus, various types of nonprofits—notably trade associations—can be reached by the FTC *depending on their activities*, but "purely charitable" organizations remain outside of the FTC's enforcement purview.²⁵⁷

Subcommittee Democrats have revived two sensible proposals from 2008 to expand the FTC's jurisdiction. Both have long enjoyed bipartisan support, and have been endorsed by the Commission under both Republican and Democratic chairmen.

FTC Jurisdiction over Common Carriers

The Protecting Consumers in Commerce Act of 2016

Jerry McNeerney's (D-CA) bill (H.R. 5239)²⁵⁸ would allow the FTC to regulate common carriers currently regulated by the Federal Communications Commission. In particular, this would ensure that the FTC and FCC have dual jurisdiction over broadband—effectively restoring the jurisdiction the FTC lost when the FCC "reclassified" broadband in 2015.

The FCC recently issued a controversial NPRM proposing privacy and data security rules for broadband that are significantly different from the approach the FTC has taken. This bill would moot the need for new FCC privacy and data security rules as a "gap filler." The bill would also allow the FTC to police net neutrality concerns, interconnection and other broadband practices (to the extent it finds un-

²⁵⁴Cf. Fed. Trade Comm'n, Federal Trade Commission Office of Policy Planning Organizational Chart, <https://www.ftc.gov/system/files/attachments/office-policy-planning/opp-org-chart-may2016.pdf>; Fed. Trade Comm'n, Shutdown of Federal Trade Commission Operations Upon Failure of the Congress to Enact Appropriations, <https://www.ftc.gov/system/files/attachments/office-executive-director/130925ftcshutdownplan.pdf>.

²⁵⁵See, e.g., *Community Blood Bank v. FTC*, 405 F.2d 1011 (8th Cir. 1969).

²⁵⁶*Cal. Dental Ass'n v. FTC*, 526 U.S. 756, 766 (1999).

²⁵⁷See *Statement of William C. Macleod, Dir. of FTC Bureau of Consumer Protection, Before The U.S. House of Representatives Committee on Energy & Commerce; Subcommittee on Transportation & Hazardous Materials; Hearing On Deceptive Fundraising By Charities* (Jul. 28, 1989), available at <http://www.freespeechcoalition.org/macleod.htm>.

²⁵⁸Protecting Consumers in Commerce Act of 2016, H.R. 5239, 114th Cong. (2016), available at <https://www.congress.gov/bill/114th-congress/house-bill/5239/text>.

fair or deceptive practices) even if the FCC's Open Internet Order fails in pending litigation.

Value of the Bill: Reclassification of Broadband by the FCC Should Not Remove FTC Jurisdiction

There has long been unusual bipartisan agreement on ending the common carrier exemption. This was proposed by Sen. Byron Dorgan's proposed FTC Reauthorization Act of 2002,²⁵⁹ and supported by Republican Commissioner Thomas Leary and Democrat Commissioner Sheila Anthony.²⁶⁰ Sen. Dorgan last proposed the same reform in 2008.²⁶¹ More recently, in 2015, Democrat Chairman Edith Ramirez and Republican Commissioner Josh Wright supported this reform.²⁶²

Section 5 jurisdiction excludes "common carriers subject to the Acts to regulate commerce."²⁶³ The bill simply edits the definition of "Acts to regulate commerce" in Section 4 to remove the Communications Act.²⁶⁴ Thus, the FTC *could* regulate common carriers regulated by the FCC but *not* transportation common carriers.

Former Commissioner Joshua Wright summarized the many advantages of keeping the FTC as a cop on the broadband beat:

The FTC has certain enforcement tools at its disposal that are not available to the FCC. Unlike the FCC, the FTC can bring enforcement cases in Federal district court and can obtain equitable remedies such as consumer redress. The FCC has only administrative proceedings at its disposal, and rather than obtain court-ordered consumer redress, the FCC can require only a "forfeiture" payment. In addition, the FTC is not bound by a one-year statute of limitations as is the FCC. The FTC's ability to proceed in Federal district court to obtain equitable remedies that fully redress consumers for the entirety of their injuries provides comprehensive consumer protection and can play an important role in deterring consumer protection violations.²⁶⁵

Recommendation: Pass the Protecting Consumers in Commerce Act to End the Exemption for Telecom Common Carriers

Ending the common carrier exemption for telecom companies is long overdue. "As the telecommunications and Internet industries continue to converge, the common carrier exemption is likely to frustrate the FTC's efforts to combat unfair or deceptive acts and practices and unfair methods of competition in these interconnected markets."²⁶⁶ Moreover, the uncertainty surrounding the application of the exemption to new technologies, as well as the long-standing uncertainty around application of the exemption to non-common-carrier activities carried out by common carriers introduce needless administrative costs.

Recommendation: Require the FCC to Terminate Its Privacy Rulemaking

With respect to the common carrier exception, the fortunes of the FTC are tied to those of the FCC; adopting optimal policy for one requires adopting complimentary policy for the other. The conclusions above are complicated by the FCC's ongoing efforts to exercise the *exclusive* authority it claimed when it reclassified Internet service providers as common carriers, particularly with respect to privacy and simi-

²⁵⁹ Federal Trade Commission Reauthorization Act of 2002, S. 2946, 104th Cong. (2002), available at <https://www.congress.gov/bill/107th-congress/senate-bill/2946/text>.

²⁶⁰ *Additional Statement of Commissioner Thomas B. Leary, Hearing Before the H. Subcomm. on Commerce, Trade and Consumer Protection of the H. Comm. on Energy and Commerce*, 108th Cong. (2003), available at https://www.ftc.gov/sites/default/files/documents/public_statements/prepared-statement-federal-trade-commission-reauthorization/030611learyhr.pdf; Federal Trade Commission Testifies Before Senate in Support of Reauthorization Request for Fiscal Years 2003 to 2005, available at <https://www.ftc.gov/es/node/63553>.

²⁶¹ Federal Trade Commission Reauthorization Act of 2008, S. 2831 § 14, 110th Cong. (2008), available at <https://www.govtrack.us/congress/bills/110/s2831/text>.

²⁶² *Prepared Statement of Commissioner Joshua D. Wright, Federal Trade Commission: Wrecking the Internet to Save It? The FCC's Net Neutrality Rule Before the H. Comm. on the Judiciary*, 114th Cong. (2015), available at https://www.ftc.gov/system/files/documents/public_statements/632771/150325wreckinginternet.pdf; Ramirez urges repeal of common carrier exemption, FTC WATCH, available at <http://www.ftcwatch.com/ramirez-urges-repeal-of-common-carrier-exemption/>.

²⁶³ 15 U.S.C. § 45(a)(2).

²⁶⁴ Cf. 15 U.S.C. § 44.

²⁶⁵ *Prepared Statement of Commissioner Joshua D. Wright, supra*, available at https://www.ftc.gov/system/files/documents/public_statements/632771/150325wreckinginternet.pdf (internal citations omitted).

²⁶⁶ FED TRADE COMM'N, BROADBAND CONNECTIVITY COMPETITION REPORT, 41 (2007), available at <https://www.ftc.gov/sites/default/files/documents/reports/broadband-connectivity-competition-policy/v070000report.pdf>.

lar matters.²⁶⁷ Because the FCC's rationale for its proposed privacy rules is to fill the gap it created by "reclassifying" broadband and thus removing it from the FTC's jurisdiction, enactment of this legislation would moot the need for new FCC rules. Accordingly, this bill should include a provision directing the FCC to terminate that rulemaking—so that the FTC may resume its former role in policing broadband privacy and data security without unnecessary and costly duplicative regulations.

This situation is very much unlike that in the 1980 FTC Improvements Act, by which Congress both tightened the FTC's Section 5 rulemaking processes (as instituted in 1975) and also ended the FTC's children's advertising rulemaking.²⁶⁸ In signing the bill, President Carter lauded the former but objected to the latter:

We need vigorous congressional oversight of regulatory agencies. But the reauthorization bills passed by the Senate and the House went beyond such oversight and actually required termination of specific, major, ongoing proceedings before the Commission. I am pleased that the conferees have modified these provisions. If powerful interests can turn to the political arena as an alternative to the legal process, our system of justice will not function in a fair and orderly fashion.²⁶⁹

President Carter had a point, in general. But in this case, Congress would not be telling an agency to stop a pending rulemaking because of a policy difference; it would be telling the FCC to stop a rulemaking that it claims is necessary only because of a regulatory vacuum of its own creation.

If the FCC insists on issuing its own rules, the bill will result in overlapping jurisdiction, which could create problems of its own: forum-shopping, inconsistent results, and politicization of the enforcement process. The Memorandum of Understanding reached between the two agencies on how to handle enforcement where their authority *does* overlap will do little to minimize potential conflicts.²⁷⁰ It would be particularly incongruous to enact legislation authorizing overlapping and conflicting jurisdiction while Congress is also considering the SMARTER Act, aimed at mitigating exactly such problematic overlap in the antitrust enforcement authority of the FTC and DOJ.²⁷¹ None of these concerns are inherent reasons not to restore the FTC's jurisdiction; after all, the FTC is the better regulator, in large part because applying standards of general applicability makes the FTC a more difficult agency to capture than a sector-specific regulator like the FCC. But these concerns do make it important that passage of this bill be tied to ending the FCC's foray into privacy and data-security regulation.

FTC Jurisdiction over Tax-Exempt Organizations & Nonprofits

The Tax Exempt Organizations Act

Representative Rush's (D-IL) bill (H.R. 5255)²⁷² would add tax-exempt, 501(c)(3) nonprofits to the definition of "corporation" subject to the FTC Act in Section 4 (15 U.S.C. § 44). It would not, however, amend Section 4 to remove the language that limits the FTC's jurisdiction to corporations that "carry on business for [their] own profit or that of [their] members." Thus, the FTC would still be limited to policing for-profit activities but would have an easier time establishing that a nonprofit was essentially conducting for-profit activities.

²⁶⁷ Protecting the Privacy of Customers of Broadband and Other Telecommunications Services, *Notice of Proposed Rulemaking*, WC Docket No. 16-106 (rel. Apr. 1, 2016), available at https://apps.fcc.gov/edocs_public/attachmatch/FCC-16-39A1_Rcd.pdf.

²⁶⁸ FTC Improvements Act Section 11 added the following language to 17 U.S.C. § 57a: "The Commission shall not have any authority to promulgate any rule in the children's advertising proceeding pending on the date of the enactment of the Federal Trade Commission Improvements Act, p. 374. Act of 1980 or in any substantially similar proceeding on the basis of a determination by the Commission that such advertising constitutes an unfair act or practice in or affecting commerce."

²⁶⁹ Carter, *supra* note 19.

²⁷⁰ Memorandum of Understanding on Consumer Protection Between the Federal Trade Commission and the Federal Communications Commission (Nov. 2015), available at https://www.ftc.gov/system/files/documents/cooperation_agreements/151116ftcc-mou.pdf.

²⁷¹ SMARTER Act, *supra* note 228.

²⁷² A Bill to Amend the Federal Trade Commission Act to Permit the Federal Trade Commission to Enforce Such Act Against Certain Tax-exempt Organizations, H.R. 5255, 114th Cong. (2016) available at <https://www.congress.gov/bills/114th-congress/house-bill/5255/text>.

Value of the Bill: Would Reduce Litigation Expenses for the FTC

This bill does precisely the same thing proposed by Sen. Byron Dorgan's FTC Reauthorization Act of 2008.²⁷³ The Republican-led FTC supported this provision at the time.²⁷⁴

In 2008, in supporting Sen. Dorgan's version of this bill, the FTC explained the advantage of this reform, even though it would not technically change the substance of the FTC's jurisdiction:

The proposed legislation would also help increase certainty and reduce litigation costs in this area. Although the FTC has been successful in asserting jurisdiction against "sham" nonprofits and against non-profit trade associations, the proposed legislation would help avoid protracted factual inquiries and litigation battles to establish jurisdiction over such entities.²⁷⁵

We agree with the FTC's 2008 assessment.

Recommendation: Extend Jurisdiction to Tax-Exempt Entities, Including Trade Associations

In 2008, in supporting Sen. Dorgan's version of this bill, the FTC also said:

The Commission would be pleased to work with Congressional staff on crafting appropriate language. The Commission notes that, as drafted, Section 6 would reach only those non-profit entities that have tax-exempt status under section 501(c)(3) of the Internal Revenue Code. The Commission would benefit from broadening this provision to cover certain other nonprofits, such as Section 501(c)(6) trade associations. The Commission has previously engaged in protracted litigation battles to determine whether such entities are currently covered under the FTC Act. *See, e.g., California Dental Ass'n v. FTC*, 526 U.S. 756, 765–69 (1999) (holding that FTC Act applies to anticompetitive conduct by non-profit dental association whose activities provide substantial economic benefits to for-profit members); *American Medical Ass'n v. FTC*, 638 F.2d 443, 447–448 (1980) (finding FTC jurisdiction over non-profit medical societies whose activities "serve both the business and non-business interests of their member physicians").²⁷⁶

Recommendation: Extend Jurisdiction to All Non-Profits

We likewise recommend expanding the bill to encompass all nonprofit corporations, regardless of their tax-exempt status.²⁷⁷ The logic of the FTC's jurisdiction doesn't turn on the tax-exempt status of organizations, which, for these purposes, is essentially a meaningless dividing line between entities. It makes little sense to include tax-exempt nonprofits within the FTC's ambit while excluding nonprofits without Federal tax-exempt status.

Rulemaking

The FTC makes rules in two ways: (1) under Section 5, through the process created by Congress in 1980 to require additional economic rigor and evidence; and (2) under narrow grants of standard APA rulemaking authority specific to a particular issue.

*Economic Analysis in All FTC Rulemakings***No Bill Proposed***Recommendation: Require BE to Comment on Rulemakings*

The RECS Act, discussed below, would require the FTC to include BE analysis of any recommendations it makes for rulemakings. However, this would not apply to the FTC's own rulemakings because that bill is focused on the FTC's statutory

²⁷³ Federal Trade Commission Reauthorization Act of 2008, *supra* note 261, § 6, available at <https://www.govtrack.us/congress/bills/110/s2831/text>.

²⁷⁴ Prepared Statement of the Federal Trade Commission: Hearing Before the S. Comm. on Commerce, Science, and Transportation. 110th Cong. (2008), 19, available at https://www.ftc.gov/sites/default/files/documents/public_statements/ftc-testimony-reauthorization/p034101_reauth.pdf.

²⁷⁵ *Id.* at 16.

²⁷⁶ *Id.* at 18 n.49.

²⁷⁷ The nonprofit designation is a creature of state incorporation law, and obligates corporations to adopt certain governance rules and structures. Federal tax-exempt status is a creature of Federal tax law, and, while it obligates companies to limit their corporate purpose (*e.g.*, to education, religious activities, etc.), it doesn't appreciably affect their governance structure. Companies can be nonprofit but not tax-exempt, although all tax-exempt companies are nonprofit.

authority to make recommendations to Congress, other agencies, and state and local governments.

Requiring regulatory agencies to do cost-benefit analysis has been uncontroversial for decades, dating back at least to the Carter Administration. Indeed, in 2011, shortly after President Obama issued Executive Order 13563,²⁷⁸ his version of President Clinton's 1993 Executive Order 12866²⁷⁹ applying to Executive Branch agencies, he issued a second order, Regulation and Independent Regulatory Agencies, Executive Order 13579.²⁸⁰ The key difference between the two is that the President said Executive agencies "must" do cost-benefit analysis for each new regulation, but that independent agencies "should" undertake retrospective analysis of its rules and periodically update them.

FTC Chairman Jon Leibowitz fully endorsed the idea in the White House's blog about the Order:

President Obama deserves enormous credit for ensuring regulatory review throughout the Federal government, including at independent agencies. Although regulations are critically important for protecting consumers, they need to be reviewed on a regular basis to ensure that they are up-to-date, effective, and not overly burdensome. For all agencies—dependent or not—periodic reviews of your rules is just good government. The announcement raises the profile of this issue, and I think that's a constructive step.²⁸¹

The chief (indeed, perhaps the only) reason for the difference is that the President has no authority over independent agencies, which are creatures and servants of Congress. The bipartisan Independent Agency Regulatory Analysis Act of 2015 (S. 1607) would solve this problem, giving the President the authority to set cost-benefit standards for independent agencies as well.²⁸² We fully support that bill and believe this requirement should apply to *all* independent agencies. But there is no reason to wait for passage of the more comprehensive bill. The FTC in particular would benefit from a commitment to cost-benefit analysis in its rulemakings immediately.

Of course, it is true that the Commission has abandoned using its Section 5 rule-making power (precisely because it reflects the Carter-era commitment to cost-benefit analysis). But the Commission *does* continue to make rules under a variety of issue-specific statutes such as several of those now pending before the House Energy and Commerce Committee, Subcommittee on Commerce, Manufacturing and Trade in May 2016.²⁸³ As the chief example of the need for greater economic rigor in FTC rulemakings, we note the FTC's 2012 COPPA rulemaking: the agency expanded the definition of "personal information," thus greatly expanding the number of children's-oriented media subject to the rule, with no meaningful analysis of what this would do to children's media.

Despite loud protests from small operators that the rule might cause them to cease offering child-oriented products, the FTC produced a meaningless estimate that the rule would cost \$21.5 million in the aggregate.²⁸⁴ Of course, the *real* cost of the new rule is not the direct compliance cost but the second-order effects of the number of providers who exit the children's market, reduce functionality, slow innovation or raise prices—none of which did the FTC even attempt to estimate. This was a clear failure of economic analysis.

We also note Commissioner Ohlhausen's 2015 dissent from the Commission's vote to update the Telemarketing Sales Rule to ban telemarketers from using four "novel" payment methods. Ohlhausen cited no less an authority than the Federal Reserve Bank of Atlanta (FRBA), which is not merely one of twelve Federal Reserve

²⁷⁸ Exec. Order No. 13,563, 3 C.F.R. 13563 (2012) available at <https://www.whitehouse.gov/the-press-office/2011/01/18/executive-order-13563-improving-regulation-and-regulatory-review>.

²⁷⁹ Exec. Order No. 12,866 3 C.F.R. 12866 (1993) available at https://www.whitehouse.gov/sites/default/files/omb/inforeg/EO12866/EO12866_10041993.pdf.

²⁸⁰ Exec. Order No. 13,579, 3 C.F.R. 13579 (2012) available at <https://www.whitehouse.gov/the-press-office/2011/07/11/executive-order-13579-regulation-and-independent-regulatory-agencies>.

²⁸¹ Cass Sunstein, *The President's Executive Order on Improving and Streamlining Regulation by Independent Regulatory Agencies*, WHITEHOUSE.GOV BLOG (Jul. 11, 2011), <https://www.whitehouse.gov/blog/2011/07/11/president-s-executive-order-improving-and-streamlining-regulation-independent-regula>.

²⁸² Independent Agency Regulatory Analysis Act of 2015, S. 1607, 114th Cong. (2015), available at <https://www.congress.gov/bills/114th-congress/senate-bill/1607/text>.

²⁸³ See Press Release, HEARING: SubCMT to Review 17 Bills Modernizing the FTC for the 21st Century NEXT WEEK, THE ENERGY AND COMMERCE COMMITTEE (May 17, 2016), <https://energycommerce.house.gov/news-center/press-releases/hearing-subcmt-review-17-bills-modernizing-ftc-21st-century-next-week>.

²⁸⁴ 78 Fed. Reg. 4002 available at https://www.ftc.gov/system/files/documents/federal_register_notices/2013/01/2012-31341.pdf

Branches, but the one responsible for “operat[ing] the Federal Reserve System’s Retail Payments Product Office, which manages and oversees the check and Automated Clearing House (ACH) services that the Federal Reserve banks provide to U.S. financial institutions.”²⁸⁵ Ohlhausen explained:

The amendments do not satisfy the third prong of the unfairness analysis in Section 5(n) of the FTC Act, which requires us to balance consumer injury against countervailing benefits to consumers or competition. Although the record shows there is consumer injury from the use of novel payment methods in telemarketing fraud, it is not clear that this injury likely outweighs the countervailing benefits to consumers and competition of permitting novel payments methods. . . .

In sum, the FRBA’s analysis of the prohibition of novel payments in telemarketing indicates that any reduction in consumer harm from telemarketing fraud is outweighed by the likely benefits to consumers and competition of avoiding a fragmented law of payments, not limiting the use of novel payments prematurely, and allowing financial regulators working with industry to develop better consumer protections.²⁸⁶

Again, it appears that the Commission majority failed to undertake an economically rigorous analysis of the sort BE would likely perform, in this case failing to properly weigh injury and countervailing benefits as Section 5(n) requires.

At a minimum, the Commission would have done well to solicit further public comment on its rule, heeding the experience of past chairmen, as summarized by Former Chairman Tim Muris:

By their nature, however, rules also must apply to legitimate actors, who actually deliver the goods and services they promise. Remedies and approaches that are entirely appropriate for bad actors can be extremely burdensome when applied to legitimate businesses, and there is usually no easy or straightforward way to limit a rule to fraud. Rather than enhancing consumer welfare, overly burdensome rules can harm the very market processes that serve consumers’ interests. For example, the Commission’s initial proposal for the Telemarketing Sales Rule was extremely broad and burdensome, and one of the first acts of the Pitofsky Commission was to narrow the rule. More recently, the Commission found it necessary to re-propose its Business Opportunity Rule, because the initial proposal would have adversely affected millions of self-employed workers.²⁸⁷

Issue-Specific Rulemakings

Several Bills Proposed

Congress has long enacted legislation tasking the FTC with enacting regulations in a specific area through standard rulemaking under the Administrative Procedure Act. This, in effect, has allowed the FTC to avoid having to conduct rulemakings under the Magnuson-Moss Act of 1975 (as amended in 1980). The result has been that there may not be anyone left at the FTC who has ever conducted a Section 5 rulemaking. This contributes to the common misconception that the FTC lacks rulemaking authority—something the Chairman and other Commissioners have said casually. Of course, they mean that the FTC lacks *APA* rulemaking authority, and that they believe Section 5 rulemaking is too difficult.

But this belief is unfounded. There is good reason to think that the FTC could have conducted a Section 5 rulemaking to address telemarketing complaints, for example, in about the same amount of time it took Congress to pass the Do Not Call Act and for the FTC to conduct an *APA* rulemaking, and perhaps even less. As Former Chairman Tim Muris explained, in 2010:

The Commission’s most prominent rulemaking endeavor, the creation of the National Do Not Call Registry, could have proceeded in a timely fashion under Magnuson-Moss procedures. It took two years from the time the rule was first publicly discussed until it was implemented. Although it would have been nec-

²⁸⁵ Separate Statement of Commissioner Maureen K. Ohlhausen, Dissenting in Part, In the Matter of the Tel-emarketing Sales Rule, Project No. R411001, at n. 3 (Nov. 18, 2015), available at https://www.ftc.gov/system/files/documents/public_statements/881203/151118tsrmkospeech.pdf.

²⁸⁶ *Id.* at 1–2.

²⁸⁷ Statement of Timothy J. Muris, *supra* note 14, at 24.

essary to structure the proceedings differently, there would have been little, if any, additional delay from using Magnuson-Moss procedures.²⁸⁸

This is not idle speculation. Muris actually ran the FTC during its creation of the Do Not Call registry. Attempting a Section 5 rulemaking would have been a valuable experience for the FTC, and it might have avoided some of the unintended consequences of *ex ante* legislation.

We make two broad recommendations applicable to all six rulemaking bills.

Recommendation: Require the FTC to Conduct Section 5 Rulemakings & Report on the Process

The FTC would greatly benefit from conducting a Section 5 rulemaking. Congress should direct the FTC to conduct such a rulemaking on at least one, and preferably two or three, of the issues to be addressed by these proposed issue-specific bills. Having multiple rulemakings would produce a more representative experience with the FTC's Section 5 rulemaking powers. However many Section 5 rulemakings the FTC does, Congress should direct the FTC to report back in, say, three years as to the state of these rulemakings and the FTC's general experience with its Section 5 rulemaking procedures. This is the only way Congress will ever be able to make informed decisions about how existing Section 5 rulemaking processes might be expedited or streamlined without removing the safeguards that Congress rightly imposed to prevent the FTC from abusing its rulemaking powers.

Any reconsideration of the FTC's Section 5 rulemaking processes should be undertaken with the utmost caution. Unfairness is a uniquely elastic concept, which requires unique procedural safeguards if it is to serve as the basis for rulemaking. If anything, FTC's approach to enforcing Section 5 in high tech matters over the last 15–20 years reconfirms the need for safeguards: in its “common law of consent decrees,” the FTC has paid little more than lip service to the balancing test inherent in unfairness, and has increasingly nullified the materiality requirement at the heart of the deception policy statement.

Recommendation: Include Periodic Re-Assessment Requirements in Any New Grants of APA Rulemaking Authority

It is impossible to predict the unintended consequences of any of the proposed issue-specific bills granting the FTC new rulemaking authority.²⁸⁹ However narrowly targeted they may seem, they may wind up constraining new technologies or business models that would otherwise serve consumers.

Consider the Video Privacy Protection Act of 1988 (“VPPA”), which barred “wrongful disclosure of video tape rental or sale records.”²⁹⁰ After the experience of Judge Robert Bork, whose video rental records were made an issue at his (failed) Supreme Court confirmation hearings, this quick-fix bill must have seemed utterly uncontroversial. Yet it proved overly rigid in the digital age. In 2009, an anonymous plaintiff sued Netflix over its release of data sets for the Netflix Prize, alleging that the company's release of the information constituted a violation of the VPPA.²⁹¹ In 2011 Netflix launched a feature integrating its service with Facebook—everywhere *except* in the U.S., citing the 2009 lawsuit and concerns over the VPPA. After two years, President Obama signed legislation (H.R. 6671) amending the VPPA to allow Netflix and other video companies to *give consumers the option* of sharing information about their viewing history on social networking sites like Facebook.²⁹² Despite this amendment, the VPPA continues to threaten to overly restrict novel online transactions that were never contemplated or intended by the drafters of the statute.²⁹³

The VPPA is just one of many laws that have proven unable to keep up with technological change (the 1996 Telecommunications Act, (largely) a classic example of

²⁸⁸ *Id.* at 27.

²⁸⁹ See Press Release, #SubCMT Releases Reform Package to Modernize the FTC and Promote Innovation, THE ENERGY AND COMMERCE COMMITTEE (May 5, 2016), <https://energycommerce.house.gov/news-center/press-releases/subcmt-releases-reform-package-modernize-ftc-and-promote-innovation>.

²⁹⁰ Video Privacy Protection Act of 1988, Pub. L. 100–618, 102 Stat. 3195 (Nov. 5, 1988), available at <https://www.gpo.gov/fdsys/pkg/STATUTE-102/pdf/STATUTE-102-Pg3195.pdf>.

²⁹¹ See Kristian Stout, *Pushing Ad Networks Out of Business: Yershov v. Gannett and the War Against Online Platforms*, TRUTH ON THE MARKET (May 10, 2016), <https://truthonthemarket.com/2016/05/10/pushing-ad-networks-out-of-business-yershov-v-gannett-and-the-war-against-online-platforms/>.

²⁹² Video Privacy Protection Act Amendments Act of 2012, H.R. 6671, 112th Cong (2012), available at <https://www.congress.gov/bill/112th-congress/house-bill/6671?q=%7B%22search%22%3A%5B%22%5C%22hr6671%5C%22%22%5D%7D&resultIndex=1>.

²⁹³ See Stout, *supra* note 291.

the Rulemaking Model, comes readily to mind). To protect against this inevitability, Congress should include regular review of legislation as a “safety hatch.” The 1998 Children’s Online Privacy Protection Act (COPPA) included this review provision:

Not later than 5 years after the effective date of the regulations initially issued under . . . this title, the Commission shall—

(1) review the implementation of this chapter, including the effect of the implementation of this chapter on practices relating to the collection and disclosure of information relating to children, children’s ability to obtain access to information of their choice online, and on the availability of websites directed to children; and (2) prepare and submit to Congress a report on the results of the review under paragraph (1).²⁹⁴

In principle, this is the right idea. However, in practice, this requirement has proven ineffective. The FTC’s review of COPPA included little meaningful analysis of the cost of COPPA.²⁹⁵ Indeed, the FTC used the discretion afforded it by Congress in the statute to expand the definition of the term “personal information” in ways that appear to have reduced the availability, affordability and diversity of children’s media—yet without any economic analysis by the Commission.

At a minimum, Congress should include something like the following in any issue-specific grant of new APA rulemaking authority it enacts:

Not later than 5 years after the effective date of the regulations initially issued under . . . this title, *and every 5 years thereafter*, the Commission shall—

(1) *direct the Bureau of Economics, with the assistance of the Office of Technology Research and Investigation*, to review the implementation of this chapter, including the effect of the implementation of this chapter on practices relating to *[affected industries]*; and

(2) prepare and submit to Congress a report on the results of the review under paragraph (1).

Conclusion

The letter by which the FTC submitted the Unfairness Policy Statement to the Chairman and Ranking Member of the Senate Commerce Committee in December 1980 concludes as follows:

We hope this letter has given you the information that you require. Please do not hesitate to call if we can be of any further assistance. With best regards,
/s/ Michael Pertschuk, Chairman²⁹⁶

We believe it’s high time Congress picked up the phone.

To be effective, any effort to reform the FTC would require a constructive dialogue with the Commission—not just those currently sitting on the Commission, but past Commissioners and the agency’s staff, including veterans of the agency. Along with the community of practitioners who navigate the agency on behalf of companies and civil society alike, all of these will have something to add. We do not presume to fully understand the inner workings of the Commission as only veterans of the agency can. Nor do we presume that the ideas presented here are necessarily the best or only ones to accomplish the task at hand. But reform cannot be effective if it begins from the presumption that today’s is the “best of all possible FTCs,” or that any significant reform to the agency would cripple it.

Unfortunately, many of those who would tend to know the most about the inner workings of the agency are also the most blinded by status quo bias, the tendency not just to take for granted that the FTC works, and has always worked, well, but to dismiss proposals for change as an attacks upon the agency. It would be ironic, indeed, if an agency that wields its own discretion so freely in the name of flexibility and adaptation were itself unwilling to adapt.

We believe that reforms to push the FTC back towards the Evolutionary Model can be part of a bipartisan overhaul and reauthorization of the agency, just as they were in 1980 and 1994. At stake is much more than how the FTC operates; it is nothing less than the authority of Congress as the body of our democratically elected representatives to steer the FTC. Congress should not, as Justice Scalia warned

²⁹⁴ 15 U.S.C. § 6506.

²⁹⁵ See *supra* note 284.

²⁹⁶ Fed. Trade Comm’n, FTC Policy Statement on Unfairness (Dec. 17, 1980), available at <https://www.ftc.gov/public-statements/1980/12/ftc-policy-statement-unfairness>

in 2014 in *UARG v. EPA*, willingly “stand on the dock and wave goodbye as [the FTC] embarks on this multiyear voyage of discovery.”²⁹⁷

AMERICAN BAR ASSOCIATION SECTION OF ANTITRUST LAW

PRESIDENTIAL TRANSITION REPORT: THE STATE OF ANTITRUST
ENFORCEMENT—JANUARY 2017

The views expressed herein are on behalf of the American Bar Association Section of Antitrust Law. They have not been approved by the House of Delegates or the Board of Governors of the American Bar Association, and unless otherwise noted, should not be construed as representing the policy of the American Bar Association.

I. INTRODUCTION

II. EXECUTIVE SUMMARY

- A. Enforcement Matters
- B. Legal Doctrine
- C. Industry-Specific Issues
- D. International Matter

III. ENFORCEMENT MATTERS

- E. Agency Enforcement and Policy
- F. Cartel Enforcement
- G. Civil Enforcement and Litigation
- H. Mergers
- I. Consumer Protection

IV. LEGAL DOCTRINE

- J. Monopoly
- K. Antitrust and Intellectual Property

V. INDUSTRY-SPECIFIC ISSUES

- L. Financial Sector
- M. Healthcare Industry

VI. INTERNATIONAL

- N. Establishing U.S. Focus and Leadership in International Antitrust Policy
- O. Clarify the Jurisdictional Character of the FTAIA
- P. Encourage Direct Agency Intercession in Foreign Agency Proceedings
- Q. Engage in a Critical Self-Assessment of U.S. Antitrust Procedures

VII. CONCLUSION

I. INTRODUCTION

The Section of Antitrust Law of the American Bar Association (the “Section”) is pleased to offer its views regarding the current state of Federal antitrust and consumer protection enforcement and its recommendations for ways the new administration might consider further strengthening policy and enforcement to deal with new challenges on the horizon. The views and recommendations contained in this Report are those of the Section. They have not been approved by the House of Delegates or the Board of Governors of the American Bar Association, and unless otherwise noted, should not be construed as representing the policy of the American Bar Association.

This will be the eighth sequential Presidential Transition Report prepared by the Section. Section Chairs, Roxann E. Henry (2015–16) and William MacLeod (2016–17), appointed this Presidential Transition Task Force of 20 lawyers, professors, and economists in May 2016.¹ The membership of the Task Force mirrors the deep ex-

²⁹⁷ Util. Air Regulatory Grp. v. EPA, 134 S. Ct. 2427, 2446 (2014).

¹ The 2016 Presidential Transition Task Force was co-chaired by Theodore Voorhees and Leah Brannon. Samantha Knox served as the Reporter and Organizer of the Task Force. The Task Force members included Roxane Busey, Mary Ellen Callahan, Dennis Carlton, Michael A. Carrier, Paul T. Denis, Douglas H. Ginsburg, Louis Kaplow, Donald C. Klawiter, William Kovacic,

expertise, diversity of viewpoint and breadth of experience of the Section's 6,900 members. The Task Force includes attorneys in private practice representing defendants and plaintiffs; a member of the Federal judiciary; and antitrust law and economics scholars from the Nation's leading universities. More than half of the members have served in senior leadership positions in the Antitrust Division of the Department of Justice (the "Division") or the Federal Trade Commission (the "FTC") (collectively, the "Agencies"), including several former Assistant Attorneys General and Commissioners. Members of the Task Force have served in every Administration extending back more than four decades. Task Force members have also made significant contributions to the body of scholarly literature in the fields of competition and consumer protection law, and have been active in the international competition community, including as advisors to foreign competition authorities and the International Competition Network (ICN).

The Task Force Members represent a diverse range of political, ideological, and professional views, and the Report is the result of an often vibrant and spirited debate among the members. In keeping with the strong philosophy favoring action by consensus that animates all Section reports and publications, all Members worked hard to accommodate one another's perspectives, with the result that some of the findings and conclusions offered herein would not have been written in exactly the same way by any individual member writing alone. This being said, the Report has been endorsed by all Task Force members and was approved by the Section's Council.

II. EXECUTIVE SUMMARY

Antitrust figured prominently in the 2016 Election: for the first time in recent memory, both major parties prominently featured their respective viewpoints on competition and consumer protection policy. Campaign commentary included sharp criticism of an alleged absence of vigor and overall ineffectiveness in current patterns of antitrust enforcement, with comments calling for sharp, even radical reorientation of enforcement policy, especially in the review of proposed mergers and treatment of large industrial firms. As will be seen in this Report, the Section does not share these views about the current state of antitrust enforcement policy. To the contrary, although dynamic market forces will always pose challenges for government enforcement policy, and enforcement efforts must adapt to meet those challenges, the Section's view is that the Nation's system of competition enforcement has been in good hands, that an arc of continuous improvement and advancement can be discerned that stretches back over many years and multiple administrations, and that enforcement policy should remain firmly tethered to its statutory basis.

This Report is divided into four sections. First, the Report focuses on the current state of antitrust and consumer protection enforcement under the stewardship of the Agencies. This section reviews cartel, civil, merger, and consumer protection enforcement, with an emphasis on issues that are likely to present the most significant challenges over the next four years. In its second section, the Report addresses some of the most important and challenging doctrinal questions facing the Agencies and courts today. Section three of the Report discusses some of the unique competition issues that will be facing two key industrial sectors: healthcare and financial services. Finally, the last section of the Report discusses challenges facing the Administration, the Agencies, and U.S. firms in the international arena as competition enforcement regimes proliferate and continue to evolve throughout the world.

A. Enforcement Matters

The Agencies have a broad range of policy tools at their disposal and for the most part have been making good use of them. Agency guidance plays an important role in ensuring that markets function efficiently and competitively. The Section encourages the Agencies to continue providing this guidance in written form, including formal guidance documents, agency reports, closing statements, speeches by top agency officials, and the like. Written guidance from the Agencies is especially important in connection with novel market conditions and forms of behavior as well as in circumstances where there has been a shift in the Agencies' enforcement policies and priorities. Further guidance is particularly needed on vertical issues arising in the context of mergers, resale price maintenance, state action, and intellectual property ("IP"). The Section encourages the Agencies to continue to use litigation as a policy

Jon Leibowitz, Abbott B. Lipsky, Jr., A. Douglas Melamed, Fiona Scott Morton, James H. Mutchnik, Richard Parker, Lydia Parnes, James Rill, and Joel Winston. Megan Browdie served as the Young Lawyer Representative to the Task Force. The views and conclusions of Task Force Members that are reflected in this Report have been provided in their individual capacities and should not be attributed in any way to their law firms, clients or academic institutions, as applicable.

tool to clarify important issues. The Agencies should continue to review and comment on legislation and regulations that affect competition policy, agency jurisdiction, and the abilities of agencies to effectuate their missions.

The Section commends the Division for the continued success of its cartel enforcement program, and encourages the Division to build on this success by providing increased transparency and ongoing practical guidance on its Corporate and Individual Leniency Programs, and promoting the adoption of similar leniency programs throughout the world. This initiative could alleviate our concern that the sentencing and fining processes in international cartel investigations have grown too complex to understand, and encourages the Division to closely examine its policies and procedures for “volume of commerce” (VOC) determinations.

Also needed is further guidance in the wake of the Yates Memorandum. The Section commends the Division for recognizing the importance of corporate compliance measures in several recent sentencing proceedings, and encourages the Division to pursue an open dialogue with the bar and business community about model “robust” compliance programs and effective detection and screening techniques. The Division should also consider exploring proactive methods of cartel detection in partnership with federal, state, and local law enforcement agencies.

The Section commends the Agencies’ recent focus on litigating cases and being “trial ready.” To enhance this facet of enforcement, we propose that the Agencies form a working group to identify procedural and structural measures that could improve antitrust litigation in Federal court. Potential reforms might include structuring trials by issue (instead of by party) and greater use of court-appointed experts.

In the merger enforcement area, the Section focuses on the need for increased transparency, including in merger trials, and increased utilization of closing statements for merger investigations not resulting in agency action. The Section also recommends that the Agencies make greater use of merger retrospectives to evaluate the effectiveness of merger policy, tools, and remedies. These studies should focus on both price and output effects, and should evaluate the efficacy of tools and models used to evaluate mergers. Finally, the Section reiterates the need for process symmetry between the Division and the FTC in merger enforcement litigation.

In consumer protection, law enforcement and the regulatory landscapes have changed significantly over the last four years. This Report notes numerous initiatives of the FTC, as well as actions of the Consumer Financial Protection Bureau (CFPB) and the Federal Communications Commission (FCC), that have enhanced protection of the Nation’s consumers. However, the overlapping jurisdictions of the FTC, CFPB, and FCC give rise to risks of inconsistent regulatory approaches that cause confusion and complicate compliance, particularly with respect to privacy protection. Such inconsistencies could undermine the objectives the Agencies seek to advance.

The Section urges the FTC, FCC, and CFPB to take action to address these risks, including by supporting repeal of the common carrier exception in the FTCA and by adopting consistent privacy protection frameworks. The Section urges the FTC and CFPB to adopt reforms to enhance the transparency and fairness of the enforcement process, including dedicating resources to cases involving significant consumer harm, using civil investigative demands more judiciously, adopting internal guidelines for staff in communicating with investigation targets, reducing burdens of “boilerplate” order provisions, tailoring monetary relief to the injury caused and the defendant’s culpability, and providing targets with the opportunity to meet with decision makers. Finally, the Section notes the need for additional guidance and harmonization on topics relating to abusive and unfair practices (CFPB’s and FTC’s respective standards), data security, monetary remedies, advertising interpretation, and “clear and conspicuous” disclosure requirements.

B. Legal Doctrine

The Agencies will play a pivotal role in shaping legal doctrine over the next four years. The Report identifies needs in key substantive areas—better delineation of problematic exclusionary conduct that may have adverse market effects—where the Agencies can reduce legal uncertainty and avoid conflicts by offering sound policy leadership.

With respect to exclusionary conduct, the Section sees three areas that could benefit from further Agency attention and guidance. First, two-sided markets are increasingly important in today’s economy, but have received relatively little attention in recent court decisions and Agency statements. Second, there is need for further clarification concerning the legal analysis of contracts that reference rivals. Third, further guidance would be helpful in assessing the potential anticompetitive and

procompetitive effects of tying and bundling arrangements, particularly in light of recent conflicting decisions issued by the Third and Ninth Circuits.

With regard to patent matters, the Section recommends that the Agencies gather and analyze further evidence related to activity that may have competitive significance—for example with respect to patent assertion entities and potential holdups and holdouts—and share their assessments of competitive effects with the public and other government agencies. The Section also encourages the Agencies to consider the multinational implications of actions that alter patent rights and remedies.

C. Industry-Specific Issues

In certain industries, unique challenges and complexities arise when analyzing questions of competition law. The Obama Administration focused a large portion of its antitrust enforcement efforts on the healthcare and financial sectors. The Report addresses some of the key issues in these sectors facing the incoming Administration.

With respect to the financial sector, when evaluating proposals for new or revised regulations that will be administered by other agencies, the Section encourages the Agencies to consider the adverse effect that regulations might have on competition, particularly with respect to the burdens the regulations may impose on smaller firms. As for mergers of financial institutions, the Section believes that the Agencies should not alter their legal standards in order to benefit equity holders of banks. Finally, further clarification is needed regarding the Division's treatment of cases involving alleged interference with financial benchmarks and in particular the implications for enforcement policy and sentencing where the underlying misconduct could be seen as fraud or anticompetitive behavior or a combination of the two offenses.

With respect to the healthcare industry, the Section encourages the Agencies to provide further guidance on their merger analysis, including the theories of harm and potential benefits resulting from vertical integrations, exclusive contracts, merger-specific efficiencies, and the competitive impact of electronic healthcare records, and regulatory policies at the state and Federal levels. The Section also encourages the FTC to articulate and apply a rule-of-reason enforcement policy with respect to reverse payment settlements and to assess the implications for competition and consumer protection of discouraging purchases or refusing to deal in pharmaceutical markets.

D. International Matters

The global expansion of competition law regimes has dramatically increased the complexity and cost of compliance for U.S. businesses. The Section commends the Agencies for working to address these challenges through formal and informal cooperation, communication, and consensus-building efforts. However, there is much work yet to be done. Now, more than ever, it is important for the United States to speak with one voice in international antitrust matters. The Section encourages the Agencies to work more closely with each other and with the Administration to develop and communicate a unified global antitrust policy. To accomplish this goal, the Administration may wish to consider how the Executive Branch could facilitate more extensive coordination between the Agencies and better respond to pressing international competition law matters. The Section commends the Agencies for their efforts to promote comity through deference to foreign authorities' enforcement actions. That said, where appropriate legal grounds exist, and where consistent with U.S. policy, the Agencies should not hesitate to intervene in foreign enforcement proceedings where it appears that U.S. firms are being subjected to rules or policies that are antithetical to U.S. antitrust law, particularly where serious due process concerns are at stake. Finally, in the wake of recent Federal appellate decisions opining that the Federal Trade and Antitrust Improvements Act (FTAIA) is a substantive element of a Sherman Act claim, the Section recommends that the Agencies clarify that the FTAIA places a jurisdictional limit on Sherman Act enforcement.

III. ENFORCEMENT MATTERS

A. Agency Enforcement and Policy

1. Guidance

Where there are uncertainties in the Agencies' enforcement policies or priorities, it is often essential for the Agencies to provide guidance. The formal guidance can take the form of formal guidance documents (such as the Horizontal Merger Guidelines of 2010) or FTC opinions. Informal guidance can take the form of agency re-

ports,² speeches by key agency personnel, amicus briefs, decisions to litigate, or closing statements. Agency guidance is important and beneficial for multiple reasons, such as providing clarity for businesses, moving competition policy in the right direction, and ensuring a U.S. perspective on the international arena. Agency guidance is also particularly useful to communicate a shift in enforcement policy or practice.³

Furthermore, uncertainty as to the boundaries of antitrust laws may chill potentially procompetitive conduct or enable potentially anticompetitive behavior to continue unchecked. Businesses may be less willing to engage in novel business activities that could benefit consumers.⁴ Moreover, agency guidance and enforcement not only define the boundaries of how the Agencies view and enforce the law, but may also impact how courts rule in litigation.

Guidance also ensures a place for the U.S. perspective on the international stage. Because so many foreign antitrust authorities look to the Agencies for leadership and study U.S. enforcement decisions and cases, clearly articulated guidance helps achieve uniformity across jurisdictions. Moreover, an international presence and influence as to antitrust policy is particularly critical in an era in which some foreign competition agencies use the pretense of antitrust enforcement as a cover to mask decisions that are actually based on industrial policy or protectionism.

Speeches, while not binding on the Agencies or as long-lasting as more formal agency documents, can give advance notice of enforcement priorities and the views of agency leadership regarding how best to analyze certain forms of conduct. For instance, in her first speech as Acting Assistant Attorney General, Renata Hesse offered important insights into the use of bargaining models in analyzing vertical mergers and the Division's skepticism of procompetitive claims in horizontal mergers.⁵ Indeed, for changes in agency thinking, an agency speech or other non-enforcement guidance can be the fairer approach, at least in the first instance, than initially embarking on litigation.

Business review letters from the Division and advisory opinions from the FTC serve as another avenue for providing guidance on novel conduct. More important, by setting forth the respective agency's reasoning for how it views proposed conduct, these documents in effect make a policy statement as to what characteristics of the conduct are considered to be beneficial or harmful for consumers.

2. Inter-Agency Coordination

The Section commends the coordination between the Agencies, especially when issuing guidance. Inter-agency coordination will ensure that the benefits that result from issuing guidance, discussed above, are fully recognized. With respect to enforcement, greater coordination will not only make the Agencies more effective but also help achieve uniformity within the United States and provide a consistent message internationally.

The Section believes that the necessary level of coordination can be accomplished in a variety of ways. For example, joint workshops provide a useful and convenient opportunity to clarify enforcement community thinking. To be most effective, such workshops should ideally be linked to some internal implementation mechanism coordinated between both agencies. Annual joint agency statements at key antitrust bar events, such as the ABA Enforcers' Roundtable or the Global Antitrust Enforcement Symposium, discussing the themes and goals of the Agencies going forward provide other meaningful opportunities for clarifying agency policies and intentions in a coordinated way.

²See, e.g., FED. TRADE COMM'N, PATENT ASSERTION ENTITY ACTIVITY: AN FTC STUDY 8–13 (2016) (hereinafter FTC PAE STUDY), available at www.ftc.gov/system/files/documents/reports/patent-assertion-entity-activity-ftc-study.

³The recent guidance issued by the Division and the FTC communicating the decision to treat wage-fixing and no-poaching agreements as criminal violations going forward provides an excellent example of this. See DEP'T OF JUSTICE, ANTITRUST DIV., FED. TRADE COMM'N, ANTITRUST GUIDANCE FOR HUMAN RESOURCE PROFESSIONALS (Oct. 2016), available at www.ftc.gov/system/files/documents/public_statements/992623/ftc-doj_hr_guidance_final_10-20-16.pdf.

⁴Cf. *Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398, 414 (2004) (discussing how mistaken inferences of conduct can chill potentially procompetitive business activity).

⁵See Renata Hesse, Acting Ass't Att'y Gen., U.S. Dep't of Justice, Antitrust Div., And Never the Twain Shall Meet?: Connecting Popular and Professional Visions for Antitrust Enforcement, Opening Remarks at the 2016 Global Antitrust Enforcement Symposium 15 (Sept. 20, 2016), available at www.justice.gov/opa/speech/acting-assistant-attorney-general-renata-hesse-antitrust-division-delivers-opening.

3. *Litigation as a Policy Tool*

The Section recommends using litigation on important antitrust issues as a complement to public guidance and policy development. Litigation serves a critically important role in developing the law. Therefore, it is important for agencies to litigate their own cases (as opposed to leaving it to “private attorneys general”⁶ to challenge potential antitrust violations).

Private litigation does not always protect consumers and it often results in damage recovery for past practices, rather than injunctive relief that would stop the consumer harm from occurring. To further the antitrust laws’ core tenet of benefiting consumers, it is important for the Agencies to be seen as a leader in taking cases to court. Litigating cases also tests the current boundaries of the antitrust laws in a way that guidance alone cannot. In short, the primary benefit of a litigated decision with respect to shaping antitrust policy is that its outcome is an analysis and balancing of opposing arguments, such that the decision explains both what conduct is deemed legal and what is deemed illegal.⁷

The Section notes that there have been some recent expressions of concern that the Agencies may have become risk averse to litigation, especially with respect to conduct cases.⁸ While the Section lacks the information to agree or disagree, we believe the Agencies should demonstrate a willingness to take intelligent risks if the payoff enhances consumer welfare and moves the law in the proper direction. Even losing a case can have a beneficial effect on antitrust policy, for example, by contributing to a better understanding of the boundaries of what is considered acceptable competitive conduct.

4. *Specific Areas Where Guidance Could Be Useful*

There are a number of areas within competition law where additional guidance could be especially helpful. As economic and commercial realities develop, so too must application of the antitrust laws in these areas. Several important, illustrative areas of antitrust law that could benefit from additional guidance are discussed below.

a. Vertical Issues

Non-horizontal merger enforcement is one particular area that would benefit from agency guidance, given the recent increase in industry consolidation and vertical mergers. These mergers have attracted considerable attention recently.⁹ The last such guidelines were issued in 1984, and there have been substantial changes in antitrust policy and the application of modern economics thinking since then.¹⁰ The 2010 Horizontal Merger Guidelines do not address vertical or conglomerate mergers. The uncertainty in thinking about non-horizontal mergers becomes particularly apparent when one compares Acting Assistant Attorney General Renata Hesse’s recent comment, noted previously, that “the Antitrust Division and the FTC have become *justifiably more skeptical* about the promise of procompetitive benefits of merg-

⁶See, e.g., *Hawaii v. Standard Oil*, 405 U.S. 251, 262 (1972) (“By offering potential litigants the prospect of a recovery in three times the amount of their damages, Congress encouraged these persons to serve as ‘private attorneys general.’”).

⁷See Jan M. Rybnicek & Joshua D. Wright, *Defining Section 5 of the FTC Act: The Failure of the Common Law Method and the Case for Formal Agency Guidance*, 21 GEO. MASON L. REV. 1287, 1311 (2014).

⁸See, e.g., ORG. FOR ECON. COOPERATION AND DEV., COMPETITION COMMITTEE, COMMITMENT DECISIONS IN ANTITRUST CASES: NOTE BY THE UNITED STATES 7 (2016), available at www.justice.gov/atr/file/873491/download (citing a total of only six civil non-merger cases with litigated outcomes between January 1, 2011 and April 30, 2016).

⁹See also Peter Navarro, Senior Economic Advisor, Trump Campaign, Statement on Monopoly Power of New Media Conglomerates, Oct. 23, 2016, available at <https://www.donaldjtrump.com/press-releases/statement-on-monopoly-power-of-new-media-conglomerates> (“AT&T, the original and abusive “Ma Bell” telephone monopoly, is now trying to buy Time Warner. . . . Donald Trump would never approve such a deal because it concentrates too much power in the hands of the too and powerful few.”); Ryan Knutson, *Trump Says He Would Block AT&T-Time Warner Deal*, THE WALL STREET JOURNAL, Oct. 22, 2016, available at <http://www.wsj.com/articles/trump-says-he-would-block-at-t-time-warner-deal-1477162214>; S. Elizabeth Warren, *Regigniting Competition in the American Economy*, Keynote Remarks at New America’s Open Markets Program Event 6 (June 29, 2016), available at www.warren.senate.gov/files/documents/2016-6-29_Warren_Antitrust_Speech.pdf (advocating for increased scrutiny of vertical mergers and for a revision of the non-horizontal merger guidelines).

¹⁰See U.S. DEPT OF JUSTICE, Press Release, *Department of Justice and Federal Trade Commission Issued Revised Horizontal Merger Guidelines: 2010 Guidelines More Accurately Represent Agencies’ Merger Review Process*, August 19, 2010, available at <https://www.justice.gov/opa/pr/department-justice-and-federal-trade-commission-issue-revised-horizontal-merger-guidelines> (describing “several important ways” in which new guidelines differed from previous guidelines).

ers,”¹¹ with the 1984 Guidelines’ statement that “substantial economies are afforded by vertical integration [and thus] the [agencies] will give relatively more weight to expected efficiencies in determining whether to challenge a vertical merger.”¹²

Another important vertical issue, resale price maintenance (RPM), historically received a fair amount of attention through litigated cases. However, despite being the subject of two important Supreme Court cases that have ushered in the use of rule of reason analysis to this practice,¹³ RPM is an area of Federal antitrust law that has received little apparent attention in recent years.¹⁴ Recognizing that the current state of RPM law in both minimum and maximum price contexts requires sophisticated balancing of pro- and anti-competitive tendencies, the dearth of guidance from the Agencies in the form of either guidelines or litigated cases leaves open important questions in an area of law that can have a direct and substantial impact on consumers. For example, it would be beneficial for the Agencies to provide guidance on how they think about balancing asserted quality and service benefits that can flow from maintaining minimum prices for certain types of products against the potential that RPM reduces competition to the detriment of consumers. Perhaps equally important, the Agencies should provide guidance on how they would analyze the vigor of interbrand competition in markets where some producers have restricted intrabrand competition among distributors of their products.

b. Intellectual Property

Much valuable work could be devoted to providing guidance at the intersection of antitrust and intellectual property laws. The Agencies’ efforts in updating the Antitrust Guidelines for Intellectual Property are timely, especially in light of recently issued IP guidelines by several foreign jurisdictions (some of which diverge from generally accepted antitrust principles in the United States). For example, China has issued two separate sets of IP guidelines that conflict in several important areas with each other and with the position of other antitrust agencies, including in the United States.¹⁵ As noted previously, guidelines from the Division and FTC are critical for providing clarity in the international arena, and may help to achieve international conformity on important cross-border antitrust issues.

The Agencies have issued policy statements regarding Standard Essential Patents (SEPs), such as the joint statement issued by the Division and the Patent and Trademark Office on remedies for SEP violations subject to Fair, Reasonable and Non-Discriminatory (FRAND) commitments.¹⁶ These have been helpful, although certain aspects of those reports raise issues that merit additional analysis regarding the legal rights of the parties involved. The Section applauds the FTC’s recent 6(b) Study on patent assertion entities that recommends, among other things, litigation reforms that lower the costs and burdens of defending an infringement suit but preserve the patent system’s beneficial role in promoting innovation and consumer welfare.¹⁷ The Section encourages the Agencies to continue undertaking studies of competitive issues in the IP arena designed to provide guidance where the potential exists for competitive harm. Likewise, clarification of enforcement policy for the inter-

¹¹ Hesse, *supra* note 5, at 15 (emphasis added).

¹² U.S. DEPT OF JUSTICE & FED. TRADE COMM’N, NON-HORIZONTAL MERGER GUIDELINES § 4.24 (1984), available at www.justice.gov/atr/non-horizontal-merger-guidelines.

¹³ *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U.S. 877, 881 (2007); *State Oil Co. v. Khan*, 522 U.S. 3, 22 (1997).

¹⁴ The last government action against RPM was brought almost 20 years ago and the last speech by an agency head was in 2009. See *United States v. Ixtlera de Santa Catarina*, 1996 WL 925857 (E.D. Pa. 1996); Christine Varney, Ass’t Att’y Gen., U.S. Dep’t of Justice, Antitrust Div., Antitrust Federalism: Enhancing Federal/State Cooperation, Remarks as Prepared for the National Association of Attorneys General Columbia Law School State Attorneys General Program (Oct. 7, 2009), available at www.justice.gov/atr/speech/antitrust-federalism-enhancing-federalstate-cooperation.

¹⁵ Compare, Anti-Monopoly Guideline on Abuse of Intellectual Property Rights (promulgated in draft form by the Anti-Monopoly Comm’n of the State Council, Nat’l Dev. and Reform Comm’n, Dec. 31, 2015) (China), available at http://www.aipia.org/committees/committee_pages/Standards_and_Open_Source/Committee%20Documents/IPR%20Guideline%20%28draft%29%2020151231-EN.pdf with Provisions on Prohibition of Abuse of Intellectual Property Rights to Eliminate or Restrict Competition (promulgated on Apr. 7, 2015 by the State Admin. for Indus. and Commerce) (China), available at <http://www.linklaters.com/pdfs/mkt/beijing/19848090.pdf>.

¹⁶ U.S. DEPT OF JUSTICE & U.S. PATENT & TRADEMARK OFFICE, POLICY STATEMENT ON REMEDIES FOR STANDARDS-ESSENTIAL PATENTS SUBJECT TO VOLUNTARY FRAND COMMITMENTS (Jan. 8, 2013), available at www.justice.gov/sites/default/files/atr/legacy/2014/09/18/290994.pdf. The Section notes that the proposed revisions to the IP Licensing Guidelines do not include a discussion of SEPs.

¹⁷ FTC PAE STUDY, *supra* note 2. This study is the FTC’s “first use of its Section 6(b) authority to investigate transactions in the [IP] marketplace.” *Id.* at 14.

section between IP and antitrust would be welcome where uncertainty remains concerning the agencies' views of the boundaries their policies.

A further discussion of antitrust policy as it relates to IP issues is contained in Section IV-B *infra*.

c. State Action Doctrine

To its credit, the FTC has secured important decisions limiting the scope of the state action doctrine in two recent cases before the Supreme Court, *Phoebe Putney*¹⁸ and *North Carolina Dental Board*.¹⁹ In the aftermath of *North Carolina Dental Board* and in response to the request for advice from state officials and others as to what constitutes antitrust compliance for state regulatory occupations, the FTC staff provided guidance on two issues: (1) When does a state regulatory board require active supervision by the state to invoke the state action defense? and (2) What factors are relevant to determining whether the active supervision requirement is satisfied?²⁰

While the above Guidance clarified some of the issues raised by the Supreme Court's ruling on what constitutes active supervision, the approach taken by the FTC seems to be a statement of best practices and a safe harbor for state supervision of licensing boards. The factors articulated may be viewed as relevant by the FTC staff in interpreting the "constant requirements" of active supervision as set forth in *North Carolina Dental Board* and other Supreme Court precedents.²¹

There continues to be confusion about the Supreme Court's ruling in *North Carolina Dental Board* and, at least with respect to licensing boards, concern by members of such boards about their potential antitrust exposure as individuals. A variety of cases alleging antitrust violations have been brought.²² As the FTC Staff Guidance notes, some cases raise issues that are unlikely to be found to have an anticompetitive effect on competition, as opposed to individual competitors. The agencies have filed amicus briefs in at least two recent Federal cases and have at least one pending investigation in this area.²³

5. Legislation, Regulation, and Executive Action

The Agencies have long advocated against efforts by regulators to limit the application of the antitrust laws. The Section encourages the Agencies to continue to review and comment on Federal legislation and regulations that affect competition policy, agency jurisdiction, and procedures,²⁴ or the ability of agencies to effectuate their missions (including agency budgets).

The Agencies should also continue to be vigilant in monitoring state actions and regulations that may be anticompetitive or designed to protect incumbent firms from competition. The Agencies should continue to provide their expert input with respect

¹⁸ *FTC v. Phoebe Putney Health Sys.*, 133 S. Ct. 1003 (2013).

¹⁹ *FTC v. N.C. State Bd. of Dental Exam'rs*, 135 S. Ct. 1101 (2015).

²⁰ FED. TRADE COMM'N, FTC STAFF GUIDANCE ON ACTIVE SUPERVISION OF STATE REGULATORY BOARDS CONTROLLED BY MARKET PARTICIPANTS (Oct. 2015), available at www.ftc.gov/system/files/attachments/competition-policy-guidance/active_supervision_of_state_boards.pdf. At least two states, California and Oklahoma, have also issued guidance. See California Attorney General Opinion No. 15-402 (Sept. 10, 2015), Oklahoma Executive Order 2015-33 (July 17, 2015); Letter from E. Scott Pruitt, Att'y Gen. of Okla., to All Boards and Commissions with Active Market Participant Majorities (Aug. 17, 2015).

²¹ See Comm'r Maureen K. Ohlhausen, Reflections on the Supreme Court's *North Carolina Dental Board* Decision and the FTC's Campaign to Rein in State Action Immunity, Remarks before the Heritage Foundation (Mar. 31, 2015), available at www.ftc.gov/system/files/documents/public_statements/634091/150403heritagedental.pdf; *State Bd. of Dental Exam'rs*, 135 S. Ct. at 1116-17.

²² See, e.g., *Teladoc v. Texas Medical Board*, No. 1-15-CV-343, 112 F. Supp. 3d 529 (W.D. Tex. 2015) (granting motion for preliminary injunction against anticompetitive rulemaking by self-interested licensing board); *Robb v. Conn. Bd. of Veterinary Med.*, 157 F. Supp. 3d 130 (D. Conn. 2016) (motion to dismiss granted in antitrust suit by veterinarian over his vaccination procedures); *Access Med. Clinic v. Miss. Bd. of Med. Licensure*, No. 3:15-cv-307 (S.D. Miss. 2015) (suit brought challenging board's finding of unauthorized practice of medicine by non-physician owners of pain management practice) (subsequently dismissed); *Henry et al., v. N.C. Acupuncture Licensing Bd. et al.*, No. 1:15-cv-831 (M.D.N.C. 2015) (suit by physical therapists and patients regarding cease and desist letter from the board regarding dry needling services).

²³ Brief for Amicus United States of America, *Solarcity v. Salt River Project Agricultural Improvement and Power District*, No. 15-17302 (9th Cir. Jun. 7, 2016); Brief for the United States and Fed. T. Comm'n, *Teladoc*, No. 16-50017 n.1 (5th Cir. Sept. 9, 2016) (disclosing parallel FTC investigation).

²⁴ For example, the SMARTER Act would: (1) create identical standards for the FTC and Division for obtaining a preliminary injunction against a proposed merger or acquisition; and (2) eliminate the FTC's ability to pursue administrative adjudication to challenge a proposed transaction when it seeks a preliminary injunction in court. H.R. 2745, 114th Cong. (2016).

to state laws that: (1) involve occupational licensing;²⁵ (2) add unnecessary new barriers to entry to platform and sharing companies, like Uber or AirBnB;²⁶ (3) place anachronistic distribution requirements on innovative, vertically integrated companies (e.g., laws to exclude car manufacturers from operating in states without physical dealer locations);²⁷ and (4) circumvent the antitrust laws in the healthcare area, including, but not limited to, Certificate of Public Advantage (COPA) laws and Certificate of Need (CON) laws.²⁸

To effectively and efficiently perform their antitrust and consumer protection missions, the Agencies must receive sufficient funding to attract and retain competent staff, conduct investigations, and engage in all the other enforcement activities on which consumer welfare depends. Given that the U.S. economy and population are projected to grow, it is plausible that the Agencies would need more resources to enable them to continue to effectively carry out their role in protecting consumers, but as always in the competition for appropriations, a compelling argument must be articulated. We encourage the Agencies to advocate for the resources they require, and to ensure that the quality of their work is not undermined by the quantity of demands placed upon them.

Finally, the Section notes that, on April 15, 2016, President Obama issued an Executive Order (E.O.) requiring executive agencies to “identify specific actions that they can take in their areas of responsibility to build upon efforts to detect [competitive] abuses . . . [and] address undue burdens on competition.”²⁹ This E.O. opens opportunities for the Agencies to ensure that sound competition policy is appropriately and effectively recognized and utilized by executive agencies and departments. The Division and FTC should participate in the antitrust reviews. Their advocacy would enhance the regulatory impact analyses that agencies are already required to undertake. In light of this mandate, the Administration may also consider whether a public competitive impact analysis should be undertaken in connection with proposed regulations.³⁰

B. Cartel Enforcement

1. Introduction

Over the past two decades, the Division has transformed cartel enforcement for the better. The Division’s enforcement efforts have had unparalleled success, an accomplishment that has had dramatic global implications. Today, more than 120 countries have cartel enforcement regimes; bid-rigging, market allocation and price-fixing are now criminal offenses in more than 20 of these jurisdictions. From the lysine and citric acid cases that first raised the specter of parallel enforcement actions, and the nine-digit fines and substantial jail sentences, to the more recent, sprawling automotive parts investigations, prosecution and defense of international

²⁵ E.g., *Competition and the Potential Costs and Benefits of Professional Licensure, before the H. Comm. on Small Bus.*, 113th Cong. (2014) (statement of Andrew Gavil, Dir. Office of Policy Planning, Fed. Trade Comm’n) (providing an overview of the FTC’s advocacy efforts in the area of occupational licensing).

²⁶ E.g., Workshop Transcript, The “Sharing” Economy: Issues Facing Platforms, Participants, and Regulators (June 9, 2015), available at www.ftc.gov/system/files/documents/public_events/636241/sharing_economy_workshop_transcript.pdf (examining competition, consumer protection, and economic issues arising in the sharing economy).

²⁷ E.g., Workshop Transcript, Auto Distribution: Current Issues and Future Trends (Jan. 19, 2016), available at https://www.ftc.gov/system/files/documents/public_events/895193/auto_distribution_transcript.pdf (including a discussion of restrictions on manufacturers’ ability to engage in direct selling and new technological developments affecting distribution, among other topics).

²⁸ E.g., FED. TRADE COMM’N & DEP’T OF JUSTICE, ANTITRUST DIV., JOINT STATEMENT ON CERTIFICATE-OF-NEED LAWS AND SOUTH CAROLINA HOUSE BILL 3250 (2016), available at www.ftc.gov/system/files/documents/advocacy_documents/joint-statement-federal-trade-commission-antitrust-division-u.s.department-justice-certificate-need-laws-south-carolina-house-bill-3250/160111ftc-doj-sclaw.pdf (advocating for repeal of South Carolina’s CON law). The FTC has also submitted comments in opposition to New York, Virginia, Tennessee, West Virginia, and Alabama COPA laws. See, e.g., Comment by the FTC regarding Certificate of Public Advantage Applications Filed pursuant to New York Public Health Law, 10 NYCRR, Subpart 83-1 (Apr. 22, 2015), available at https://www.ftc.gov/system/files/documents/advocacy_documents/ftc-staff-comment-center-health-care-policy-resource-development-office-primary-care-health-systems/150422newyorkhealth.pdf.

²⁹ Exec. Order 13,725, 81 Fed. Reg. 23,417 (Apr. 15, 2016), available at www.whitehouse.gov/the-press-office/2016/04/15/executive-order-steps-increase-competition-and-better-inform-consulters.

³⁰ Such requirement would be similar to the regulatory impact analysis that is already required of executive agencies undertaking new regulatory initiatives. See Exec. Order 12,866, 58 Fed. Reg. 51,735 (Sept. 30, 1993); OFFICE OF MGMT. & BUDGET, EXEC. OFFICE OF THE PRESIDENT, CIRCULAR A-4, REGULATORY ANALYSIS (2003).

cartel investigations have grown increasingly complex in the United States and in jurisdictions around the world.

Over the last decade, the Division has collected more than \$11 billion in criminal fines and penalties; 98 percent of these fines were collected in connection with prosecution of international cartels.³¹ The average corporate fine has also increased over the last decade. Until 1994, the largest corporate fine imposed for a single Sherman Act violation was \$6 million.³² Today, fines of \$10 million or more are commonplace, including fines in excess of \$100 million.³³ More than sanctions, these amounts represent a fraction of the value to consumers of this enforcement activity.

The Section commends the Division on its remarkable successes, and offers several recommendations to ensure that the criminal enforcement program remains vibrant and effectively deters future violations.

2. Corporate and Individual Leniency Policies

The Division adopted the current version of its Corporate and Individual Leniency Policies in 1993, and these policies remain the mainstay of the Division's anti-cartel enforcement efforts.³⁴

These policies work because they are transparent and because the Division promotes them widely and implements them carefully and consistently.³⁵ The Section encourages the Division to maintain these efforts, seek out opportunities to promote the Leniency Policies, and clarify any uncertainties through public statements. Practical guidance in the form of a "case study" addressing requirements or expectations for securing first-in conditional leniency (*e.g.*, timing, document productions, proffers, and employee interviews) and unconditional leniency (*e.g.*, full or partial restitution) would further the bar's and the business community's understanding of the Leniency Programs and what applicants should expect when seeking conditional and, ultimately, unconditional leniency. The Section encourages the Division to continue its efforts to increase transparency and provide information about its operations.

The Division has played, and continues to play, a leading role in developing cartel prosecution processes, including the development and operation of its own leniency programs for corporations and individuals. The Section commends the Division for making these developments transparent to the world through its prosecutions, speeches, policy statements, and model agreements.³⁶ The Division also takes seriously its emissary responsibilities by having its most senior and experienced prosecutors attend antitrust conferences, such as the International Cartel Workshop, the Organisation for Economic Co-operation and Development (OECD), and the ICN. The Division also meets formally and informally with prosecutors and enforcers the world over. Leniency has become the hallmark of nearly every cartel enforcement regime around the world; more than 50 countries have adopted leniency programs.³⁷ We encourage the Division to remain engaged with these activities and events in order to promote the adoption and operation of transparent (and ultimately mutually beneficial) leniency programs throughout the world.

3. Sentencing Complexities

A concern is spreading among the members of the antitrust defense bar that sentencing and fining processes for cartel prosecutions here and abroad are becoming too complex to understand. The ranges of imposed sentences and fines are so broad that it is unclear as to how such outcomes were determined. Transparent and fair outcomes following cartel investigations are important for the companies and individuals that find themselves in such matters. If the resolution (*i.e.*, jail time to be served and the fines to be paid) cannot be understood or is perceived to be unfair, companies and individuals may choose not to cooperate. In the past, the Division

³¹ U.S. Dep't of Justice, Congressional Submission FY 2017 Performance Budget 4, available at www.justice.gov/jmd/file/821001/download.

³² *Id.*

³³ U.S. Dep't of Justice, Sherman Act Violations Yielding a Corporate Fine of \$10 Million or More (Sept. 12, 2016), available at www.justice.gov/atr/sherman-act-violations-yielding-corporate-fine-10-million-or-more.

³⁴ See, *e.g.*, Scott Hammond, Deputy Ass't Att'y Gen., Antitrust Div., U.S. Dep't of Justice, The Evolution of Criminal Antitrust Enforcement Over the Last Two Decades, Remarks at the 24th Annual Nat'l Institute on White Collar Crime (Feb. 25, 2010), available at www.justice.gov/atr/file/518241/download.

³⁵ *Id.*

³⁶ See, *e.g.*, Scott Hammond, Deputy Ass't Att'y Gen., U.S. Dep't of Justice, Antitrust Div., Cornerstones of an Effective Leniency Program, Presented before the ICN Workshop on Leniency Programs (Nov. 22–23, 2004), available at www.justice.gov/atr/speech/cornerstones-effective-lenieny-program.

³⁷ See, *e.g.*, Hammond, *supra* note 35.

has consistently provided guidance and transparency with respect to its sentencing policies and procedures, including the interpretation and implementation of the Sentencing Guidelines.³⁸ The Section encourages the Division to reexamine the fundamental building blocks of the sentencing process, including, most importantly, the volume of commerce (VOC) determinations in domestic and international cartel cases. VOC determinations can present highly troubling risks of “double counting” and unfair sentencing outcomes in international cartel cases. These risks are heightened in cases involving component products and in cases where enforcers in different jurisdictions adopt differing approaches to calculating the relevant VOC. The Section encourages the Division to adopt measures for treating VOC determinations consistently across its cases and to promote greater coordination and consistency among enforcers making VOC determinations in international cartel cases. If, upon a closer review, the Division identifies gaps in its prior guidance, the Section encourages the Division to issue general statements of enforcement policy about VOC determinations or any other factor in the sentencing process.³⁹

4. Individual Responsibility

The Division has always focused considerable attention on the role of individual executives in antitrust enforcement and over the years has developed an aggressive and increasingly well-calibrated record of incarceration of the executives who most heavily participated in and personally directed the illegal conduct. The United States is sending twice as many individuals to prison for cartel offenses as it did in the 1990s.⁴⁰ During this period, average prison terms have grown to two years.⁴¹ The Division has been especially successful at building cases against foreign executives in international cartel cases. To date, nearly 90 foreign defendants have served or have been sentenced to serve prison sentences in the U.S. for antitrust violations.⁴²

In the wake of the Yates Memo,⁴³ the Division has intensified its focus on holding individuals accountable.⁴⁴ In relevant part, the Yates Memo requires the cooperating corporation to provide all information against its own culpable executives in order to obtain corporate credit in plea (and potentially leniency) negotiations. The Yates Memo provides that the Department will not release executives as part of a cooperation deal with a corporation or resolve matters with the corporation until the Department has a clear plan to resolve actions against the individuals. Finally, the Yates Memo instructs the Department to pursue prosecution of executives in both civil and criminal cases.

The Section encourages the Division to provide clear and transparent guidance as to how the Yates Memo will affect Division enforcement and prosecution efforts. Specifically, further guidance is needed on the definition and identification of the “highest ranking, most culpable employee,” and how and when the Division will negotiate “carve-in” and “carve-out” determinations. The Section also urges the Division to provide explicit guidance addressing when, if ever, individuals would be

³⁸ For example, the Division recently released updated annotated versions of the model corporate and individual plea agreements; the Section commends the Division for continuing to offer such practical and helpful guidance. See U.S. Dep’t of Justice, Antitrust Div., Model Annotated Corporate Plea Agreement (Aug. 29, 2016), available at <https://www.justice.gov/atr/file/889021/download>; U.S. Dep’t of Justice, Antitrust Div., Model Annotated Individual Plea Agreement (Aug. 29, 2016), available at <https://www.justice.gov/atr/file/888481/download>. See also *United States v. Kabaya Indus. Co., Ltd. d/b/a KYB Corp.*, NO. 1:15-cr-98 (S.D. Ohio 2015); Gary R. Spratling, Deputy Ass’t Att’y Gen., Antitrust Div., U.S. Dep’t of Justice, *Transparency in Enforcement Maximizes Cooperation from Antitrust Offenders*, Address at Fordham University School of Law (Oct. 15, 1999), available at <https://www.justice.gov/atr/speech/transparency-enforcement-maximizes-cooperation-antitrust-offenders>; Hammond, *supra* note 35.

³⁹ In the 2012 Presidential Transition Report, the Section recommended that “given the rapidly expanding state of global cartel enforcement, consideration might be given to whether it would be worthwhile for the Division to coordinate with foreign jurisdictions on how VOC calculations are handled in order to create a uniform approach and more effectively allocate VOC among relevant jurisdictions.” The Section renews this recommendation.

⁴⁰ U.S. Dep’t of Justice, Antitrust Div., Division Update Spring 2015, available at www.justice.gov/atr/division-update/2015/criminal-program-update.

⁴¹ U.S. Dep’t of Justice, Antitrust Div., Division Update Spring 2016, Criminal Enforcement Trends Charts, available at www.justice.gov/atr/criminal-enforcement-fine-and-jail-charts.

⁴² FY 2017 Performance Budget, *supra* note 32.

⁴³ See Memorandum of Deputy Att’y Gen. Sally Quinn Yates, *Individual Accountability for Corporate Wrongdoing* (Sept. 9, 2015), available at www.justice.gov/dag/file/769036/download.

⁴⁴ See, e.g., Brent Snyder, Deputy Ass’t Att’y Gen., U.S. Dep’t of Justice, Antitrust Div., *Individual Accountability for Antitrust Crimes*, Remarks at the Yale Global Antitrust Enforcement Conference (Feb. 19, 2016), available at www.justice.gov/opa/speech/deputy-assistant-attorney-general-brent-snyder-delivers-remarks-yale-global-antitrust.

charged in civil antitrust enforcement actions and explain the rationale for that practice.

5. Compliance Programs and Sentencing Credit

The Section commends the Division's recognition of companies' compliance efforts in recent public statements and sentencing proceedings.⁴⁵ To date, the Division has offered sentencing benefits to corporate defendants that implemented more robust antitrust cartel compliance measures after their prior misconduct had been discovered.⁴⁶ The Section applauds this development and believes that it brings the Division closer in line with the provisions of the United States Sentencing Guidelines.⁴⁷ The Section encourages the Division to expand its review of compliance programs in place prior to the occurrence of the misconduct, and to consider providing appropriate credit for robust compliance programs. Such recognition would reward companies that go well beyond adopting corporate statements and conducting online training, and encourage more companies to engage in sample audits of behavior, review trade association travel and agendas, document investigative and disciplinary procedures, monitor e-mail traffic for competitor contacts, and adopt a "tone at the top" that deters competitor misconduct. The Section respectfully suggests that the opportunity to earn sentencing credit for robust compliance programs would be a very attractive "carrot" that would foster compliance well beyond individual enforcement actions.⁴⁸

As a way to proceed, the Section recommends that the Division pursue an open dialogue with the bar and business community regarding adoption of "robust" and effective compliance methods and improved detection and screening techniques. A first step might be a Division-hosted roundtable discussion that compares and contrasts what works and what does not work, what is "exemplary" vs. ordinary, and what could be scored positively under the United States Sentencing Guidelines and by the Division. Another step could be a request for comments from the antitrust bar and business community in order to develop antitrust-specific minimum compliance guidelines and identify those exemplary compliance measures which could support a reduction in sentencing upon the detection of offense.

6. Cartel Detection

Cartels are among the greatest threats to a competitive economy, and effective cartel enforcement in the United States is one of the most important missions of modern antitrust law.⁴⁹ The Division's successes in pursuing this mission have depended in large part on the contributions of leniency applicants and other informants.⁵⁰ To expand on the success of its program, the Section encourages the Division to be more proactive in identifying possible cartels. Such activity might include the examination of empirical evidence to see where cartel pricing may exist, intersected with or supplemented by examination of settings particularly conducive to collusion. Detection would be enhanced through greater outreach to industry trade groups, large buyers, or others that may be in a position to observe suspicious activity. What, if any, enforcement action would then be appropriate will depend on the magnitude of possible overcharges, the nature and extent of preliminary indications that illegal activity may be taking place, and the feasibility of focused follow-on activity (rather than fishing expeditions) that might identify whether, in fact, serious violations have occurred.

The Division's outreach and education efforts with federal, state and local law enforcement agencies and state attorneys general have been helpful. These "on-the-ground" agencies are well-suited to detect cartels and to learn about potential antitrust misconduct, for example, in association with local procurements. In the past, the Division's close relationships with these local agencies generated many long-

⁴⁵ See, e.g., Brent Snyder, Deputy Ass't Att'y Gen., U.S. Dep't of Justice, Antitrust Div., Remarks at the Sixth Annual Chicago Forum on Int'l Antitrust, (Jun. 8, 2015) available at <https://www.justice.gov/opa/speech/deputy-assistant-attorney-general-brent-snyder-delivers-remarks-sixth-annual-chicago>.

⁴⁶ United States v. Kayaba Indus. Co., Ltd. d/b/a/KYB Corp., No. 1:15-cr-98 (S.D. Ohio 2015).

⁴⁷ U.S. Sentencing Guidelines Manual §§ 8B2.1, 8D1.4 (U.S. Sentencing Comm'n 2013).

⁴⁸ Cf. Brent Snyder, Deputy Ass't Att'y Gen., Compliance Is a Culture, Not Just a Policy, Remarks as Prepared for the International Chamber of Commerce and United States Council of International Business Joint Antitrust Compliance Workshop (Sept. 9, 2014), available at www.justice.gov/atr/file/517796/download.

⁴⁹ See, e.g., Thomas O. Barnett, Ass't Att'y Gen., Antitrust Div., U.S. Dep't of Justice, Global Antitrust Enforcement, Speech at Georgetown Law Center Global Antitrust Enforcement Symposium (Sept. 26, 2007), <https://www.justice.gov/atr/speech/global-antitrust-enforcement>; ANTI-TRUST MODERNIZATION COMM'N, REPORT AND RECOMMENDATIONS 247 (2007), available at http://govinfo.library.unt.edu/amc/report_recommendation/amc_final_report.pdf.

⁵⁰ See, e.g., Hammond, *supra* note 35.

standing and important prosecutions successes, such as with the school milk and school bus conspiracies.⁵¹ Military procurement cartel cases were also built in cooperation with Department of Defense Inspector Generals and related investigators.⁵²

7. Prohibitions on Leniency Disclosures

The Section commends the Division on its realistic and balanced view regarding the demands on public and even private companies to make appropriate constituent (e.g., employee, shareholder, and auditor) disclosures about antitrust events, including the application for, and the receipt of, conditional leniency or the service of a grand jury subpoena at the outset of an investigation. The Division recognizes that its immediate investigative interests must be balanced against the obligations of its investigative subjects and targets to serve the important public interest of keeping constituents, including actual and prospective shareholders, informed of material developments.⁵³ By contrast, leniency programs in other jurisdictions like the European Commission go further in restricting a cooperating company's ability to disclose the existence and content of a leniency application, and statements submitted may not be used for any other purpose other than the Commission's own cartel proceedings.⁵⁴ The Section believes that confidentiality restrictions imposed by other competition authorities deprive U.S. firms of the opportunity to satisfy investor or other constituent needs for material information, and may conflict with U.S. securities law requirements. The Section encourages the Division to provide private or public consultative guidance to these other jurisdictions regarding confidentiality restrictions (whether outright bans or prior-consent requirements) in leniency programs that would force a company to choose between the benefits of the program and the need to inform constituents of material developments.

C. Civil Enforcement and Litigation

Antitrust litigation is notoriously complex—a daunting exercise for the litigants and the courts. The typical case involves substantial testimony from economists and other experts, esoteric theories, hypothetical constructs, and predictions about the future, all before a judge who may never have encountered such a case before. The stakes can be extraordinarily high, with billions of dollars and the structures of industries riding on the decisions. The quality of court decisions regarding mergers and other antitrust cases is central to the Agencies' work, valuable to businesses seeking to better understand what types of conduct are lawful, and critical to the economy that depends on the right outcomes. Accordingly, improvements in the quality of adjudication could yield substantial payoffs.

The Section proposes that the Agencies launch a joint project to identify and recommend potential improvements in the conduct of antitrust civil litigation in the Federal courts. We recommend that the Agencies convene a working group that includes their most experienced litigators, members of the private bar, economic consultants, and Federal judges to formulate proposals regarding the conduct of com-

⁵¹ See R. Lanzillotti, *The Great School Milk Conspiracies of the 1980s*, 11 REV. OF INDUS. ORG. 413 (1996); Press Release, U.S. Dep't of Justice, Justice Department Reaches Settlement with Dean Foods Company (Mar. 29, 2011), available at <https://www.justice.gov/opa/pr/justice-department-reaches-settlement-dean-foods-company>; Press Release, U.S. Dep't of Justice, Five School Bus Owners Indicted for Bid-Rigging and Fraud Conspiracies at Puerto Rico Public School Bus Auction (May 21, 2015), available at <https://www.justice.gov/opa/pr/five-school-bus-owners-indicted-bid-rigging-and-fraud-conspiracies-puerto-rico-public-school>; Anne K. Bingham, Ass't Att'y Gen., and Gary R. Spratling, Deputy Ass't Att'y Gen., Antitrust Div., U.S. Dep't of Justice, Criminal Antitrust Enforcement, Presentation before the Criminal Antitrust Law and Procedure Workshop, ABA Section of Antitrust Law (Feb. 23, 1995), available at <https://www.justice.gov/atr/speech/criminal-antitrust-enforcement-joint-address-aag-anne-k-bingaman-and-daag-gary-r-spratling>.

⁵² Press Release, U.S. Dep't of Justice, Navy Civilian Engineer Pleads Guilty to Attempted Espionage (June 15, 2015), available at <https://www.justice.gov/opa/pr/navy-civilian-engineer-pleads-guilty-attempted-espionage>; Press Release, U.S. Dep't of Justice, Former U.S. Navy Contractor Pleads Guilty to False Statement Charges (Feb. 23, 2016), available at <https://www.justice.gov/usao-mdpa/pr/former-us-navy-contractor-pleads-guilty-false-statement-charges>; Scott D. Hammond, Ass't Att'y Gen., Antitrust Div., U.S. Dep't of Justice, Detecting and Detering Cartel Activity through Effective Leniency Program, Speech Before the International Workshop on Cartels (Nov. 21–22, 2000), available at <https://www.justice.gov/atr/speech/detecting-and-detering-cartel-activity-through-effective-leniency-program>.

⁵³ Scott Hammond, Ass't Att'y Gen., Antitrust Div., U.S. Dep't of Justice, An Update of the Antitrust Division's Criminal Enforcement Program, Speech Before the ABA Section of Antitrust Law Cartel Enforcement Roundtable (Nov. 16, 2005), available at <https://www.justice.gov/atr/speech/update-antitrust-divisions-criminal-enforcement-program>.

⁵⁴ See European Commission, Competition, Cartels, <http://ec.europa.eu/competition/cartels/leniency/leniency.html>.

plex antitrust adjudication. Involvement of these stakeholders in the formulation of the proposals will enhance their credibility as balanced enhancements to the litigation process and increase the likelihood of their adoption and success. The Agencies could use the recommendations from the working group to suggest alternative modes of proceeding in future cases. Lessons learned from these experiences could enable more informed decisions about the efficacy of the techniques implemented, what refinements or supplements may be warranted, and which innovations should be implemented more broadly.

The Section notes that the Agencies are in a unique position both to convene such a working group and to foster the implementation of new approaches to litigation. For example, if a particular proposal were to be endorsed, the Agencies could announce, in advance, their intention to recommend it to judges in the next set of cases they bring. This approach would avoid the concern that the Agencies were proposing procedural suggestions opportunistically.

Topics that may merit exploration and discussion include the sequencing of presentations at trial and increased use of court-appointed experts.⁵⁵ With respect to the first possible topic, the working group might explore alternative trial structures, including the organization of trial presentations by issue, rather than by party (*e.g.*, where the plaintiff or government presents its entire case, followed by defendant). Similarly, experts' appearances could be broken up and sequenced so that testimony addressing a particular question might be followed immediately by the opposing expert's testimony on the same topic, with rebuttal right after that. Another emerging concept that has faced some resistance but nevertheless warrants experimentation and further study involves having experts appear side by side so that questions may be put to both experts simultaneously and to allow for direct exchanges between the experts.⁵⁶

With respect to the second possible topic, the working group might explore ways in which the parties and the court could make greater use of court-appointed experts.⁵⁷ A court-appointed expert might supplement parties' experts, either operating independently or acting after the two sides' expert reports have been submitted. A court-appointed expert might also be used to aid in the conduct of trial. For example, if the two parties' experts were to testify side by side, a court-appointed expert might help to question them or join the group in the discussion, offering opinions in addition to posing queries.⁵⁸ Court-appointed experts might also assist in the structuring of litigation. Court-appointed experts might be able to identify an issue that, if addressed early, may more quickly and efficiently resolve a dispute or narrow disagreement. Before trial, they might distinguish issues on which the contesting experts largely agree and focus the trial on areas where disagreement remains. After trial, they might articulate significant areas of remaining disagreement and provide a common template for addressing them in post-trial briefings.

The Section, in proposing that the working group convened by the Agencies consider these and other topics, is motivated in part by positive reports on the use of related techniques in other legal systems. For example, in Australia, Canada, and New Zealand, the courts sometimes have experts appear together,⁵⁹ and arbitration is often successful with a more informal and interactive approach. These other models may help generate ideas and give reason to believe that alternatives exist that may be superior.

⁵⁵ While the Section provides these two topics by way of example, and recommends that these and other issues be the subject of further exploration and discussion, the Section has not considered the merits of these proposals and does not take a position on their adoption.

⁵⁶ Other jurisdictions have experimented with a form of this approach, sometimes referred to by supporters and critics alike as "hot tubbing." CIVIL JUSTICE COUNCIL, CONCURRENT EXPERT EVIDENCE AND 'HOT-TUBBING' IN ENGLISH LITIGATION SINCE THE 'JACKSON REFORMS': A LEGAL AND EMPIRICAL STUDY (July 2016); Steven Rares, *Using the "Hot Tub"—How Concurrent Expert Evidence Aids Understanding Issues*, 95 J. INTELL. AND INDUST. PROP. SOC'Y OF AUSTRALIA AND NEW ZEALAND 28 (2013). Some commentators have advocated for its adoption in the United States. See Scott Welch, *From Witness Box to the Hot Tub: How the "Hot Tub" Approach to Expert Witnesses Might Relax an American Finder of Fact*, 5 J. INT'L COMM. L. AND TECH. 154 (2010) ("The Australian concurrent evidence procedure, informally known as "hot tubbing," may provide an excellent opportunity for a court to more thoroughly understand the issues between, and testimony of, expert witnesses.")

⁵⁷ See J. Gregory Sidak, *Court-Appointed Neutral Economic Experts*, 9(2) J. COMPETITION L. & ECON., 359–394 (2013) (arguing that "wider use of Rule 706 would assist the judge and jury and would facilitate the prompt settlement of intellectual property, antitrust, securities, contract, business tort, and other complex disputes.")

⁵⁸ Garry Downes, *Problems with Expert Evidence: Are Single or Court-Appointed Experts the Answer?*, 15 J. JUDICIAL ADMIN. 185 (2006).

⁵⁹ See Rares, *supra* note 57.

D. Mergers

Antitrust merger enforcement should remain a major focus of the Agencies. While there is broad support for the basic framework of U.S. antitrust merger analysis, concerns exist with the level of transparency into how that framework is being applied by the Agencies, the effectiveness of merger policy and the tools used to apply it, and the impact of procedural differences between merger litigation conducted by the Division and the FTC. The Section recommends that the Agencies address concerns about transparency and effectiveness through more detailed use of Competitive Impact Statements and Aids to Analysis of Public Comment, increased utilization of closing statements, and public presentation of detailed merger retrospective studies. To address concerns over procedural differences between the two Federal enforcement agencies in merger litigation, the Section recommends that the Administration endorse legislation that would require the FTC to invoke Section 15 of the Clayton Act, 15 U.S.C. §25, to challenge unconsummated mergers in Federal court.

1. Increased Transparency

While the Agencies traditionally have maintained a shared commitment to providing transparency in their approach to merger enforcement, the Section believes that there would be substantial public benefit if the Agencies were to provide even greater transparency into their thinking about merger enforcement practices and standards. Transparency increases public confidence in merger enforcement decisions, enables more rigorous assessment of the effectiveness of merger policy, and contributes to general deterrence of transactions the Agencies believe to be anti-competitive by enabling merging parties and their counsel to self-police against more clearly revealed standards (thus also conserving agency resources). By increasing transparency in U.S. merger enforcement, the Agencies will also be modeling best practices that can be adopted by enforcement authorities around the world—authorities that play an increasingly significant role in multi-jurisdictional merger review.

Litigated merger cases present great opportunities for transparency, as the Agencies must prove their cases in court, but there are ways in which the merger litigation process might be improved to increase transparency. The Section recommends that the Agencies, while protecting legitimate interests in the confidentiality of commercially and competitively sensitive business information, should encourage the courts (1) to conduct merger trials in open court, and (2) to require public versions of expert reports so that analytical models, empirical methods, and their application can be evaluated.

The inclusion of more detailed discussions of analytical models and empirical methods in some Division Competitive Impact Statements and FTC Aids to Analysis of Public Comment has fostered greater transparency into the thinking behind settled merger investigations. More often than not, however, those important documents merely reiterate points made in the complaint without offering greater insight into the foundations for those allegations. The Section recommends that the Agencies further enhance transparency by making greater use of Competitive Impact Statements and Aids to Analysis of Public Comment to reveal the foundations both for complaint allegations and remedies accepted.

Increased utilization of closing statements for those merger investigations not resulting in agency action is perhaps the greatest source of incremental transparency in that public knowledge of those matters is the weakest. After averaging over three closing statements per year in investigations of Hart-Scott-Rodino (HSR) reportable transactions closed between 2011 and 2013, the Agencies have issued only three closing statements in total for investigations of HSR reportable transactions closed between 2014 and the present, and none this year.⁶⁰ The Section recommends that the Agencies commit to issuing more frequent closing statements in most Hart-Scott-Rodino reportable second request investigations not resulting in a contested complaint or consent order, particularly to clarify important considerations of enforcement policy or implementation. Over time, the Agencies should consider issuing closing statements in all Hart-Scott-Rodino reportable second request investigations. In the past four Fiscal Years, the Agencies have commenced fewer than fifty second request investigations per year, more than half of which resulted in contested complaints or consent orders, so this suggestion would require issuing only fewer than

⁶⁰The Section calculated the above-referenced data as of October 17, 2016. See Press Releases, Antitrust Div., Dep't of Justice, available at [www.justice.gov/justice-news?keys=&component=376&topic=All&date\[value\]\[month\]=&date\[value\]\[year\]=&items_per_page=25](http://www.justice.gov/justice-news?keys=&component=376&topic=All&date[value][month]=&date[value][year]=&items_per_page=25) and Press Releases, Fed. Trade Comm'n Press Releases, available at www.ftc.gov/news-events/press-releases.

twenty-five closing statements per year.⁶¹ By way of comparison, the European Commission issued the equivalent of closing statements in roughly seventy transactions per year over the past four calendar years.⁶²

Finally, the Section recommends that retrospective analysis of past enforcement decisions—challenges brought, transactions remedied by consent, and those cleared without agency action—should be performed and the results published with greater frequency in order to enhance transparency. As discussed in more detail *infra*, transparency would be enhanced by the Agencies presenting retrospectives in open workshops that include detailed presentation and discussion of the methods and models employed in past enforcement decisions and how those methods and models were implemented.

2. Evaluating the Effectiveness of Enforcement Policy, Tools and Remedies

Despite broad consensus in the antitrust community in support of the basic framework of antitrust merger analysis, questions have been raised about the effectiveness of merger policy, linking merger policy to various measures of industry concentration regarded as indicators of declining competition.⁶³ The Section recommends that the Agencies utilize retrospective analysis of past merger enforcement decisions to lead a detailed examination of how well merger policy has worked and whether the tools being used to evaluate and remedy mergers are adequate.

There is growing literature on the effect of past mergers. Most merger retrospective studies focus on price effects, but interpretation of the results of those studies may be confounded by quality effects arising from the merger under study or other efficiencies that benefit consumers. For this reason, it is the combination of higher prices and reduced output that is required to conclude that a merger was anti-competitive.⁶⁴ The Section encourages the Agencies to support and undertake merger retrospective studies with price and output effects as part of the study.

Price and output are not the only factors that should be studied to assess a merger's effect. Particularly given the increased emphasis in recent enforcement decisions on the innovation effects of mergers, the Section recommends that post-merger effects on new product introductions, research and development, and other measures of innovation should also be analyzed as part of merger retrospective studies. The impact of mergers and merger enforcement on the behavior of firms in the industry should also be part of the Agencies' merger retrospective studies, particularly whether enforcement in an industry might deter future efficient mergers that might otherwise go forward. In sum, the Section recommends that the Agencies undertake merger retrospectives that take into account not just the effect of mergers on price, but also the effects of mergers on output, product innovation, and future merger activity.

In order to assess the adequacy of the tools used to evaluate mergers, there also needs to be an assessment of the accuracy of those tools in predicting merger outcomes. The Section recommends that the Agencies develop a clear record for each merger of what tools and models were used along with the models' associated assumptions and predictions. With this record in place, the Agencies could then revisit those analyses post-merger in order to determine which models and assumptions worked best. For example, the Agencies could examine how well econometric merger simulation models do in predicting post-merger prices, output, and market shares and which assumptions (*e.g.*, assumed efficiencies, assumed strategies employed by the firms, the instability or imprecision of the parameters estimated in the demand system, or the failure to account for new product introductions) in retrospect were ones that were shown later to be false. The Agencies could also examine whether static merger simulation models were more useful than crude analysis where price is assumed to be a function of market concentration. Similarly, the Agencies could determine the performance of gross upward pricing pressure indices (GUPPIs) compared to market shares or static simulation models.

Problematic mergers can be remedied by a variety of means, including structural solutions—divestitures handled either prior or subsequent to the merger being remedied—and behavioral solutions, though the latter are more controversial. Appro-

⁶¹ See FED. TRADE COMM'N AND DEPT OF JUSTICE, HART-SCOTT-RODINO ANN. REP. APP'X A (FY 2015), available at www.ftc.gov/system/files/documents/reports/federal-trade-commission-bureau-competition-department-justice-antitrust-division-hart-scott-rodino/160801hsrreport.pdf.

⁶² See EUROPEAN COMMISSION MERGER STATISTICS 2016, available at <http://ec.europa.eu/competition/mergers/statistics.pdf>.

⁶³ See COUNCIL OF ECON. ADVISERS, ISSUES, BRIEF, BENEFITS OF COMPETITION AND INDICATORS OF MARKET POWER 9 (Updated May 2016), available at www.whitehouse.gov/sites/default/files/page/files/20160502_competition_issue_brief_updated_cea.pdf.

⁶⁴ See Dennis W. Carlton, *Why We Need to Measure the Effect of Merger Policy and How to Do It*, 5 COMPETITION POL'Y INT'L 1 (2009).

propriately, the Agencies regularly question the efficacy of merger remedies,⁶⁵ and occasionally review them retrospectively. Maintaining confidence in merger remedies should remain a priority of the Agencies. The Section recommends another retrospective study of the effectiveness of the various remedies used. Among other issues, we recommend considering divestitures to “upfront buyers,” divestitures handled by the parties or third-party trustees post-merger, and behavioral remedies, in order to make sure that remedies are appropriate to the transaction and effective at preserving competition.⁶⁶ When the remedies involve behavioral restrictions on information sharing and require monitoring by the Agencies, the Section endorses evaluation of the effectiveness of such remedies on an ongoing basis.

3. *Process Symmetry Between Division and FTC in Merger Enforcement Litigation*

The Section has previously identified the need for greater process symmetry in the standards for the grant of a preliminary injunction motion in merger challenges brought by the Division and the FTC.⁶⁷ The Section recommended administrative action or amendment of Section 13(b) of the FTC Act to ensure that it is applied consistently with traditional equitable standards for injunctive relief applicable to the Division, noting that the outcome of challenges to proposed mergers should depend on the merits of the proposed transaction and the competitive issues it raises, not on procedural differences depending on which Agency happens to draw the case.⁶⁸ The Section did not, however, address the issue of merger challenges through administrative proceedings under Part 3 of the Commission’s Rule of Practice, another procedural difference from DOJ enforcement practice regarded by some as potentially outcome determinative.

Since the Section published its recommendation, the SMARTER Act was introduced in Congress and passed the House of Representatives to harmonize preliminary injunction standards and require the FTC to resolve challenges to unconsummated mergers in Federal court, consistent with the 2007 recommendation of the Antitrust Modernization Commission.⁶⁹ Accordingly, the Section recommends that the Administration support legislation that would require the FTC to invoke Section 15 of the Clayton Act, 15 U.S.C. § 25, to challenge unconsummated mergers in Federal court, a recommendation that is consistent with the 2007 recommendation of the Antitrust Modernization Commission. In making this recommendation, the Section neither endorses nor opposes the approach to these issues taken in the SMARTER Act.

E. Consumer Protection

1. *Introduction*

For decades, the FTC has been the Nation’s premier consumer protection agency. Since the publication of the ABA Report in 1969,⁷⁰ in which the Agency was criticized for its passivity and neglect, the FTC has been a vigorous and effective agency, boasting an aggressive enforcement program to stop unfair or deceptive acts or practices.⁷¹ In the 1980s, the FTC promulgated three seminal documents—the Decep-

⁶⁵ See Renata Hesse, Acting Ass’t Att’y Gen., Antitrust Div., U.S. Dep’t of Justice, *And Never the Twain Shall Meet?: Connecting Popular and Professional Visions for Antitrust Enforcement*, Opening Remarks at the 2016 Global Antitrust Enforcement Symposium 15 (Sept. 20, 2016), available at www.justice.gov/opa/speech/acting-assistant-attorney-general-renata-heese-antitrust-division-delivers-opening.

⁶⁶ See *id.*; see also Edith Ramirez, Chairwoman, Fed. Trade Comm’n, Keynote Remarks at the Tenth Annual Global Antitrust Enforcement Symposium 8–9 (Sept. 20, 2016), available at https://www.ftc.gov/system/files/documents/public_statements/985423/ramirez_global_antitrust_enforcement_symposium_keynote_remarks_9-20-16.pdf.

⁶⁷ See AM. BAR ASS’N, SECTION OF ANTITRUST LAW, PRESIDENTIAL TRANSITION REPORT: THE STATE OF ANTITRUST ENFORCEMENT 2012 at 9–10 (Feb. 2013) [hereinafter 2012 PRESIDENTIAL TRANSITION REPORT], available at http://www.americanbar.org/content/dam/aba/administrative/antitrust_law/at_comments_presidential_201302.authcheckdam.pdf.

⁶⁸ *Id.*

⁶⁹ See The Standard Merger and Acquisition Reviews Through Equal Rules Act of 2015, H.R. 2745 114th Cong. (as passed by the House, March 23, 2016), available at www.congress.gov/bills/114th-congress/house-bill/2745; ANTITRUST MODERNIZATION COMM’N, REPORT AND RECOMMENDATIONS 131–32, 138–41 (Apr. 2007), available at http://go.lib.unt.edu/amc/report_recommendation/amc_final_report.pdf.

⁷⁰ AM. BAR ASS’N, REPORT OF THE ABA COMMISSION TO STUDY THE FEDERAL TRADE COMMISSION (1969) [hereinafter Kirkpatrick Report]. The Kirkpatrick Report was commissioned by President Nixon in response to a scathing critique of the FTC by a Ralph Nader-sponsored group of law students. See E. COX, R. FELLMETH & J. SCHULZ, THE CONSUMER AND THE FEDERAL TRADE COMMISSION (1969).

⁷¹ See Fed. Trade Comm’n, Strategic Plan for Fiscal Years 2014 to 2018 10 (April 30, 2014), available at www.ftc.gov/system/files/documents/reports/2014-2018-strategic-plan/spfy14-fy18.pdf.

tion,⁷² Unfairness,⁷³ and Advertising Substantiation⁷⁴ Policy Statements—that ever since have defined the parameters under which the agency exercises its enforcement authority. In particular, the Deception and Unfairness Policy Statements have served to focus the FTC’s actions on practices that are, or are likely to be, harmful to consumers.⁷⁵

The Section has long recognized the FTC’s key role in protecting consumers from harm, noting in both its 2008 and 2012 Transition Reports that the FTC’s consumer protection mission has exceeded its competition mission in resources,⁷⁶ activity, and public attention. This remains true today.⁷⁷ While the Section has recommendations for improvement, the Section acknowledges and applauds the impressive contributions of the FTC’s consumer protection mission to consumer welfare and a competitive economy.⁷⁸ Indeed, for over 30 years, FTC enforcement efforts have protected consumers from a wide variety of fraudulent, misleading, and unfair practices and have returned many hundreds of millions of dollars to victims injured by these practice.

The FTC, however, is no longer the proverbial primary “cop on the consumer protection beat.” The past four years have witnessed considerable change in the consumer protection law enforcement and regulatory landscape, with both the CFPB and the FCC playing increasingly important roles in consumer protection enforcement; the three agencies have overlapping jurisdiction. Accordingly, the Report includes recommendations for those agencies as well.

2. Overlapping Privacy Jurisdiction

The overlapping jurisdiction of the FTC, the FCC, and the CFPB presents the very real possibility of inconsistent approaches, nowhere more noticeably than in the privacy arena. This was underscored most recently when the FCC adopted its 2015 Open Internet Order and reclassified the provision of Internet broadband access as

⁷²Fed. Trade Comm’n, FTC Policy Statement on Deception (Oct. 14, 1983), available at https://www.ftc.gov/system/files/documents/public_statements/410531/831014deceptionstmt.pdf.

⁷³Fed. Trade Comm’n, FTC Policy Statement on Unfairness (Dec. 17, 1980), available at <https://www.ftc.gov/public-statements/1980/12/ftc-policy-statement-unfairness>.

⁷⁴Fed. Trade Comm’n, FTC Policy Statement Regarding Advertising Substantiation (Mar. 11, 1983), available at <https://www.ftc.gov/public-statements/1983/03/ftc-policy-statement-regarding-advertising-substantiation>.

⁷⁵The Deception Statement defines deception as a representation, omission, or practice that is likely to mislead consumers acting reasonably under the circumstances, in a material way (*i.e.*, in a way that is likely to cause consumer injury). The Unfairness Statement defines an unfair act or practice as one that causes, or is likely to cause, substantial consumer injury that is not reasonably avoidable by consumers and is not outweighed by benefits to consumers and competition. In 1984, Congress enshrined the unfairness definition into the FTC Act as Section 5(n), 15 U.S.C. § 45(n). The Deception Statement’s focus on “consumers acting reasonably” and the Unfairness Statement’s requirement that the injury from the practice not be reasonably avoidable by consumers recognize the role that consumers themselves play in avoiding harm.

⁷⁶See PRESIDENTIAL TRANSITION REPORT, *supra* note 68, at 21 n.48 (February 2013).

⁷⁷The FTC reportedly allotted \$165,879,000, and \$175,043,000, to its consumer protection mission in FY 2015 and 2016, respectively. The allotments exceeded those for competition, which were \$127,121,000 and \$134,163,000, respectively. See Fed. Trade Comm’n, Congressional Budget Justification Summary for FY 2016 38, available at www.ftc.gov/system/files/documents/reports/fy-2016-congressional-budget-justification/2016-cbj.pdf.

⁷⁸For example, the FTC recently settled one of the largest actions brought to date against charity fraud. Between March 2016 and May 2016, the FTC settled charges against four sham charities that claimed to help cancer patients, but instead spent \$187 million of donors’ money on their operators, families and friends, and fundraisers. Under the settlement, the sham charities were permanently dissolved and their assets liquidated, and a multimillion dollar penalty issued. See Press Releases, Fed. Trade Comm’n, *FTC, States Settle Claims Against Two Entities Claiming to Be Cancer Charities; Orders Require Entities to Be Dissolved and Ban Leader from Working for Non-Profits* (Mar. 30, 2016), available at www.ftc.gov/news-events/press-releases/2016/03/ftc-states-settle-claims-against-two-entities-claiming-be-cancer. 2015 was also a record year of debt collection enforcement, with twelve cases brought against fifty-two defendants and nine settlements reaching nearly \$94 million in judgments. See Fed. Trade Comm’n, Annual Highlights 2015, Enforcement, available at www.ftc.gov/reports/annual-highlights-2015. The FTC also continues to target deceptive health claims, settling a complaint in July 2016 against the marketers of a powdered drink mix touted as enabling opiate-addicted consumers to overcome addiction and withdrawal. The terms of the settlement require the company to discontinue all deceptive claims, and to pay \$235,000 as redress or disgorgement. See Press Release, Fed. Trade Comm’n, *Sellers of At-Home Treatment for Opioid Withdrawal and Addiction Barred from Making Deceptive Claims* (July 6, 2015), available at www.ftc.gov/news-events/press-releases/2016/07/sellers-home-treatment-opioid-withdrawal-addiction-barred-making.

a “telecommunications service” under Title II of the Telecommunications Act.⁷⁹ The provision of broadband service by Internet service providers (ISPs) is now deemed a common carrier service. As such, it is exempt from the FTC’s jurisdiction pursuant to the common carrier exemption in the FTC Act. Further, the Court of Appeals for the Ninth Circuit recently held in *FTC v. AT&T Mobility*,⁸⁰ that common carriers are exempt from the FTC’s jurisdiction even in their provision of non-common carrier services.⁸¹ However, the FCC’s authority over non-common carrier services is limited, leaving a potential regulatory gap for non-common carrier services offered by common carriers. Thus, similar activities engaged in by different entities, one of which has common carrier status, may be regulated differently. Over the years, the FTC has urged Congress to repeal the common carrier exemption.⁸² The Section believes that this exemption is outdated and urges the FTC and the FCC to support its repeal.

The potential for inconsistent regulatory approaches is significant, as witnessed by the FCC’s recently adopted Privacy Rules.⁸³ The FCC’s rules take a different approach from the FTC in determining what data is considered sensitive and, therefore, subject to enhanced consent. The FTC has required affirmative or opt-in consent only for uses of certain sensitive types of data including financial, health, precise geolocation and children’s data, for example. The FCC’s approach, on the other hand, largely treats as sensitive other types of data that the FTC has not historically considered sensitive, namely web browsing data and application usage history, and requires opt-in consent for the use of such data. Thus, non-broadband providers subject to FTC authority may collect and use web browsing and application usage data while broadband providers are subject to different requirements for such data. The Section believes these inconsistent approaches warrant ongoing attention and urges the agencies to consider whether these differing approaches have a detrimental effect on competition and consumer welfare.

The overlapping privacy jurisdiction and related inconsistent approaches to privacy enforcement also create confusion among other nation-states when U.S. privacy law is relevant, for example, as part of cross-border data transfers. The European Union’s (EU) data protection law prohibits companies from transferring the personal data of EU data subjects to countries outside of the European Economic Area (EEA) unless those countries have “adequate” privacy laws.⁸⁴ Adequacy is often correlated to an umbrella privacy law that mirrors the EU approach; the United States, however, takes a sectoral approach to privacy. Until October 2015, U.S. companies that certified to the EU–U.S. Safe Harbor Framework could rely on that Framework as a valid legal basis for transferring the data of EU data subjects to the United States.⁸⁵ Based in part on its negative perception of the U.S. sectoral approach to

⁷⁹Protecting and Promoting the Open Internet, GN Docket No. 14–28, Report and Order on Remand, Declaratory Ruling, and Order, 30 FCC Red. 5601 (2015) (hereinafter 2015 Open Internet Order).

⁸⁰*FTC v. AT&T Mobility*, No. 15-16585, 2016 WL 4501685 (9th Cir. Aug. 29, 2016).

⁸¹The FTC Act specifically exempts “common carriers subject to the Acts to regulate commerce” from the Commission’s jurisdiction. 15 U.S.C. § 45(a)(2). The Commission has taken the position that common carriers are exempt from its jurisdiction only to the extent that they are engaged in common carrier activities (an “activity-based exemption”). However, the Ninth Circuit held that common carriers are entitled to that exemption by virtue of their status (a “status-based exemption”). *AT&T Mobility*, 2016 WL 4501685, at *4. In October 2016, the FTC petitioned the Ninth Circuit for a rehearing en banc, challenging the dismissal of the agency’s suit under Section 5. Petition for Rehearing En Banc, *AT&T Mobility*, 2016 WL 4501685 (filed Oct. 13, 2016).

⁸²*See Oversight of the Fed. Trade Comm’n Before the S. Comm. on Commerce, Science, and Transp.*, 114 Cong. 25 (2016) (Statement of the FTC), available at www.ftc.gov/system/files/documents/public_statements/986433/commission_testimony_oversight_senate_09272016.pdf; Maureen K. Ohlhausen, Commissioner, Fed. Trade Comm’n, 100 is the New 30: Recommendations for the FTC’s Next 100 Years, Address at the GCR Antitrust Law Leaders’ Forum 2014 12–14 (Feb. 7, 2014), available at www.ftc.gov/system/files/documents/public_statements/100-new-30-recommendations-ftcs-next-100-years/140207gcrantitrust-mko.pdf; *Consumer Online Privacy: Hearing Before the S. Comm. on Commerce, Science, and Transp.*, 111th Cong. 24–26 (2010) (Statement of the FTC), available at www.ftc.gov/os/testimony/10072consumer_privacy.pdf; H.R. 3402, *The Calling Card Consumer Protection Act: Hearing Before the Subcommittee on Commerce, Trade, and Consumer Protection of the Committee on Energy and Commerce*, 110th Cong. 12–13 (2008), available at www.ftc.gov/os/2008/09/P074406prepaidec.pdf.

⁸³*See* Protecting the Privacy of Customers of Broadband and Other Telecommunications Services, 81 ed. Reg. 23360 (Proposed Apr. 20, 2016), available at www.gpo.gov/fdsys/pkg/FR-2016-04-20/pdf/2016-08458.pdf.

⁸⁴Council Directive 95/46 of the European Parliament and of the Council of Oct. 24, 1995 on the Protection of Individuals with Regard to the Processing of Personal Data and on the Free Movement of Such Data, 1995 O.J. (L 281) 31 (EU).

⁸⁵Under the US–EU Safe Harbor, transfer of personal data from the EU to a U.S. organization was lawful if the U.S. organization receiving the data has unambiguously and publicly dis-

privacy, the European Court of Justice issued a decision in 2015 finding that the EU–U.S. Safe Harbor insufficiently protected EU residents’ personal data.⁸⁶ Following this decision, the EU and the United States negotiated the Privacy Shield, a new legal basis for U.S. companies to rely on when transferring personal data from the EEA to the United States. The Privacy Shield has already attracted critics, however, and some commentators worry that the inconsistent privacy enforcement frameworks among the FTC, the FCC, and the CFPB may weaken the Privacy Shield’s effectiveness.⁸⁷ Reducing the ability for U.S. companies to transfer personal data effectively and appropriately could impact the U.S.’s competitive posture. Although the Section is not advocating for an umbrella privacy law at this time, it does observe that the inconsistent privacy approaches pose a risk of harm to U.S. companies and competition internationally. More consistency among the regulatory approaches would likely yield reduced compliance costs and promote competitiveness with resulting benefit to consumers.⁸⁸

3. Enforcement

Although the FTC has many tools at its disposal to foster compliance with the law, it is, at its core, an enforcement agency. The Section recommends that the FTC adopt a number of reforms to help it deploy its limited enforcement resources in a manner that enhances the impact of its actions while, at the same time, treating target companies in a way that is fair and proportionate to the alleged offenses. Where appropriate, the Report includes parallel recommendations relating to the CFPB and the FCC.

The Section recommends that the FTC adopt reforms to enhance the transparency and fairness of the enforcement process. Government investigations and enforcement actions are inherently different from private disputes. They are not contests between equals—federal agencies have enormous advantages in terms of resources and power. Businesses, especially smaller companies and their principals, simply cannot afford in many cases to take on the risks and costs of defending themselves during an investigation or when confronted with a complaint and order. Unless they are careful in how they use their leverage, the agencies may cause unintended damage to companies and the marketplace without corresponding benefits to consumers or competition. It is critical that the process be fair and transparent.

Case selection: The FTC and CFPB have broad prosecutorial discretion in choosing targets for their law enforcement actions. The Section recommends that the agencies focus their limited enforcement resources on cases involving significant consumer harm. This has not always been the case. Recently, for example, the CFPB has brought actions for technical violations of certain statutes against very small companies, in many cases where the challenged practices—and even the companies themselves—had ceased. The consumer injury in those cases appeared to be minimal, and it was not otherwise apparent what public policy goals the cases served.⁸⁹ From time to time, the FTC also has prosecuted small companies for minor violations.⁹⁰

closed its commitment to comply with the “Safe Harbor Privacy Principles” as set out in the Commission Decision 2000/520, 2000 O.J. (L215) 7 (EC), available at <http://eurlex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX%3A32000D0520%3AEN%3AHTML>. The FTC has brought enforcement actions against companies who have falsely claimed that they were certified members of the Safe Harbor Framework when their certifications had lapsed or they had never applied for membership in the program at all. Press Release, Fed. Trade Comm’n, *Thirteen Companies Agree to Settle Charges They Falsely Claimed To Comply with International Safe Harbor Framework* (Aug. 17, 2015), available at www.ftc.gov/news-events/press-releases/2015/08/thirteen-companies-agree-settle-ftc-charges-they-falsely-claimed.

⁸⁶ Maximilian Schrems v. Data Prot. Comm’r, Case C-362/14, available at curia.europa.eu/juris/document.jsf?docid=169195&doclang=en.

⁸⁷ See, e.g., Nancy Libin *The FCC’s Privacy Problem*, THE HILL, Sept. 22, 2016, available at <http://thehill.com/blogs/congress-blog/technology/297199-the-fccs-privacy-problem>.

⁸⁸ FED. TRADE COMM’N, PROTECTING CONSUMER PRIVACY IN AN ERA OF RAPID CHANGE: RECOMMENDATIONS FOR BUSINESSES AND POLICYMAKERS 9 (2012), available at <https://www.ftc.gov/sites/default/files/documents/reports/federal-trade-commission-report-protecting-consumer-privacy-era-rapid-change-recommendations/120326privacyreport.pdf>.

⁸⁹ See, e.g., In the Matter of Presto Auto Loans, Inc., File NO. 2016–CFPB–0021 (Sept. 20, 2016), available at https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/2016-CFFPB-0021_Document_001_09202016.pdf.

⁹⁰ See, e.g., Nomi Techs., Inc., Docket No. C-4538, 2015 WL 5304114 (F.T.C. Aug. 28, 2015). The dissenting statements of Commissioners Ohlhausen and Wright criticized the majority’s decision to bring the case despite the technical nature of the violations and the absence of evidence of consumer harm. See *id.* at *5, *8. In 1997, the FTC published its Compliance Assistance and Civil Penalty Leniency Policies for Small Entities, which establish a “variety of mechanisms available for small business to obtain” compliance advice and describe the “FTC’s approach to reducing or waiving civil penalties for small entities in various mitigating circumstances.” 62

Continued

The agencies should recognize the enormous impact their law enforcement actions can have, especially on small businesses that, as a result, often lose the assets, customers, business partners, and financing they need to survive.

Civil Investigative Demands: FTC investigations (like those of the CFPB) often begin with the issuance of civil investigative demands (CIDs). The Section recommends that the agencies use this powerful tool judiciously to avoid unnecessary costs to companies and individuals who receive them.

The FTC has broad, but not unfettered, authority to conduct investigations and compel the production of documents and information. The Section recognizes that CIDs must be written broadly enough to ensure that the documents and information necessary to carry out the investigation are produced, especially when the agency is unfamiliar with how the company compiles and maintains its records. Nevertheless, there has been a trend in recent years toward generic and overly-broad CIDs that are not tailored to the nature of the business or the practices at issue. The result in many cases has been that companies have incurred astronomical costs in responding. While the agency staff is willing to some extent to negotiate narrower terms and/or extend production deadlines, small companies and individuals in particular may end up facing resource demands they cannot afford. Just the legal fees alone that targets incur in negotiating the terms of the CID and making the production can be prohibitive. This problem has been exacerbated by the FTC's and CFPB's adoption of specific electronic submission standards that require formats that frequently are different from those used by the company in the ordinary course of business. As a result, the company may be forced to hire third-party contractors—at substantial cost—to transfer the records into the required format.

Although a company can file a petition to quash or limit a CID, these petitions are made public—which imposes considerable reputational costs on a company—and are rarely granted. Rather than casting a net designed to bring in every possible fish, the Agencies should, in the first instance, issue CIDs that are more narrowly focused, with the option of following up with additional CIDs should that be necessary.⁹¹

Information sharing in investigations: The extent to which FTC staff is willing to reveal to an investigational target the practices about which they have concerns and the legal theories underlying those concerns varies widely from case to case. In some cases, the staff has encouraged open discussions at an early stage of the investigation so that the company understands the nature of, and theories underlying, the investigation and has an opportunity to provide countervailing evidence or arguments before decisions are made. In other cases, the company only finds out what the matter is about when confronted with a proposed complaint and order that has been authorized by the Director of the Bureau of Consumer Protection (BCP). Even at this point, the company may not be told what the real basis for the charges is, and the proposed pleadings may not make it clear. In these cases, the company is at a severe disadvantage and is forced to decide how to respond based on incomplete information. The need for greater transparency begins with the resolution issued by the Commission authorizing the use of compulsory process. The resolution ostensibly is designed to give the CID recipient notice of the nature of the investigation. In practice, the “omnibus” resolutions the FTC commonly uses are broad and generic and provide little guidance or any real boundaries on the scope of the investigation.

In litigation, where pleadings precede discovery, parties have access to the basis for information demands. That context is fundamental to the process whereby parties invoke and courts apply the balancing test of relevance and burden that governs discovery under the Federal Rules of Civil Procedure. Subjects of government investigations should also have the information necessary to understand demands that can impose significant costs and consequences. The Section recommends that the FTC adopt internal guidelines for staff on communicating with investigational targets about the contemplated law enforcement action. Absent compelling circumstances indicating otherwise, staff should be as transparent as possible, as early as possible in the process, and should encourage a dialogue on the substantive

Fed. Reg. 16809 (Apr. 8, 1997). Although the Policies only apply to civil penalties and not to other remedies the FTC can pursue, they evidence the importance of the FTC carefully considering the impact of its actions on small businesses. The FTC recently reaffirmed the Policies in announcing dramatic increases in the maximum civil penalties it can seek for violations of various laws and rules enforced by the FTC. Adjustment of Civil Monetary Penalty Amounts, 81 Fed. Reg. 42476 (June 30, 2016).

⁹¹Some recent CIDs have sought all information that might possibly relate to violations of virtually every consumer protection law that might apply. Although the FTC does not need “reason to believe” a specific violation has occurred before commencing an investigation, it should minimize the use of these types of fishing expeditions.

issues. This is not only fairer to the company, but is likely to result in enforcement recommendations that are more thoughtful and better supported. This will also help focus the investigation (and remediation) more effectively, avoiding the broad CID requests and responses addressed above.

The Section recommends that the CFPB adopt similar guidelines. The CFPB often uses its Notice of Opportunity to Respond and Advise (NORA) process to notify companies in general terms of the allegations against them. As is the case with the FTC's consent authority process, however, the NORA notification takes place after staff and their supervisors have conducted extensive and expensive investigation, after they have concluded that the case should be prosecuted, but before respondents have understood the nature of the concerns. These decisions are rarely reversed. In addition, sending a NORA is discretionary with CFPB staff. In some recent cases, CFPB staff has not only declined to provide NORAs, but never even notified the companies of their interest in the matter before serving them with Notices of Charges that it had filed in its administrative tribunal and issuing a press release. By doing so, the staff deprived the companies of the opportunity to provide information that might have caused the staff to reconsider its decision to file the cases in the first instance and the opportunity to avoid the costs of unnecessary demands, as well as the opportunity to settle the charges pre-filing and pre-press release.⁹²

Order Provisions: One manifestation of the burden of contesting FTC investigations is in the consent orders that the FTC imposes on alleged violators. Resource-constrained companies and individuals without a realistic recourse to litigation may have to accept orders that impose burdens unnecessary to achieve legitimate remedial purposes. The burdens can be unduly harsh, raising competitors' costs and even threatening companies' existence. Moreover, they can acquire the mantle of precedent over time, making it very difficult for a company to argue for treatment different from that accorded to others. Accordingly, the Section recommends that the FTC consider:

- *Reducing the burden of standard "boilerplate" order provisions:* FTC orders contain a number of administrative provisions that are, more or less, the same in every order. For example, since 1996—the past 20 years—the FTC has required companies signing administrative orders to agree to an order duration of 20 years (longer, if there are subsequent violations) and Federal court orders that last in perpetuity.⁹³ This can create a severe burden on the companies involved, given the breadth and vagueness of "fencing in" order provisions⁹⁴ as well as burdensome affirmative obligations.⁹⁵ Especially in areas where technology is rapidly evolving, order provisions that make sense when they are entered may no longer be appropriate in 10 years, let alone 20 years later, and may serve to chill innovative and useful corporate practices. Although FTC rules allow for a petition to modify an order based on "changed conditions of law or fact" or

⁹²An executive order issued by President Clinton in 1996 [Exec. Order No. 12,988, 61 Fed. Reg. 4729 (Feb. 5, 1996)] requires Federal agencies that conduct or otherwise participate in Federal civil litigation on behalf of the U.S. government, before filing cases in court or administratively, to make a reasonable effort to notify all parties about the nature of the dispute and to attempt to achieve a settlement. There are several, narrow exceptions to this requirement, including cases involving forfeiture or bankruptcy, when the assets or defendants themselves are subject to dissipation or flight, or when "exigent circumstances make providing the notice impracticable or such notice would otherwise defeat the purpose of the litigation," such as in cases seeking a temporary restraining order or preliminary injunction. *Id.*

⁹³See Press Release, Fed. Trade Comm'n, FTC Rule Incorporating Sunset Policy for Existing Administrative Orders in Consumer Protection and Antitrust Cases (Nov. 20, 1995), available at www.ftc.gov/news-events/press-releases/1995/11/ftc-rule-incorporating-sunset-policy-existing-administrative. The Commission justified keeping Federal court orders unlimited because "many of these orders are against defendants involved in hard-core fraud." *Id.* As explained in the text, the FTC now files most of its cases in Federal court, including non-fraud cases.

⁹⁴Most orders include "fencing-in" relief that extends beyond prohibiting the violations alleged in the complaint to reach purportedly related practices. For instance, the Commission typically will seek against a company that is alleged to have made unsubstantiated claims about the efficacy of a particular dietary supplement for treating or preventing a specific health condition an order that requires scientific substantiation for any claim about the health benefits, efficacy, or performance of any food, drug, or dietary supplement. *E.g.*, POM Wonderful v. FTC, 777 F.3d 478, 505 (D.C. Cir. 2015). The company under order is often left guessing, at the peril of civil penalties or a contempt citation for an order violation, at which implied claims the FTC will find in future advertising and what substantiation for those claims it will deem sufficient.

⁹⁵For example, data security orders typically require expensive biennial security audits. *E.g.*, In the Matter of Snapchat, Inc., Docket No. C-4501, 2014 WL 1993567, at *14 (F.T.C. May 8, 2014).

“that the public interest so requires,”⁹⁶ in practice the standard for an order modification is very high and the process is often protracted and costly. CFPB orders typically sunset after five years. The Section recommends that the FTC adopt a comparable sunset period for both administrative and district court orders, at least where there are no extenuating circumstances (such as fraud or recidivism) justifying a longer duration.

Similarly, FTC administrative and Federal court orders include provisions (the so-called “Scofflaw” provisions) that require the respondent/defendant to distribute the order to various individuals, keep records, report changes such as asset sales, mergers or bankruptcy, and file compliance reports.⁹⁷ Some of these provisions last for the duration of the order, while others sunset after various numbers of years ranging from three to twenty, depending on the case.⁹⁸ The Federal court boilerplate traditionally has imposed additional Scofflaw provisions beyond those in administrative orders that, for example, give the FTC the right to gather information in various ways. Some of these additional provisions are burdensome and intrusive. For example, one Federal court order’s Scofflaw provision permits the FTC to contact the defendant directly, and not through counsel, about order-related matters (although counsel may be present during FTC “interviews”). Provisions such as these were drafted originally to ensure sufficient oversight of defendants that were engaged in fraud. The FTC increasingly has filed cases, including routine non-fraud cases, in Federal court, however. But, rather than ameliorating the harsh Federal court Scofflaw provisions, the FTC has imported them into some administrative orders.⁹⁹ The Section recommends that the FTC reconsider this approach so that burdensome Scofflaw provisions are not imposed on respondents or defendants engaged in legitimate businesses.

- *Seeking monetary relief that corresponds more closely to the nature of the violations, the extent of consumer injury, and the culpability of the respondent/defendant:* The FTC has increasingly sought strong monetary relief—civil penalties, restitution, and/or disgorgement—in ordinary Section 5 cases. Historically, the FTC sought restitution or disgorgement mainly in cases of fraud or blatant deception with tangible consumer injury, and tied the amount sought to the injury or unjust enrichment that could be traced to the violations. It now appears, however, that the FTC demands monetary relief in virtually all cases, even where the violations were unintentional and marginal and the injury slight or nonexistent. Moreover, staff in consent negotiations commonly seek the maximum possible relief regardless of the facts of the case or any mitigating circumstances, and without consideration of litigation risk. For example, in recent civil penalty cases, staff have pursued the defendant’s gross revenues without consideration of the statutorily imposed civil penalty factors that take into account, among other things, the defendant’s degree of culpability and the nature and seriousness of the violations.¹⁰⁰

⁹⁶ FTC Rule of Practice § 2.51, 16 C.F.R. § 2.51 (2016).

⁹⁷ A recent addition to the CFPB’s boilerplate requires defendants, before transferring or selling any of their “operations” to a third party, to notify the purchaser of the existence of the CFPB order, and obtain the purchaser’s written agreement to comply with the order. *See, e.g., In the Matter of TMX Finance LLC*, File No. 2016–CFPB–0022 (Sept. 26, 2016). Although the term “operations” is undefined, this provision apparently is designed to avoid the long-standing rule that an asset purchaser is not a “successor or assign” under an order unless the sale was designed to evade the order or the purchaser simply continued the seller’s business unchanged. As a result of the CFPB’s new policy, companies under order, for the duration of that order, likely cannot sell assets even to bona fide purchasers for anything close to their real value, if at all. This is unfairly punitive, and the Section recommends that the CFPB eliminate this provision from its orders.

⁹⁸ It is not clear why these time periods vary from case to case and provision to provision, but in some instances it may depend on the relative knowledge and negotiating skill of the company’s counsel. Having a shorter overall sunset in all orders could remove the inconsistency by making it unnecessary to have separate sunsets for each provision.

⁹⁹ *See, e.g., In the Matter of Practice Fusion, Inc.*, Docket No. C–4591, 2016 WL 3345406 (F.T.C. Aug. 16, 2016), available at www.ftc.gov/system/files/documents/cases/160816practicefusiondo.pdf.

¹⁰⁰ For example, the press release issued by the FTC announcing a settlement with Consumer Education Group notes that the civil penalty (most of which was suspended due to inability to pay) “is equivalent to the revenue defendants obtained through their illegal acts.” *See* Press Release, Fed. Trade Comm’n, Sales Lead Generators Fined and Barred from Violating FTC’s Telemarketing Sales Rule (Nov. 1, 2016), available at <https://www.ftc.gov/news-events/press-releases/2016/11/sales-lead-generators-fined-barred-violating-ftcs-telemarketing>. The CFPB also has insisted on civil monetary penalties in every case. That agency, unlike the FTC, has unre-

Although the Section believes that the FTC has reason to raise the cost of violating the law in appropriate cases, the Section recommends that those efforts be tempered by considerations of equity and proportionality, as well as the constraints imposed by the statutes and case law. Monetary relief in non-fraud cases should not be punitive or threaten a company's ability to compete. In evaluating the deterrent effect of an order, the Commission should take into account the enormous damage an FTC action can cause a defendant, beyond any monetary judgment. In an age of instant and comprehensive information, whenever interested parties, such as licensing bodies, or prospective finance sources or vendors, search for information about individuals or companies, those named in FTC cases can be indefinitely branded as wrongdoers, even when the alleged violations were never proven in court or may have been inadvertent or minor. Seeing the agency's increased focus on extending liability to third parties for assisting violators, finance sources, vendors, and others may be very reluctant to provide the money or services to those facing FTC actions or under an order.

Meeting Decision Makers: The FTC has well-established "due process" norms that give targets facing possible enforcement the opportunity to meet with division and Bureau managers before a complaint recommendation is forwarded to the Commission, and then with Commissioners before the complaint is issued or filed.¹⁰¹ This process generally works well, but could be improved by encouraging transparency earlier in the investigation.

The CFPB, on the other hand, does not appear to have any comparable process. With some exceptions, the Assistant Director of Enforcement and his superiors have been unwilling to meet with many companies they are deciding to prosecute. This can have serious disadvantages: companies cannot know that their concerns have been heard (which in some cases may make them less willing to settle), and the decision makers are denied information that would better inform their decisions. The Section recommends that the CFPB adopt standard internal appeal procedures like those of the FTC.

While the FCC has procedural due process measures that resemble those of the FTC, there are some important differences in the authority delegated to staff. In particular, the Enforcement Bureau has delegated authority to propose forfeitures only up to a maximum amount of \$100,000.¹⁰² The FCC must vote to approve any forfeiture above \$100,000. However, the Enforcement Bureau has delegated authority to resolve investigations via consent agreements involving any amount of money, even in matters that involved an earlier, FCC-voted proposed forfeiture. Thus, the Bureau has significant authority to undertake enforcement actions and shape enforcement policy on its own, without Commission involvement. The Section recommends that the FCC consider reducing the delegated authority of the Enforcement Bureau and requiring Commission votes on any consent agreements involving payments that exceed the Bureau's delegated authority for proposed forfeitures.

4. Guidance

In addition to law enforcement and rulemaking, one of the principal ways the FTC and other agencies that enforce Federal consumer protection laws encourage compliance is by providing guidance on their legal interpretations and expectations as applied to specific industries or practices. The FTC has broad (but not unlimited) discretion in choosing strategies for fostering compliance, including bringing individual enforcement actions even when the violative practices are common throughout an industry.¹⁰³ In many situations, however, guidance may be more effective and efficient than enforcement in fostering compliance. It also may be fairer to the individual defendants, who can suffer catastrophic damage from being the subject of government law enforcement simply because they happened to be selected among many other possible targets. This is especially true when the law is unclear and the practices at issue are long-standing or widespread.

Although enforcement actions are a good means of providing guidance, their usefulness for this purpose is often limited by the information they reveal. Businesses carefully scrutinize complaints and orders to glean insights into the agencies' think-

stricted civil penalty authority in cases alleging unfair or deceptive acts or practices. 15 U.S.C. §5565(c).

¹⁰¹ An exception is for fraud cases in which the Commission may seek ex parte relief.

¹⁰² 47 C.F.R. §0.311.

¹⁰³ *E.g.*, *FTC v. Universal-Rundle Corp.*, 387 U.S. 244, 251 (1967); *but see Johnson Products Co. v. FTC*, 549 F.2d 35, 41 (7th Cir. 1977) (FTC may not issue orders that "would arbitrarily destroy one of many violators in the market," *citing* *L.G. Balfour Co. v. FTC*, 442 F.2d 1, 24 (7th Cir. 1971)).

ing.¹⁰⁴ In some cases, however, the pleadings are not sufficiently clear or detailed in identifying the alleged illegal conduct to serve this purpose, and businesses are left to “read the tea leaves” as to how the agencies might view their particular practices.

The agencies have issued useful guidance in many areas and in many forms, including enforcement policy statements, advisory opinions, informal staff opinion letters, warning letters, studies, reports, bulletins, speeches, testimony, and business education materials.¹⁰⁵ Topics run the gamut from advertising testimonials and endorsements, to “native advertising,” to motor vehicle financing under the Equal Credit Opportunity Act. The Section recommends that the agencies provide further guidance on four substantive issues:

a. The Meaning of “Abusive”

The CFPB’s abusiveness authority¹⁰⁶ has been applied in an inconsistent manner, and it is often difficult to discern why the CFPB has challenged a particular practice as abusive, as opposed to (or in addition to) unfair or deceptive. The agency has resisted providing additional guidance on this term beyond the statutory definition. The Section encourages the CFPB to provide a policy statement on abusive acts or practices, similar to those issued by the FTC on unfairness¹⁰⁷ and deception¹⁰⁸ in the 1980s, which have proven extremely useful.

b. Monetary Remedies

The FTC in many cases has not clearly articulated its rationale for the type or amount of monetary relief it demands, and in some cases where the rationale was evident, the legal theory behind it was questionable. For example, as noted earlier, FTC staff have demanded civil penalties in rule violation cases based on the defendant’s gross revenues, a disgorgement measure, rather than the statutorily-imposed civil penalty factors. In the interests of greater transparency, the Section recommends that the FTC issue a policy statement setting forth the theories on which it relies to justify its demands for monetary relief.

The CFPB has taken an even more aggressive approach in seeking fines under Dodd-Frank and other statutory authorities. Understanding the ways in which the CFPB is analyzing the purported harm would be useful for companies to integrate compliance in their operations, and gauge the potential risks.

c. Advertising Interpretation and Disclosures

The agencies have pursued failure to disclose theories and imposed “clear and conspicuous” disclosure requirements with increasing vigor in recent years. This has created considerable uncertainty for businesses in determining what information is sufficiently important (*e.g.*, material and necessary to prevent unfairness or deception) that it must be disclosed and where the disclosures must appear (*e.g.*, in advertising or at point of sale). The different opinions on claim interpretation and disclosure clarity at the Commission in *POM Wonderful* were not reconciled in the decision of the D.C. Circuit, leaving additional uncertainty as to whether and what kind of substantiation is needed for a claim, what claims trigger a disclosure, and how much information should be disclosed.

Especially in the case of short-form broadcast advertising, there simply is not sufficient space to include all of the information the agencies have deemed necessary in forms of advertising. The need for qualifying information is especially important

¹⁰⁴The FTC and CFPB have taken somewhat different positions on whether an order establishes standards for lawful versus unlawful conduct that apply beyond the individual case at issue. The FTC stresses that its orders often contain fencing-in relief that may go beyond what the law requires and may not be required of other companies. See Letter from Joel Winston, Fed. Trade Comm’n to Jonathan L. Kempner, Mortgage Bankers Assoc. (June 17, 2004), available at www.ftc.gov/system/files/documents/advisory_opinions/letter-mortgage-bankers-association-regarding-ftc-settlement/fairbanks/040617staffopltrtomba.pdf. CFPB Director Richard Cordray, on the other hand, recently asserted that it would be “‘compliance malpractice’ for executives not to take careful bearings from the contents of these orders about how to comply with the law and treat consumers fairly.” See Richard Cordray, Speech at the Consumer Bankers Assoc. (Mar. 9, 2016), available at www.consumerfinance.gov/about-us/newsroom/prepared-remarks-of-cfpb-director-richard-cordray-at-the-consumer-bankers-association/.

¹⁰⁵Note, however, that the Dodd-Frank Act transferred the FTC’s authority to “prescribe rules [or] issue guidelines” to the CFPB in areas of overlapping jurisdiction. 12 U.S.C. § 5581(b)(5). The FTC generally has interpreted this transfer to apply only to formal types of guidance (such as agency-issued industry guides), rather than, for example, staff opinion letters or other less formal guidance.

¹⁰⁶Section 1031 of the Dodd-Frank Act prohibits unfair, deceptive, or abusive acts or practices. 12 U.S.C. § 5531.

¹⁰⁷See FTC Policy Statement on Unfairness, *supra* note 74.

¹⁰⁸See FTC Policy Statement on Deception, *supra* note 73.

to establish when the cost of the qualification is the loss of other information or the loss of the advertisement itself. In any medium, increasing the amount of information that must be disclosed can obscure the most important messages, thus creating a tension with the “clear and conspicuous” objectives of the disclosure.

Moreover, there is uncertainty on how the “clear and conspicuous” standard will be applied in particular fact situations. While some uncertainty is inevitable given the fact-specific nature of deception, the Section recommends that the agencies look for additional opportunities to clarify their expectations in specific areas through guidance and give businesses an opportunity to come into compliance before the agencies start bringing enforcement actions.¹⁰⁹ The Section encourages the Commission to explore each element of disclosure policy—from the representation that would trigger a disclosure to the clarity and prominence of the disclosure—and how the factors vary across media.

IV. LEGAL DOCTRINE

A. Monopoly

The Section does not support the aggressive view, espoused recently by certain politicians and administration economists, that competition has declined in the United States as a result of the increasing concentration in key industries, which itself is attributed to the reluctance of the Agencies to challenge and the failure of courts to block more mergers.¹¹⁰ Evidence offered in support of the criticism has been vague and anecdotal at best, but the evidence available to analysts outside the Agencies does not permit the kind of analysis that the Agencies themselves can conduct with the information obtained in the course of law enforcement. The Agencies are in a unique position to add empirical evidence to the debate. The Section applauds the Agency officials who have addressed the criticism. We believe a more systematic response would contribute a great deal to public confidence in antitrust enforcement. For example, as we noted above, the Agencies should address this question in their merger retrospective studies. Likewise, the Section recommends that the Agencies use their authority to identify and assess conduct that may generate adverse economic consequences in the United States. Such an assessment should precede any conclusion¹¹¹ that a marked reorientation of enforcement emphasis or new legal rules are needed.

It has always been an important responsibility of the Agencies to preserve competition and to ensure that anticompetitive exclusion is deterred in order to preclude firms from achieving dominant market positions by anticompetitive means. Both actual collusion and exclusion are harmful to consumers. Thus, the Agencies should

¹⁰⁹ For example, the FTC has brought twenty-five or so cases in the past few years against auto dealers alleging the failure to adequately disclose in advertising certain material conditions, qualifications, and restrictions on the advertised offer. *See generally* Letter from Malini Mithal, Acting Assoc. Dir., Div. of Fin. Practices, FTC to Paul Sanford, Ass’t Dir., Supervision Examinations, CFPB (May 27, 2016), available at https://www.ftc.gov/system/files/documents/reports/ftc-enforcement-activities-related-compliance-regulation-z-truth-lending-act-regulation-m-consumer/160606cfpbrpttila.pdf?utm_source=govdelivery (summarizing recent FTC enforcement actions against auto dealers). In most cases, the disclosures appeared in the fine print at the bottom of a print ad or on the last screen of a television ad, consistent with how auto manufacturers and dealers have been advertising for decades. Without questioning the merits of these cases, given the uncertainty about the agency’s disclosure standards and the severe impact on the dealers that were unlucky enough to have been singled out, this may have been a situation where clearer guidance could have been issued before beginning enforcement.

¹¹⁰ Marc Jarsulic, Ethan Gurwitz, Kate Bah, and Andy Green, Center for American Progress, *REVIVING ANTITRUST: WHY OUR ECONOMY NEEDS A PROGRESSIVE COMPETITION POLICY* (June 2016); S. Elizabeth Warren, *Reigniting Competition in the American Economy*, Keynote Remarks at New America’s Open Markets Program Event (June 29, 2016), available at www.warren.senate.gov/files/documents/2016-6-29_Warren_Antitrust_Speech.pdf.

¹¹¹ Comm’r Terrell McSweeney, U.S. Fed. Trade Comm’n, *Making Antitrust Work for the 21st Century*, Keynote Remarks at Washington Center for Equitable Growth (Oct. 6, 2016), available at https://www.ftc.gov/system/files/documents/public_statements/988713/mcsweeney_-_keynote_remarks_at_equitable_growth_10-6-16.pdf; Renata Hesse, Acting Ass’t Att’y Gen., U.S. Dep’t of Justice, Antitrust Div., *And Never the Twain Shall Meet?: Connecting Popular and Professional Visions for Antitrust Enforcement*, Opening Remarks at the 2016 Global Antitrust Enforcement Symposium (Sept. 20, 2016), available at www.justice.gov/opa/speech/acting-assistant-attorney-general-renata-hesse-antitrust-division-delivers-opening; Edith Ramirez, Chairwoman, U.S. Fed. Trade Comm’n, *Keynote Remarks at the 2016 Global Antitrust Enforcement Symposium* (Sept. 20, 2016), available at <https://www.ftc.gov/public-statements/2016/09/keynote-remarks-ftc-chairwoman-edith-ramirez>; Comm’r Maureen K. Ohlhausen, U.S. Fed. Trade Comm’n, *Does the U.S. Economy Lack Competition, And If So What To Do About It?*, Remarks at Hogan Lovells, Hong Kong (June 1, 2016), available at https://www.ftc.gov/system/files/documents/public_statements/952273/160601doesuseconomylackcomp.pdf.

identify and attack conduct that achieves, enhances, or maintains market power by disadvantaging competitors other than by means of efficiency-based competition.

Vigorous enforcement of the competition laws must be balanced with the need to encourage truly competitive conduct that benefits consumers and achieves cognizable efficiencies. With this in mind, the Section respectfully suggests that there are three particularly salient matters that deserve close attention and are ripe for close enforcement attention, competition advocacy, and Agency guidance in coming years: (1) two-sided markets, (2) contracts referencing rivals (CRRs), and (3) tying and bundling.

1. Two-Sided Markets

Two-sided or multi-sided markets are increasingly important in the economy, and raise complicated and unique antitrust issues.¹¹² To date, these complex issues have not received sufficient attention. The Section therefore recommends that the Agencies take steps to provide greater guidance and clarity, including by issuing statements of enforcement policy and through bringing enforcement actions.

A two-sided market is one in which one firm (often called a platform) receives revenues from separate groups that are dependent on each other in some way. For example, a newspaper charges readers for subscriptions and also charges advertisers for advertisements. The newspaper may charge more for advertisements if it has more subscribers, and so the two sides are dependent on each other. As this example demonstrates, there is a close relationship between two-sided markets and markets involving complementary goods. The Section recommends that the Agencies clarify whether two-sided markets require special antitrust analysis or are a general case of complementary products.

Industries characterized by two-sided or multi-sided markets cannot be fully understood without a clear understanding of the interaction between the multiple sides. This impacts multiple parts of the antitrust analysis, including:

- *Analysis of constraints on the exercise of market power.* While a firm may be able to exercise market power on one side of a two-sided market even if the second side is competitive, the competitive nature of the second side may also constrain the first. For example, the publisher of the only local newspaper in a community might be reluctant or unable profitably to exercise market power over readers (*e.g.*, by charging high prices or reducing the quality of distribution) if doing so will reduce readership and thus the amount the publisher can charge advertisers that are able to choose between the newspaper and other forms of local advertising such as radio. Because the price increases could cause both lost sales to readers and lost revenues from advertisers, the two-sided nature of the market could preclude or limit the exercise of market power on either side.
- *Analysis of competitive effects.* Conversely, conduct that might appear anti-competitive if one focuses entirely on one side of the market might seem benign or procompetitive when both sides of the market are taken into account. For example, a newspaper might charge a price below marginal cost in order to generate increased readership and thus more advertising revenue. The price might appear predatory if the antitrust analysis focuses solely on the reader market. However, if the other side of the market is taken into account, the conduct might appear to be an efficient means of defraying fixed costs.¹¹³

The recent decision in *United States v. American Express*¹¹⁴ illustrates both the increasing importance of two-sided markets and the need for clarification of the applicable legal standards and appropriate modes of legal and economic analysis. The court appears to take the position that, in a vertical restriction case involving a two-sided market, the lawfulness of the allegedly anticompetitive conduct depends on the effect of the conduct on the defendant's customers on both sides of the market.¹¹⁵ The Section recommends that the Agencies encourage courts to examine the effect of the conduct on both sides of the market *as a whole* instead of the effects just on the defendant's customers.

¹¹²See David S. Evans, *Attention Rivalry Among Online Platforms*, 9 J. COMPETITION L. & ECON. 313 (2013).

¹¹³Similar issues can arise with non-price conduct. See, *e.g.*, *Lorain Journal Co. v. United States*, 342 U.S. 143 (1951); *United States v. Microsoft Corp.*, 253 F.3d 34 (D.C. Cir. 2001); *United States v. Visa U.S.A., Inc.*, 344 F.3d 229 (2d Cir. 2003).

¹¹⁴838 F.3d 179 (2d Cir. 2016).

¹¹⁵838 F.3d at 206.

2. *Contracts Referencing Rivals (CRRs)*

CRRs contain terms that refer to or depend on information about rivals, *e.g.*, their sales, prices or offers. They include provisions such as: (1) “most favored nation” provisions (MFNs), in which one party promises to trade with the other on terms as good as, or sometimes better than, the terms on which it trades with other trading partners; (2) loyalty or “market share” discounts, in which the price paid by the buyer depends in part on the percentage of its purchases from the seller; (3) exclusive dealing and exclusive distributorship agreements, which require one party to deal exclusively with the other for certain products or services; and (4) rights of first refusal, by which one party promises that the other will have a chance to meet or beat any offer the promisor receives from another party.

CRRs are ubiquitous and can have procompetitive or anticompetitive effects depending on the context.¹¹⁶ They often promote increased output and other efficiencies, such as risk-sharing or aligning incentives in the distribution chain. For example, an MFN can facilitate efficiency-enhancing transactions where one party is concerned that, because of changing circumstances or its lack of information about the market, it might wind up being disadvantaged compared to rivals. A right of first refusal can provide similar benefits. A loyalty discount can align incentives between suppliers and distributors in times of unforeseen demand shifts, when quantity discounts would not provide suitable incentives if demand increases or decreases materially, and can shift some of the risk of falling demand from the distributor to the supplier.

CRRs may also have anticompetitive effects. MFNs can deter price cuts and raise entry barriers in effect imposing a tax on lower prices offered to other or new trading partners. Loyalty discounts can deter purchasers from dealing with rival suppliers if doing so would push the percentage purchased from the firm offering the loyalty discount below certain thresholds and they can exclude rivals that are able to serve only a small part of the buyer’s needs. Exclusive dealing and, less commonly, exclusive distributorship agreements can exclude rivals by restricting their access to customers and input suppliers. And right of first refusal provisions can diminish competition by deterring rival sellers from trying to sell to the potential customer who is subject to that form of contractual restriction.

The Agencies have been instrumental in conceptualizing the competitive impact of CRRs and bringing them to the forefront of antitrust dialogue.¹¹⁷ But, while economic analysis of CRRs has advanced, the appropriate legal analysis remains unclear, in part because of problems administering standards implied by some economic analyses. For example, the kind of discount attribution test favored by some economists for loyalty discounts raises difficult factual issues with which courts have had little experience.¹¹⁸ Judicial decisions, particularly those regarding loyalty discounts, have been inconsistent.¹¹⁹

The Section recommends that the Agencies look for opportunities to advance the evolution of legal doctrine applicable to CRRs through enforcement actions, amicus briefs, and perhaps agency guidelines. Greater clarity about the legal rules would benefit businesses in assessing the risk associated with a particular provision, as well as reduce judicial errors and litigation costs.

The recent case involving Apple’s e-book pricing model highlights the need for further guidance relating to CRRs.¹²⁰ In the Apple e-books matter, the Division alleged that Apple facilitated an illegal horizontal price-fixing agreement among the publishers of e-books. Further guidance is needed to clarify how similar CRRs would be analyzed in a vertical context (absent evidence of horizontal collusion).

3. *Tying and Bundling*

A tying arrangement is an agreement by a party to sell one product on the condition that the buyer also purchase a separate product. Tying can be challenged as

¹¹⁶See Joshua D. Wright, Comm’r, Fed. Trade Comm’n, Simple but Wrong or Complex but More Accurate? The Case for an Exclusive Dealing-Based Approach to Evaluating Loyalty Discounts (June 3, 2013), available at www.ftc.gov/sites/default/files/documents/public_state_documents/simple-wrong-or-complex-more-accurate-case-exclusive-dealing-based-approach-evaluating-loyalty/130603bateswhite.pdf.

¹¹⁷See, *e.g.*, Fiona Scott-Morton, Deputy Asst. Att’y Gen., U.S. Dep’t of Justice, Antitrust Div., Contracts that Reference Rivals, Address at the Georgetown University Law Center: Antitrust Seminar (April 5, 2012), available at <https://www.justice.gov/atr/file/518971/download>.

¹¹⁸Benjamin Klein & Andres Lerner, *The Economics of Alternative Antitrust Standards for Loyalty Contracts*, ANTITRUST L.J. (forthcoming 2016).

¹¹⁹*Compare Allied Orthopedic Appliance v. Tyco Health Care Group LP*, 592 F.3d 991 (9th Cir. 2009), with *Virgin Atl. Airways v. British Airways*, 257 F.3d 256 (2d Cir. 2001).

¹²⁰*United States v. Apple, Inc.*, 791 F.3d 290 (2d Cir. 2015).

an act of exclusion under Section 2 of the Sherman Act, as well as under Section 1 of the Sherman Act and Section 3 of the Clayton Act.

Early decisions held tying arrangements to be per se illegal.¹²¹ More recent decisions suggest that judicial disapproval of tying arrangements is dissipating.¹²² The Supreme Court in *Illinois Tool Works v. Independent Ink Inc.* clearly indicated that tying arrangements are not always or almost always anticompetitive.¹²³ In addition, in *United States v. Microsoft*,¹²⁴ the D.C. Circuit declined to apply the per se rule to the tying of an operating system and a web browser, reasoning that platform software tying arrangements may have procompetitive efficiencies.

Other courts and commentators have observed that tying frequently has procompetitive effects, including: (1) enhanced ability to assure product quality; (2) achieving economies through joint production, distribution, or marketing; (3) undermining collusion by enabling secret price-cutting; (4) precluding excessive markups by sellers of complementary products; and (5) avoiding double marginalization.¹²⁵

Although less numerous, some commentators and decisions have continued to find potential anticompetitive effects in tying arrangements, including: (1) raising prices to consumers; (2) limiting consumer choices; and (3) excluding or impairing rivals by raising their costs, thereby triggering higher prices and facilitating anticompetitive price discrimination.¹²⁶

Bundling, like tying, is a practice that, in different market contexts, can be either procompetitive or anticompetitive. Bundled discounts are awarded to customers who make a designated number of purchases across multiple product lines. Bundled discounts offered by large firms with numerous product lines may impair competition in circumstances where the bundled discount cannot be matched by smaller firms lacking broad product lines, regardless of whether the smaller firm is the more efficient producer of a particular product.¹²⁷ On the other hand, bundling can result in a real discount, reducing market prices and increasing competition, and can help generate economies of scope and scale.

The Third and Ninth Circuits disagree on the proper antitrust test for bundled discounts. The Ninth Circuit applies predatory pricing standards (though without the recoupment feature).¹²⁸ The Third Circuit rejects predatory pricing tests and condemns bundled discounts that “foreclose the opportunities of rivals” in an “unnecessarily restrictive way.”¹²⁹ When different rules apply to conduct depending on where it occurs, the potential for erroneous enforcement is unacceptably high. The Section suggests that bundling is another area ripe for an Agency enforcement policy statement to identify and distinguish the circumstances where the practice produces procompetitive or anticompetitive effects.

In light of the countervailing considerations that tying and bundling cases present, this is an area in which the Agencies should proceed carefully, concentrating on practices they believe to be truly anticompetitive, while considering the efficiency justification both as a matter of prosecutorial discretion and as presented in court. Such prudential enforcement activity would be very helpful in drawing the line between what is procompetitive and what is not.

¹²¹ *E.g.*, *Int'l Salt Co. v. United States*, 332 U.S. 392 (1947).

¹²² *Illinois Tool Works v. Independent Ink Inc.*, 547 U.S. 28 (2006).

¹²³ *Id.* at 45 (“Many tying arrangements . . . are fully consistent with a free, competitive market.”).

¹²⁴ 253 F.3d 34 (D.C. Cir. 2001).

¹²⁵ *See, e.g.*, *Brantley v. NBC Universal, Inc.*, 675 F.3d 1192, 1200 (9th Cir. 2012) (“Like other vertical restraints, tying arrangements may promote rather than injure competition.”); David Evans & Michael Salinger, *Why Do Firms Bundle and Tie? Evidence from Competitive Markets and Implications for Tying Law*, 22 *YALE J. ON REG.* 37 (2005).

¹²⁶ *See, e.g.*, *Collins Inkjet Corp. v. Eastman Kodak Co.*, 781 F.3d 264, 271–72 (6th Cir. 2015) (a tying arrangement may be anticompetitive if it “tends to force more efficient competitors out of the tied product market”); Steven C. Salop, *The Raising Rivals’ Cost Foreclosure Paradigm, Conditional Pricing Practices and the Flawed Incremental Price-Cost Test*, 81 *ANTITRUST L.J.* ___, 31–32 (forthcoming 2017), available at <http://scholarship.law.georgetown.edu/cgi/viewcontent.cgi?article=2632&context=facpub>.

¹²⁷ *See* Daniel A. Crane & Graciela Miralles, *Toward a Unified Theory of Exclusionary Vertical Restraints*, 84 *S. CAL. L. REV.* 605, 646 (2011) (“[A] contract or contractual provision should be deemed to foreclose some share of the market only when it prevents an equally efficient competitor from profitably offering its own set of contractual terms that the customer reasonably might chose in lieu of the defendant’s terms for some increment of the market’s output.”); Elyse Dorsey & Jonathan M. Jacobson, *Exclusionary Conduct in Antitrust*, 89 *ST. JOHN’S L. REV.* 101, 134–36 (2015).

¹²⁸ *Cascade Health Sol’ns v. PeaceHealth*, 515 F.3d 883 (9th Cir. 2008).

¹²⁹ *LePage’s Inc. v. 3M*, 324 F.3d 141 (3d Cir. 2003).

B. Antitrust and Intellectual Property

1. Patent-Related Antitrust Issues

The Section recommends that the Agencies study patent-related antitrust issues, in particular those related to phenomena sometimes called “holdup” and “holdout.” It is generally accepted that the ownership of a patent by itself is not presumed to create a presumption of market power, and that the proper assertion of a valid patent is not an antitrust violation. By the same token, improper assertions of patent rights, like those involving other assets, can raise questions of competitive significance. “Patent holdup” occurs, for example, when an SEP holder that has made a commitment to license its patents on FRAND terms instead uses the essential nature of its patent (“standard-lock-in”) to charge an unjustifiably higher royalty than would have been possible before its patent was included in the standard.¹³⁰ Supracompetitive compensation can lead to deadweight loss from revenue raising, deter commercialization of patented technologies, reduce follow-on invention, exacerbate strategic uses of patents to raise rivals’ costs, and induce costly overinvestment in patents to be used for those purposes or defensively. Subcompetitive compensation can reduce returns to investment in patentable inventions, and the prospect thereof could reduce such investment in innovation, or standard-setting, or both.

Holdout refers to the situations in which an implementer either delays or refuses to take a license or engages in bad-faith challenges to patent validity or in which a patent holder delays, or refuses to offer, or engages in bad-faith negotiation regarding, a license to the entire portfolio of patents, or any subset thereof, held by the patent holder or any commonly controlled entity for which the implementer seeks a license or conceals or fails to disclose the entire portfolio of patents held by the patent holder or any commonly controlled entity.¹³¹ Both holdup and holdout can arise with respect to technologies included in, or necessary as a practical matter to implement, public standards and patented technologies that are not included in standards.

The holdup issue raises a number of questions. One is whether patent holders that assert SEP patents are able to obtain supracompetitive royalties from users in an individual case or whether implementers of patented technologies can force patent holders to accept less than competitive royalties.¹³² Another, very different question is whether the costs incurred by technology users for using patented standards technology have in the aggregate been excessive, *e.g.*, would harm the product market or restrict output. Empirical studies on the subject require data, most of which is available only in aggregated form, which has obvious limitations. A finding that aggregate costs to technology users are not excessive could mean that patent holdup has not in the aggregate deterred the use of patented standards technologies or follow-on inventions, but such a finding would not itself demonstrate the absence of adverse effects from holdup. Aggregated data would not disclose problematic holdup if, for example, (1) relatively few patents were asserted in the period studied and the percentage of patents being asserted increases over time or (2) excessive royalties when patents are asserted have distorted the use of, or follow-on invention based on, the asserted patents or created perverse incentives for over-patenting. Careful analysis of the context is important, because neither holdup nor excessive pricing, without more, violates the antitrust laws.

There is no consensus about the factual significance and likelihood of the phenomena known as holdup and holdout, and the disagreements about these factual issues have important ramifications for patent policy and antitrust policy regarding patents. The Section concurs in the statements of ranking enforcement officials that high or low returns standing alone do not form the basis for a finding of an antitrust violation in the absence of evidence of unlawful exclusionary conduct.¹³³ It is

¹³⁰Douglas H. Ginsburg *et al.*, *The Troubling Use of Antitrust to Regulate FRAND Licensing*, 10 COMPETITION POL’Y INT’L ANTITRUST CHRON. 1 (2015); *see also*, J. Gregory Sidak, *The Antitrust Division’s Devaluation of Standard-Essential Patents*, 104 GEO. L.J. ONLINE 48, 61 & n.49 (2015).

¹³¹Sidak, *supra* note 131 at 61 & n.49; ANNE LAYNE-FARRAR, PATENT HOLDUP AND ROYALTY STACKING THEORY AND EVIDENCE: WHERE DO WE STAND AFTER 15 YEARS OF HISTORY? (2014), available at <http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=DAF/COMP/WD%282014%2984&doclanguage=en>.

¹³²*See, e.g.*, William F. Lee & A. Douglas Melamed, *Breaking the Vicious Cycle of Patent Damages*, 101 CORNELL L. REV. 384 (2016).

¹³³*See, e.g.*, Bill Baer, Ass’t Att’y Gen., U.S. Dep’t of Justice, Reflections on the Role of Competition Agencies When Patents Become Essential, Remarks at the 19th Annual Int’l Bar Association Competition Conference (Sept. 11, 2015); Edith Ramirez, Chairwoman, U.S. Fed. Trade

the exclusionary conduct that raises the unresolved questions. We therefore recommend that the Agencies gather reliable and credible information on—and propose a framework for evaluating—holdup and holdout, and the circumstances in which either may be anticompetitive. The Agencies are particularly well-suited to gather evidence and assess competitive implications of such practices, which could then inform policymaking, advocacy, and potential cases. The Agencies’ perspectives could contribute valuable insights to the larger antitrust community.

2. International Issues Related to Intellectual Property

In addition to patent issues, international topics are significant, most notably in the context of the multinational implications of agency actions and the effect of decisions by agencies such as the International Trade Commission (ITC).

a. Multinational Effects

Worldwide portfolio licensing remedies pose significant comity concerns, especially when such remedies are not consistent with other jurisdictions’ policies.¹³⁴ The United States, for example, does not regulate price; instead, because of a concern about innovation incentives, the United States protects the right of IP holders to set the prices of their products.¹³⁵ In contrast, several foreign countries have “excessive pricing” prohibitions and some foreign competition authorities have applied them to IP rights.

While the FTC and some foreign agencies have threatened to impose extra-jurisdictional remedies in some instances, other foreign jurisdictions have appropriately refrained from imposing remedies with extraterritorial effects. For example, the antitrust agencies in Europe and China typically have limited their remedies to domestic conduct pertaining to domestic patents. In April 2014, for example, the European Commission’s Directorate-General for Competition (DG Competition) entered into a settlement with Samsung¹³⁶ and issued a decision against Motorola Mobility¹³⁷ essentially prohibiting both companies from seeking injunctive relief against willing licensees of standard essential patents except under certain limited circumstances. DG Competition specifically limited its remedy to conduct occurring in the European Economic Area (EEA), and only to patents granted in the EEA. Likewise, in a 2015 penalty decision against Qualcomm for allegedly abusing a dominant position by charging unreasonably high royalties, bundling SEP and non-SEP licenses without justification, and imposing other unreasonable conditions on the sale of baseband chips (such as requiring a waiver of the licensee’s right to challenge the agreement), China’s National Development and Reform Commission (NDRC) limited remedies to conduct related to Chinese patents being licensed for use in China only.¹³⁸ In contrast, in the *Rambus* matter,¹³⁹ the FTC’s cease and desist order applied to the company’s enforcement of its patents everywhere in the world. In light of the significant comity concerns presented by extraterritorial remedies in-

Comm’n, Standard-Essential Patents and Licensing: An Antitrust Enforcement Perspective, 8th Annual Global Antitrust Enforcement Symposium (Sept. 10, 2014).

¹³⁴ See, e.g., Christine A. Varney, Ass’t Att’y Gen., Antitrust Div. U.S. Dep’t of Justice, Coordinated Remedies: Convergence, Cooperation, and the Role of Transparency, Remarks as Prepared for the Institute of Competition Law New Frontiers of Antitrust Conference (Feb. 15, 2010) (encouraging antitrust agencies to “endeavor to make our remedial decisions with our eyes open to their consequences beyond our shores, taking steps to minimize their extraterritorial effects; let us keep our eyes open to what our sister agencies have already done in particular cases, so that we do not unnecessarily diverge from their decisions”).

¹³⁵ See *supra* note 134.

¹³⁶ Press Release, European Comm’n, Antitrust: Commission Accepts Legally Binding Commitments by Samsung Electronics on Standard Essential Patent Injunctions (April 29, 2014) (IP/14/1490).

¹³⁷ Case AT.39985-Motorola-Enforcement of GPRS standard essential patents, Comm’n Decision, 2014 O.J. (C 344) 06.

¹³⁸ NDRC Administrative Sanction Decision No. 1 [2015] (Mar. 2, 2015), available at http://www.ndrc.gov.cn/gzdt/201503/t20150302_666209.html. Specifically, the NDRC approved the “rectification plan” submitted by Qualcomm, under which the company agreed: (1) not to bundle Chinese SEPs and non-SEPs and to provide patent lists during negotiations; (2) to charge royalties of not more than 5 percent for Chinese 3G SEPs and 3.5 percent for Chinese 4G SEPs using a royalty base of 65 percent of the net selling price of the device; (3) not to condition the sale of baseband chips on signing a licensing agreement with terms that NDRC found to be unreasonable (e.g., a no-challenge clause); and (4) to provide existing licensees with an opportunity to elect to take the new terms for sales of branded devices for use in China.

¹³⁹ Final Order in the Matter of Rambus Incorporated, File No. 011–0017, Dkt. No. 9302 (F.T.C. 2007), available at <https://www.ftc.gov/sites/default/files/documents/cases/2007/02/070205finalorder.pdf>. The cease and desist order was ultimately overturned by the United States Court of Appeals for the District of Columbia Circuit on other grounds. *Rambus v. FTC*, 522 F.3d 456 (D.C. Cir. 2008), *cert. denied*, 129 S. Ct. 1318 (2009).

volving patents, the Section recommends that the Agencies refrain from seeking such remedies.

Some foreign competition authorities have also considered imposing broad requirements that IP holders share their IP with others, including competitors. The United States strongly disfavors such requirements, while some Asian competition agencies have argued in favor of sanctioning refusals to license and making licensing compulsory.¹⁴⁰ The Agencies also recognize that practices such as tying and bundling, discriminatory licensing, cross-licensing, and grantbacks can be procompetitive, and thus call for an effects-based analysis. In contrast, some Asian competition agencies appear to apply presumptions that such licensing conduct is anticompetitive. To protect the ability of U.S. businesses to innovate and compete, the Agencies may wish to consider whether the concerns warrant an adjustment in U.S. policy or an international dialogue that might reconcile these conflicting policies.

b. International Trade Commission

In addition to multinational implications, issues arise from the differences between the standards that Federal courts apply for injunctions and the United States International Trade Commission's (ITC) applies for exclusionary remedies. The U.S. Supreme Court's decision in *eBay Inc. v. MercExchange*,¹⁴¹ held that a district court must apply the same standards required in all other injunction cases. After *eBay*, a district court must consider and weigh whether: the plaintiff will suffer irreparable harm; money damages are inadequate to compensate the plaintiff; the balance of hardships weigh in the plaintiff's favor; and the public interest would not be disserved by the issuance of an injunction. Because the only relief available before the ITC is injunctive in nature, complainants' primary remedy is an exclusion order excluding the importation of infringing goods,¹⁴² rather than money damages which are not available there. With its own statutory scheme that lays out a test for exclusion orders, the ITC does not follow the *eBay* test. For that reason, it is possible that patent holders who appear before the ITC could obtain exclusion orders when they would not be entitled to injunctions, or vice versa.¹⁴³ This divergence in standards could result in different outcomes for similar conduct depending on the tribunal addressing that conduct, and thus could have a significant impact on litigants' choice of tribunals.

The possibility that SEP owners might attempt to avoid district courts and obtain bargaining power in royalty negotiations by seeking exclusion orders at the ITC raises issues for the appropriate analysis of patent holdup disputes. If the ITC were to issue exclusion orders to SEP owners under circumstances in which injunctions would not be appropriate under the *eBay* standard, the inconsistency could induce SEP owners to strategically use the ITC in an effort to achieve settlements of patent disputes on terms that might require payment of supracompetitive royalties. Though it is not clear how likely this is or whether the risk has led to supracompetitive prices in the past, this dynamic could lead to holdup by SEP owners and unconscionably higher royalties.¹⁴⁴ We recognize that Congress has already established by statute standards and factors that the ITC should weigh for determining when the ITC should grant an exclusion order, but suggest that the Agencies consider offering guidance to the ITC about potential SEP holdup and holdout.

The Section believes that analysis of these issues could also yield valuable information for the Office of the United States Trade Representative (USTR) in exercising its review function to overturn what it considers to be inappropriate ITC orders. For example, can litigants be counted on to seek intervention in appropriate cases? If not, does the USTR have adequate mechanisms to ensure review when appropriate? We believe scrutiny on questions like these would be worthwhile.

¹⁴⁰ See, e.g., Chinese Antimonopoly and Anti-unfair Competition Enforcement Bureau of State Administration for Industry & Commerce, Antitrust Guideline on Intellectual Property Rights Abuses 16, available at <http://www.saic.gov.cn/fldyfbzdzjz/gzdt/201601/W020160108580399473419.pdf>.

¹⁴¹ 547 U.S. 388 (2006).

¹⁴² 19 U.S.C. § 1337(d)-(f).

¹⁴³ E.g., Colleen V. Chien & Mark A. Lemley, *Patent Holdup, The ITC, and the Public Interest*, 98 CORNELL L. REV. 1, 16 (2012).

¹⁴⁴ Whether the threat of an exclusion order is likely to lead to inflated royalties depends in part on the likelihood of an exclusion order being granted, and thus far the ITC has granted only one exclusion order on a SEP, which was disapproved by the USTR. See U.S. Trade Representative Exec. Office of the President, Disapproval of the U.S. International Trade Commission's Determination in the Matter of Certain Electronic Devices, Including Wireless Communication Devices, Portable Music and Data Processing Devices, and Tablet Computers, Investigation No. 337-TA-794 (2013), available at https://ustr.gov/sites/default/files/08032013%20Letter_1.PDF (hereinafter USTR 2013 Veto Letter to ITC).

3. Patent Acquisitions and Dispositions

The Agencies should look at purchases and sales of patents as they would other assets, to evaluate their impact on competition.

It is generally accepted that the ownership of a patent by itself is not presumed to create a presumption of market power. By the same token, acquisitions and dispositions of intellectual property, like those involving other assets, can raise questions of competitive significance. Reflecting the complexity of the setting, the Agencies should recognize the potential harms and benefits from the creation and exploitation of large patent portfolios. In some circumstances, such collections “can be used offensively, and can be valuable primarily because of their size rather than the validity of each patent in the portfolio.”¹⁴⁵ At the same time, the Agencies should take into account, as they do in other asset acquisitions, the potentially significant efficiencies from such acquisitions. In particular, they should recognize the potential benefits of aggregating complementary patents in solving the Cournot complements problem.¹⁴⁶

Combining substitute patents (*i.e.*, patents covering competing products or methods to accomplish the same objective) may raise Clayton Act issues applicable to horizontal mergers. Despite this, resolution of the competitive implications of a particular combination is often made difficult by uncertainty about the validity and scope of patents, and thus, about their competitive significance. The Agencies should use merger retrospectives to shed light on these issues.

The Agencies should also consider harm to competition that could result from disaggregating complementary patents. Disaggregating such patents could lead to a double marginalization problem that results in increased costs for technology users, and could be a strategic device for raising costs for firms that compete with one or more of the patent holders.¹⁴⁷ Enforcement actions based on the Sherman Act could be warranted depending on factors including contract terms (*e.g.*, requiring the targeting of product market rivals of the original owner) and the increased likelihood that the disposition of the patents will lead to higher aggregate prices for technology users without evident procompetitive justification.

4. Standard Development Organizations

Standard Development Organizations (SDOs) present multiple antitrust issues, including the role the Agencies should play and Sherman Act Section 1 considerations.

d. General Agency Practice

As a starting point, the Section recommends that the Agencies continue their scrutiny of SDOs. While such organizations promise significant procompetitive benefits in the form of interoperability, innovation, and enhanced consumer choice, they are also capable of having anticompetitive effects in the form of boycotts, the exercise of monopsony power, and holdup. Holdup concerns could arise from, for example, (1) the avoidance of FRAND or royalty-stacking obligations through transfer, tying, and bundling,¹⁴⁸ (2) inadequate measures to prevent patent holders from exercising market power, and (3) enabling implementers to compel subcompetitive royalty rates as a condition of including the patented technologies in the standard. On the other hand, conduct such as tying and bundling may be procompetitive or benign. There are numerous procompetitive reasons for portfolio licensing, including reducing transaction costs and providing implementers with freedom to operate.

While the guidance supplied by the Agencies as to whether certain SDO and other joint conduct may violate the antitrust laws has been instructive and should be continued, the Agencies should be careful when utilizing the business review letter process to emphasize that this form of guidance is highly fact-specific to the matter at hand. As the Division has recognized, it is unlikely that there is a “one-size-fits-all” template for analyzing SDO policies regarding IP rights. Because SDOs “vary

¹⁴⁵Michael A. Carrier, *Patent Assertion Entities: Six Actions the Antitrust Agencies Can Take*, at 2–3, CPI ANTITRUST CHRON. (Jan. 2013), available at <https://www.justice.gov/sites/default/files/atr/legacy/2013/04/03/paew-0034.pdf>.

¹⁴⁶See Mark A. Lemley & A. Douglas Melamed, *Missing the Forest for the Trolls*, 113 COLUM. L. REV. 2117, 2157–58 (2013).

¹⁴⁷See *id.* at 2158–61, 2178–80.

¹⁴⁸For a critique of the royalty-stacking theory, see Alexander Galetovic & Kirti Gupta, *Royalty Stacking and Standard Essential Patents: Theory and Evidence from the World Mobile Wireless Industry* (June 2016), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2790347.

widely in size, formality, organization and scope,”¹⁴⁹ decisions regarding specific rules are ordinarily best left to individual SDOs and their members to decide.

e. Sherman Act Section 1 Considerations

Some contend that, under certain circumstances, SDO patent policies could violate the antitrust laws.¹⁵⁰ The argument is that, first, such policies could enable even patent holders that agreed to comply with the patent policies to exercise market power *ex post* through, for example, inadequate measures to prevent the exercise of such market power. Second, they could enable technology users to exercise market power *ex ante* by, for example, requiring patent holders to agree to subcompetitive royalty rates as a condition of inclusion of their patented technologies in the standard. There is no case law that directly supports such contentions.

Standard-setting may confer market power, and in these settings, the Agencies could study the extent to which a FRAND declaration limits the potential market power derived from a patent’s inclusion in a standard. Some empirical research suggests that standardization does not confer market power, but rather serves to “crown [existing] winners.”¹⁵¹ Other research and cases show that standardization has conferred market power.¹⁵² In those instances in which an SDO creates market power in the technology market for an SEP holder, the Agencies should consider whether there may be circumstances in which the SDO might be in violation of Section 1 if it fails to take reasonable steps to prevent the exercise of that market power, such as a suitably defined and enforced FRAND policy or whatever effective alternative the SDO chooses.

As the Agencies have recognized, SDOs generally have leeway to set their own policies. While the Section acknowledges that it is a contested issue and there are strongly held opposing viewpoints, some of us believe that in appropriate cases SDO policies (or the lack thereof) can form the basis for a Section 1 claim. One example is provided by FRAND and royalty-stacking obligations, which are generally a matter of contract law, but which could conceivably form the basis of a Section 1 claim if SDOs do not implement policies that would prevent such obligations from being evaded through transfer of FRAND-encumbered patents.¹⁵³

There are a variety of possible alternatives to existing FRAND policies that SDOs might consider. These include requiring SDO members to use a certain type of arbitration when parties cannot agree on a FRAND rate and addressing the circumstances under which SDO members could seek injunctions or exclusion orders for infringement of FRAND-encumbered patents.

5. Competition Advocacy

The Agencies have done an effective job informing the PTO, USTR, Congress, ITC, and others of their competition concerns in the SEP area. In particular, the USTR disapproved an exclusion order from the ITC concerning an SEP, a decision that reflected arguments made by the Agencies.¹⁵⁴ Those efforts should be continued but are likely insufficient on their own to achieve competitive outcomes. If informed parties benefit from the status quo, competition advocacy alone will not be able to change their behavior. The Agencies could analyze the incentives that drive the remaining anticompetitive behavior, and consider what they could do to change those incentives. For example, the Agencies could (1) litigate cases that raise significant

¹⁴⁹U.S. DEP’T OF JUSTICE AND FED. TRADE COMM’N, ANTITRUST ENFORCEMENT AND INTELLECTUAL PROPERTY RIGHTS: PROMOTING INNOVATION AND COMPETITION 33–34 n.5, 48 (2007), available at <http://www.ftc.gov/reports/innovation/P040101PromotingInnovationandCompetitionrpt0704.pdf>.

¹⁵⁰*See, e.g.,* Am. Soc’y of Mech. Eng’rs v. Hydrolevel Corp., 456 U.S. 556 (1982). Seeking an injunction against a willing licensee also could potentially violate § 2 of the Sherman Act or § 5 of the Federal Trade Commission Act.

¹⁵¹*See, e.g.,* Anne Layne-Farrar & A. Jorge Padilla, *Assessing the Link Between Standards and Patents*, in INNOVATIONS IN ORGANIZATIONAL IT SPECIFICATION AND STANDARDS DEVELOPMENT 19, 2426 (Kai Jacobs ed., 2012).

¹⁵²*See, e.g.,* Rudi Bekkers *et al.*, *Declared Essential Patents* (Hoover Institution, IP2, Working Paper No. 16003, 2016); M. Rysman & T. Simcoe, *Patents and the Performance of Voluntary Standard Setting Organizations*, 54 MGMT. SCI. 11, 1920–34 (2008); David Yoffie *et al.*, *Qualcomm Incorporated 2009*, Harvard Business School case study 9–710–433 (2011); *see also, e.g.,* Rambus v. FTC, 522 F.3d 456 (D.C. Cir. 2008).

¹⁵³Note that any such liability must be consistent with the Standards Development Organization Advancement Act of 2004 (SDOAA), which extends the protections provided by the National Cooperative Research and Production Act of 1993 to SDOs. The SDOAA provides that the rule of reason applies to SDOs while they are engaged in standards development activities and limits liability to actual, as opposed to treble, damages so long as they properly notify the Agencies. 15 U.S.C. §§ 4301–4306 (2016).

¹⁵⁴*See* USTR 2013 Veto Letter to ITC, *supra* note 144.

antitrust concerns; or (2) file amicus briefs in private cases when the issues are important to obtaining procompetitive outcomes.

In the context of SDO patent policies, the Agencies have contributed to the public policy discussion and offered guidance to particular SDOs through the business review letter process. We encourage the agencies to continue reminding practitioners that general guidance does not define the limits of the law, and that the availability of guidance is not a signal that pre-approval is required or preferred before SDOs, or other entities in other areas, adopt new policies.

V. Industry-Specific Issues

A. Financial Sector

1. Interaction of Competition and Regulation

Financial markets are heavily regulated by a variety of government agencies such as the Federal Reserve (including the CFPB), SEC, and CFTC. Though government agencies in charge of competition policy have to work within the existing regulations and are in some circumstances constrained by legal precedents from using the antitrust laws to constrain industry behavior in a regulated industry, they can sometimes influence the content of the regulations and their adjudication.¹⁵⁵ The principle that competition is desirable applies to many features of financial markets and it is a very valuable application of agency resources to explain the positive and negative competitive consequences of various regulations.¹⁵⁶ As a general matter, regulations impose disproportionate burdens on small firms compared to large firms and therefore one can expect that regulations will favor large financial firms over small ones and will discourage entry of financial firms at a small scale.¹⁵⁷ The Agencies should make sure that the cost to the competitive process of those consequences should be considered as various regulatory bodies contemplate any regulatory change and evaluate current regulations.

2. Banking

By conventional competition benchmarks, the commercial banking sector in the U.S. is not highly concentrated nationally, although concentration has increased recently.¹⁵⁸ Given the generally modest national concentration in banking, despite the large size of some individual firms, calls for breaking up large national banks to promote competition¹⁵⁹ do not appear to be justified by the current state of knowledge about competition and efficiency in banking. However, some studies have found that when measured at a local level, banking is concentrated in certain areas.¹⁶⁰ Local concentration in banking can affect the availability of credit to borrowers (especially small firms) as well as the rates paid to depositors.¹⁶¹ Usual merger analysis would identify such harms and those must be considered in evaluating any merger. The Section is aware of no support for the proposition that competition policy as applied to banking should give any special consideration to stockholders or debt holders of banks (excluding depositors).¹⁶² Mergers that would enrich stockholders or debt

¹⁵⁵ See, e.g., *Credit Suisse v. Billings*, 551 U.S. 264 (2007).

¹⁵⁶ See, e.g., OECD, *Competition and Financial Markets Key Findings* (2009).

¹⁵⁷ See, e.g., Daniel K. Tarullo, Member, Board of Governors of the Fed. Reserve Sys., Statement before the U.S. Senate Committee on Banking, Housing, and Urban Affairs (Sept. 9, 2014) (noting the Federal Reserve was “cognizant that regulatory compliance can impose a disproportionate burden on smaller financial institutions” and tried to work with smaller institutions to try to minimize this burden when implementing the Dodd-Frank Act).

¹⁵⁸ For example, based on assets held, the four-firm concentration ratio of commercial banks in the United States was below 45 percent in 2014. See, e.g., Steven Schaeffer, *Five Biggest U.S. Banks Control Nearly Half Industry’s \$15 Trillion in Assets*, FORBES (Dec. 3, 2014) (reporting data from SNL Financial).

¹⁵⁹ See, e.g., Sen. Elizabeth Warren, *Reigniting Competition in the American Economy*, Keynote Remarks at New America’s Open Markets Program (June 29, 2016).

¹⁶⁰ Brian Akins et al., *Bank Competition and Financial Stability: Evidence from the Financial Crisis*, 51 J. OF FIN. AND QUANTITATIVE ANALYSIS 1 (2016).

¹⁶¹ BOARD OF GOVERNORS OF THE FED. RESERVE SYS., REPORT TO CONGRESS ON THE AVAILABILITY OF CREDIT TO SMALL BUSINESS (2012); Ben R. Craig & Valeriya Dinger, *Bank Mergers and the Dynamics of Deposit Interest Rates*, 36 J. OF FIN. SERVS. RESEARCH 111–33 (2009); Charles Kahn et al., *Bank Consolidation and the Dynamics of Consumer Loan Interest Rates*, 78 J. OF BUS. 99–133 (2005).

¹⁶² See, e.g., *Washington Mut. Sav. Bank v. Federal Deposit Ins. Corp.*, 482 F.2d 459 (9th Cir. 1973) (holding that all bank merger applications are subjected to traditional antitrust analysis and if violation is discerned, balancing of banking factors and anticompetitive effects is made, but FDIC, in weighing these interests, may not apply competitive standard more stringent than antitrust laws.); Robert E. Litan, Deputy Asst. Atty Gen., Dept. of Justice, Antitrust Div., *Antitrust Assessment of Bank Mergers*, (Apr. 6, 1994) (“The Division uses the same standards to assess the competitive impacts of all mergers, whether or not they involve banks.”).

holders but harm consumers deserve no special treatment or exception when applied to banking. Similarly, the prohibition of entry of new banking entities that could take advantage of certain scale or scope efficiencies in order to protect the profitability of existing banks is not justified from the viewpoint of competition policy. Claims that competition policy should yield to other objectives—for example, the difficulty of regulating new entities—should be evaluated relative to less costly alternatives—for example, a requirement that the new entity post sufficient financial capital to satisfy legitimate regulatory concerns. In that way, legitimate regulatory concerns can be separated from protectionist efforts to restrain competition to the detriment of consumers. An evaluation of whether current or proposed regulations needlessly distort competition would be appropriate.

3. *Setting Benchmark Prices*

Several recent cases have focused on the collective activity of firms that claim to set a rate or pricing benchmark for such things as interest rates, gold prices, aluminum prices, foreign exchange, and the like.¹⁶³ If the process turns out to be flawed either because of poor design or because the participants do something other than what they claim, the benchmark's value is affected. Although the courts in recent cases have provided some guidance, the Agencies should provide further guidance as to whether and under what circumstances such conduct is actionable and, if it is, whether it is appropriate to treat those cases as fraud, breach of contract, or antitrust cases.

4. *Creation of Markets*

Exchanges create organized markets and are often regulated by sector-specific agencies like the SEC or CFTC. In many unregulated sectors, entities also may collaborate to create de facto markets, though not organized. The creation of markets, whether organized formally or not, requires collective action among participants. Information is often exchanged and certain rules on participation might be specified. A joint venture that collects information can misuse that information to exclude others from getting it. At the same time, rules limiting participation or conduct of participants can be desirable in order to prevent free riding, thereby enabling the markets to exist.¹⁶⁴ Liquidity is a key attribute of many markets and rules that enhance liquidity at the expense of broad participation can be desirable. Forcing access to certain clearing functions of exchanges can be a form of free riding. The Division should remain vigilant that the creation and operation of financial services markets remain open, transparent, and accessible for all market participants. Experience has shown that transparent market exchanges drive procompetitive benefits and efficiencies, often leading to reduced prices and expanded output of market-made transactions.¹⁶⁵

B. Healthcare Industry

1. *Antitrust Enforcement by the FTC and Division Following Healthcare Reform*

The healthcare industry is one of the largest sectors in the U.S. economy, accounting for approximately one-fifth of GDP.¹⁶⁶ Parts of the public as well as the private U.S. healthcare system are based on principles of competition, and therefore the system only functions as well as the markets that support it.¹⁶⁷ This point also applies to the operation of the Affordable Care Act (ACA), which requires competition in healthcare markets to be cost effective. However, as suggested by the ACA and recognized by the FTC and the Division, some forms of cooperation between providers

¹⁶³See, e.g., *Gelboim v. Bank of Am. Corp.*, 823 F.3d 759 (2d Cir. 2016) (U.S. dollar London Interbank Offered Rate); *In re Aluminum Warehousing Antitrust Litig.*, 833 F.3d 151 (2d Cir. 2016) (the “Midwest Premium” for aluminum); *In re London Silver Fixing, Ltd., Antitrust Litigation*, No. 14-MD-2573 (VEC), 2016 WL 5794777 (S.D.N.Y. Oct. 3, 2016) (the silver “Fix Price”); *In re Commodity Exchange, Inc. Gold Futures and Options Trading Litigation*, No. 14-MD-2548 (VEC), 2016 WL 5794776 (S.D.N.Y. Oct. 3, 2016) (the gold “Fix Price”); *Alaska Electrical Pension Fund v. Bank of America Corp.*, No. 14-CV-7126, 2016 WL 1241533 (JMF) (S.D.N.Y. Mar. 28, 2016) (U.S. dollar ISDAfix); *In re Foreign Exchange Benchmark Rates Antitrust Litigation*, 74 F. Supp. 3d 581 (S.D.N.Y. 2015) (benchmark rates in the Foreign Exchange market).

¹⁶⁴See, e.g., *Board of Trade of City of Chicago v. United States*, 246 U.S. 231 (1918) (members of Board of Trade were restricted from trading off the exchange; the restriction forced more trading on the exchange, thereby promoting its success).

¹⁶⁵See, e.g., *id.*

¹⁶⁶ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, “BRIEFING NOTE, OECD HEALTH STATISTICS 2014: HOW DOES THE UNITED STATES COMPARE?” 3 (2014), available at www.oecd.org/unitedstates/Briefing-Note-UNITED-STATES-2014.pdf.

¹⁶⁷MARTIN GAYNOR, EFFICIENCIES ANALYSIS: FALSE DICHOTOMIES, MODELING AND APPLICATIONS TO HEALTH CARE (Aug. 3, 2014).

and others may be beneficial and not necessarily in violation of the antitrust laws.¹⁶⁸

In response to the ACA and the perceived tension between the ACA's encouragement of cooperation and the antitrust laws, the FTC and Division developed a Policy Statement¹⁶⁹ that provides a framework for analyzing networks, which at its core recognizes the continued relevance and importance of competition in healthcare reform. The Statement applies to accountable care organizations (ACOs) that serve both Medicare beneficiaries and commercially insured patients. It does not apply to mergers, which are evaluated under the Horizontal Merger Guidelines.¹⁷⁰ However, as recently acknowledged, the FTC has not filed a single enforcement action against an ACO.¹⁷¹ Its principal focus has been on mergers.

The Section recommends that the Agencies continue to challenge mergers, acquisitions and other transactions in the healthcare industry where such challenges are based on sound economic principles and focused on transactions that raise antitrust concerns. While some have argued that the goals of healthcare reform and antitrust are in conflict,¹⁷² for the reasons noted above, they are not. Effective competition in healthcare remains critical to the performance of this important sector. The Section urges the Agencies to continue to reiterate that reform does not displace competition in the healthcare industry, that antitrust enforcement is fully compatible with healthcare reform, and that mergers or conduct that reduce competition cannot be justified by measures to improve quality and lower costs that can be achieved by other means.¹⁷³

2. Agency Challenges to Healthcare Mergers

The FTC has had some notable recent success in challenging a physician merger in *St. Luke's* and healthcare provider mergers that raise competitive issues. The Section recommends that the FTC continue to challenge mergers that it believes substantially harm competition, despite the litigation risk, because of the important role competition plays in restraining the rise of national healthcare costs. As noted above, some challenges will fail, but an occasional failure does not diminish the value of litigation. Even cases that the Agencies lose help to clarify the law and demonstrate the Agencies' willingness to bring difficult cases in an effort to further develop the law. And losses in lower courts should be assessed and appealed if the decisions appear unsound. The Section encourages the FTC to appeal hospital merger decisions as it did in *Penn State Hershey Medical Center*¹⁷⁴ and *Advocate NorthShore*,¹⁷⁵ when the agency feels the court did not follow sound precedent for analyzing the competitive effects of a merger.

The Division's recent challenges to two health insurance mergers highlight the importance of careful competitive analysis of these markets.¹⁷⁶ The Section notes with interest the relevant markets pleaded in these complaints and the alleged monopsony effect of the mergers that would lower prices paid to providers. While previously relied upon,¹⁷⁷ this theory could be further expanded and explained by the Division to observers and practitioners in speeches, economic models and the like.

¹⁶⁸ Edith Ramirez, Chairwoman, Fed. Trade Comm'n, Keynote Address at Antitrust in Healthcare Conference (hereinafter "Keynote Address") (May 12, 2016), available at https://www.ftc.gov/system/files/documents/public_statements/950143/160519antitrusthealthcarekeynote.pdf ("[P]rocompetitive collaborations are already permissible under the antitrust laws.")

¹⁶⁹ Fed. Trade Comm'n & Dep't of Justice, Statement of Antitrust Enforcement Policy Regarding Accountable Care Organizations Participating in the Medicare Shared Savings Program (2011).

¹⁷⁰ The Statement provides a rule of reason analysis for ACOs that are financially or clinically integrated, *id.* at 4, and a "safety zone" for networks that enjoy 30 percent or less for each service provided by two or more of the ACO providers, *id.* at 7. It also sets forth the conduct that may be suspect for ACOs with high PSA shares. *See id.* at 10–11.

¹⁷¹ Julie Brill, Comm'r, Fed. Trade Comm'n, A Common Goal: The U.S. Federal Trade Commission's Health Care Enforcement Program and Its Implications for ACOs, Sixth Annual Accountable Care Organization Summit Preconference (June 2015), available at https://www.ftc.gov/system/files/documents/public_statements/673881/150617aco-summit.pdf.

¹⁷² *See, e.g.,* FTC v. Penn State Hershey Med. Ctr., No. 1:15-cv-2362, 2016 WL 2622372 (M.D. Pa. May 9, 2016) (denying FTC's motion for preliminary injunction), *rev'd*, 838 F.3d 327 (3d Cir. 2016).

¹⁷³ *St. Alphonsus Med. Ctr. Nampa v. St. Luke's Health Sys.*, 778 F.3d 775 (9th Cir. 2015); *FTC v. OSF Healthcare Sys.*, 852 F. Supp. 2d 1069 (N.D. Ill. 2012).

¹⁷⁴ *Penn State Hershey*, 2016 WL 2622372.

¹⁷⁵ *FTC v. Advocate Health Care*, No. 15 C 11473, 2016 WL 4063481 (N.D. Ill. June 14, 2016) (denying FTC's motion for preliminary injunction), *rev'd*, 842 F.3d 460 (7th Cir. 2016).

¹⁷⁶ *United States v. Aetna, Inc.*, No. 1:16-cv-01494 (D.D.C. filed July 21, 2016); *United States v. Anthem, Inc.*, No. 1:16-CV-01493 (D.D.C. filed July 21, 2016).

¹⁷⁷ *See United States v. Aetna, Inc.* (N.D. Tex. 1999) ("Aetna's acquisition of Prudential will also consolidate its purchasing power over physicians' services in Houston and Dallas, enabling

3. Work Product from Healthcare Workshops and Areas of Study

In an effort to keep abreast of developments in this rapidly changing industry, the FTC in conjunction with the Division and the Centers for Medicare & Medicaid Services (CMS), has held extensive workshops with industry leaders in 2014 and 2015.¹⁷⁸ The Section commends the Agencies for this joint endeavor and encourages them to continue to hold more joint workshops in the future on issues where clarity is needed, or new evidence is available that can guide policy. Medicare policies, including its payment rules, can influence provider consolidation and other aspects of market competition,¹⁷⁹ and the Section encourages FTC and Division lawyers and economists to play a more active role in influencing Medicare policies and rules so as to take into account the effect on competition and antitrust issues beyond ACOs.¹⁸⁰

Although these workshops have provided material suitable for policy development and analysis, there have been no revisions to the Policy Statements issued in 1996; few, if any, speeches by government officials outlining some of the enforcement policies coming forth from these workshops; and few enforcement actions based on the theories of harm discussed during the workshop. At a minimum the Section encourages the Agencies to consider providing more detailed, focused guidance on:

- (1) The anticompetitive use of contracting devices by dominant hospital providers as evidenced in the Division's suit against United Regional Health Care System¹⁸¹ challenging exclusive contracts, and the recent case brought by the Division against Carolinas HealthCare System challenging steering restrictions,¹⁸² What are the principles that cause the Division to choose these cases for enforcement?
- (2) The various theories of harm and potential benefits that can result from the vertical integration of hospitals and physicians,¹⁸³ insurers and physicians, and cross market consolidation of providers;¹⁸⁴ and
- (3) The broader implications of the recent FTC victories in St. Luke's, ProMedica Health System¹⁸⁵ and Penn State Hershey Medical Center, including a better understanding of cognizable, merger specific efficiencies¹⁸⁶ and how efficiencies can be achieved by contract rather than merger or consolidation.¹⁸⁷

The Section also encourages the FTC to continue its research and analysis, particularly with respect to the:

the merged entity to unduly reduce the rates paid for those services.”). *See also* Marius Schwartz, Econ. Dir. of Enft, Antitrust Div., U.S. Dep't of Justice, Buyer Power Concerns and the Aetna-Prudential Merger, 5th Annual Health Care Antitrust Forum, Northwestern University School of Law (Oct. 20, 1999).

¹⁷⁸Fed. Trade Comm'n, Examining Health Care Competition Workshops (Feb. 2014 and Mar. 2015). The materials and presentations are available at <https://www.ftc.gov/news-events/events-calendar/2015/02/examining-health-care-competition>.

¹⁷⁹*See, e.g.*, Fed. Trade Comm'n, Comments on Centers for Medicare & Medicaid Services' Proposed Changes in Contracting for Medicare Part D (March 11, 2014).

¹⁸⁰James Landman, Director at Inst. for Population Health Improvement, & Joe Miller, General Counsel for America's Health Ins. Plans, Remarks on Trends in Provider Consolidation, at Antitrust Division of the Department of Justice's Public Workshop: Examining Health Care Competition (Feb. 25, 2015) (citing Medicare payment rules).

¹⁸¹United States v. United Reg'l Health Care Sys., No. 7:11-cv-00030 (N.D. Tex. 2011).

¹⁸²United States v. Charlotte-Mecklenburg Hosp. Auth., No. 3:16-cv-00311-RJC-DCK (W.D.N.C. 2016). *See also* Fiona Scott Morton, Theodore Nierenberg Prof. of Econ. At Yale U. Sch. of Management, Healthcare Contracting, at Antitrust Division of the Department of Justice's Public Workshop: Examining Health Care Competition (Feb. 24, 2015).

¹⁸³Lawton Robert Burns, Dir. of Wharton Ctr. for Health Mgmt. & Econ. at U. Penn., Physician-Hospital Consolidation, Payer-Provider Consolidation & Payer-Provider Consolidation, at Antitrust Division of the Department of Justice's Public Workshop: Examining Health Care Competition (Feb. 25, 2015).

¹⁸⁴Leemore Dafny, Dir. of Health Enter. Mgmt. at Kellogg Sch. of Mgmt. at Nw. U., Effects of Cross-Market Combinations: Theory and Evidence from Hospital Markets, at Antitrust Division of the Department of Justice's Public Workshop: Examining Health Care Competition (Feb. 25, 2015). *See also* Leemore Dafny, Kate Ho & Robin S. Lee, *The Price Effects of Cross-Market Hospital Mergers* (Nw. Inst. For Policy Research, Working Paper 16-05, 2016).

¹⁸⁵ProMedica Health Sys. v. FTC, 749 F.3d 559 (6th Cir. 2014).

¹⁸⁶James Landman, Dir. of Inst. for Population Health Improvement, & Joe Miller, Gen. Counsel for America's Health Ins. Plans, Remarks on Trends in Provider Consolidation, at Antitrust Division of the Department of Justice's Public Workshop: Examining Health Care Competition (Feb. 25, 2015).

¹⁸⁷Kenneth Kizer, Dir. of Inst. For Population Health Improvement, U. Cal. Davis Health Sys., & Joe Miller, General Counsel for America's Health Ins. Plans, Remarks on Trends in Provider Consolidation, at Antitrust Division of the Department of Justice's Public Workshop: Examining Health Care Competition (Feb. 25, 2015).

- (4) Competitive impact of electronic health records and whether they deter patients from switching to alternative providers.

4. Reverse-Payment Settlements in the Pharmaceutical Industry

In the past two decades, the FTC has paid particular attention to settlements by which brand-name drug companies pay generic firms to settle patent litigation and delay entering the market. In its 2013 decision in *FTC v. Actavis*, the Supreme Court, though it rejected the FTC's proposal to apply a "quick look" analysis, held that these agreements could have "significant anticompetitive effects" and violate the antitrust laws under the rule of reason.¹⁸⁸ In the three years since the decision, courts have begun to flesh out the *Actavis* framework.

The issue that has received the most attention is whether the term "payment" is limited to cash or whether it extends to other types of consideration. The overwhelming majority of courts—including two Federal courts of appeals—that has analyzed the issue has held that payment is broader than cash.¹⁸⁹ These decisions are consistent with the emphasis of substance over form in antitrust. Other issues that the Agencies may confront in the years ahead include the antitrust analysis the courts should apply, the role of the patent merits, causation, pleading requirements, and the role of state law.

For the past two decades, the FTC has played a crucial role in litigating reverse-payment settlement cases, filing amicus briefs, collecting settlements filed under the 2003 Medicare Modernization Act, and raising awareness of these issues. With jurisprudence accumulating in the wake of *Actavis*, the Section encourages the FTC to provide much-needed guidance to businesses, consumers, and the courts.

5. "Product Hopping"

Another issue that has arisen in the pharmaceutical industry is "product hopping," which occurs when a brand-name drug company switches from one version of a drug to another. Most reformulations, especially those made when a generic is not about to enter the market, do not raise anticompetitive concerns. But some may. By reformulating a drug and switching the prescription base to the new product, a brand firm can avoid regulatory regimes designed to encourage generic entry, namely the Hatch-Waxman Act and state drug product selection laws.

The courts have tended to distinguish between "hard switches," viewed as anticompetitive because the brand removes the original drug from the market, and "soft switches," viewed as not concerning because the original remains on the market. Some recent scholarship has contended that this distinction should not be accorded dispositive significance, and has argued that both types of behavior could conceivably not make economic sense absent its impairment of generic competition.¹⁹⁰ Other scholarship has argued that neither type of conduct should violate the antitrust laws given the risks involved with asking courts to second-guess the value of innovation.¹⁹¹

The Section recommends that the FTC continue to follow developments in this area and to share its analysis of the nuances and consequences of product hopping and any nuances and consequences of adjudicating these cases. The Section also recommends that the FTC share its views through amicus curiae briefs in these cases as appropriate.

6. Pharmaceutical Samples

One practice that has recently received attention and that could have an effect on the development of generic drugs is brand firms' refusal to provide samples to

¹⁸⁸ 133 S. Ct. 2223, 2237–38 (2013).

¹⁸⁹ *In re* Loestrin Antitrust Litig., 814 F.3d 538, 549 (1st Cir. 2016); *King Drug Company of Florence v. Smithkline Beecham Corp.*, 791 F.3d 388, 403 (3d Cir. 2015); *In re* Opana ER Antitrust Litig., 162 F. Supp. 3d 704, 717 (N.D. Ill. 2016); *In re* Actos End Payor Antitrust Litig., 2015 WL 5610752, at *13 (S.D.N.Y. Sept. 22, 2015); *In re* Aggrenox Antitrust Litig., 94 F. Supp. 3d 224, 242 (D. Conn. 2015); *United Food & Commercial Workers Local 1776 & Participating Employers Health & Welfare Fund v. Teikoku Pharma USA*, 74 F. Supp. 3d 1052 1069–70 (N.D. Cal. 2014); *In re* Effexor XR Antitrust Litig., 2014 WL 4988410, at *20–22 (D. N.J. Oct. 6, 2014), appeal docketed and consolidated with *In re* Lipitor Antitrust Litig., 46 F. Supp. 3d 523, 544 (D.N.J. 2014) *Lipitor*, No. 15–1184 (3d Cir. July 8, 2015); *Time Ins. Co. v. AstraZeneca AB*, 52 F. Supp. 3d 705, 709–10 (E.D. Pa. 2014); *In re* Lipitor Antitrust Litig., 46 F. Supp. 3d 523, 544 (D.N.J. 2014), appeal docketed and consolidated with *In re* Effexor XR Antitrust Litig., No. 14–4202 (3d Cir. July 8, 2015); *In re* Niaspan Antitrust Litig., 42 F. Supp. 3d 735, 751 (E.D. Pa. 2014); *In re* Wellbutrin XL Antitrust Litig., No. 08-cv-02431 (E.D. Pa. Jan. 17, 2014); *In re* Nexium (Esomeprazole) Antitrust Litig., 968 F. Supp. 2d 367, 392 (D. Mass. 2013).

¹⁹⁰ Michael A. Carrier & Steve Shadowen, *Product Hopping: A New Framework*, 92 NOTRE DAME L. REV. 167 (2016).

¹⁹¹ Dennis Carlton, Frederick Flyer & Yoad Shefi, *Does the FTC's Theory of Product-Hopping Promote Competition?*, 12 J. OF COMP. LAW & ECON. 495–506 (2016).

generic manufacturers that request them. Under the Food and Drug Administration Amendments Act of 2007 (FDAAA), the FDA may require the use of Risk Evaluation and Mitigation Strategies (REMS) if needed to ensure that a drug's benefits outweigh its risks.¹⁹² Nearly 40 percent of new drugs are subject to REMS restrictions, with many of these including distribution restrictions.¹⁹³

Although REMS programs serve important purposes, Congress was concerned that they could delay generic entry, and thus made clear that holders of REMS-covered products would not be able to use REMS to “block or delay approval” of an Abbreviated New Drug Application (ANDA).¹⁹⁴ A central element of the Hatch-Waxman Act was a generic manufacturer's ability to rely on the brand's clinical studies if it could show that its drug was bioequivalent to the brand's drug. Bioequivalence can be established by testing samples of the brand drug, which (absent REMS) generics can acquire from distributors or wholesalers.¹⁹⁵ The challenge is that when an REMS program prevents distributors and wholesalers from selling the drug, and the brand refuses to sell to the generic, the generic lacks access to the samples needed for testing and may not be able to demonstrate bioequivalence in order to obtain an ANDA.¹⁹⁶

Generally, a firm does not have a duty to deal with its competitors. But the REMS restrictions imposed by the FDA can raise complex questions of market access. The interplay of competition and the regulatory regime calls for close scrutiny. The FTC has participated as amicus curiae in cases raising this issue,¹⁹⁷ and the competitive effects of distribution systems in the industry remain the subject of studies outside REMS settings.¹⁹⁸ The Section also recommends that the FTC monitor and comment on potential legislative and regulatory approaches to the issue that might be viable complements or alternatives to antitrust enforcement.

VI. INTERNATIONAL

A. Establishing U.S. Focus and Leadership in International Antitrust Policy

1. Dramatic Recent Growth in Global Antitrust Enforcement

A dramatic expansion in active competition law enforcement that began in the 1980s now encompasses more than 130 jurisdictions and virtually every significant transaction, business enterprise, and economic sector worldwide. This global expansion of antitrust rules undoubtedly did much to enhance competition, most obviously by increasing the scope of business activity subject to legal limitations on “hard-core” cartel conduct. Such hard-core cartel prohibitions are among the most analytically sound and widely-supported policies characteristic of free-market economies. Limitations on anticompetitive structural transactions as well as on unilateral conduct by monopolists or “dominant” firms also are based upon persuasive policy rationales and enjoy broad support, although design and implementation of the latter prohibitions involve a variety of significant challenges.

On the broadest level, global acceptance of the idea of free markets and the appropriate role of legal proscriptions on anticompetitive business conduct has been revolutionary in scope—and may constitute a fundamental reorientation of microeconomic policy thinking with the long-run potential to provide significant economic benefits for all participants in the global economy. But the jurisdiction-by-jurisdiction process that produced this worldwide antitrust expansion also created numerous and conflicting variations in nearly every aspect of competition law—including substance, procedure, remedy, institutional framework, and many other key characteristics of antitrust enforcement and compliance.

This huge antitrust expansion dramatically increased the cost and complexity of compliance. While industries, companies and business activities operate increasingly across borders, enforcement is still primarily national (with important supranational and subnational enforcement regimes as well—*e.g.*, the EU and Mercosur, EU Member States, states of the U.S., autonomous regions of Spain, provinces and other sub-

¹⁹² 21 U.S.C. § 355–1(a)(1).

¹⁹³ Darren S. Tucker, Gregory F. Wells & Margaret E. Sheer, *REMS: The Next Pharmaceutical Enforcement Priority?*, 28 ANTITRUST 74, 74 (2014).

¹⁹⁴ 21 U.S.C. § 355–1(f)(8).

¹⁹⁵ Lauren Battaglia, *Risky Conduct with Risk Mitigation Strategies? The Potential Antitrust Issues Associated with REMS*, ANTITRUST HEALTH CARE CHRON., Mar. 2013, at 26, 28.

¹⁹⁶ See generally HOVENKAMP ET AL., *IP AND ANTITRUST*, Chap. 15 (2015 Supp.).

¹⁹⁷ See, *e.g.*, *Mylan Pharmaceuticals, Inc. v. Warner Chilcott Pub. Lim Co.*, No. 15–2236, 2016 WL 5403626 (3d Cir. Sept. 28, 2015).

¹⁹⁸ For discussion of antitrust concerns raised by restricted distribution systems outside the REMS setting, see Michael A. Carrier, Nicole Levidow, & Aaron S. Kesselheim, *Using Antitrust Law to Challenge Turing's Daraprim Price Increase*, 31 BERKELEY TECH. L. J. (forthcoming 2017), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2724604.

ordinate jurisdictions in China, etc.). There are numerous and still-expanding opportunities for friction, complexity, and inefficiency capable of adversely affecting the economy, the business community, and consumers inside and outside the U.S. Costs can arise from inapt substantive standards (including intermixture and confusion within many competition laws of both economic and other policy goals), lack of transparency, inadequate procedural protections, inexperienced decision makers, and institutions struggling to deal with the complexities of antitrust law, economics and procedure essential to effective antitrust enforcement. Moreover, the near-universal practice of applying local antitrust rules to any conduct that results in adverse local competitive effects—regardless of the nationality or location of the parties or of the offending conduct—assures that businesses must deal constantly with the complex interactions of numerous and to some extent conflicting provisions of competition laws of a multitude of jurisdictions, regardless of where their operations are located.

The potential that such costs and frictions would arise as antitrust expanded globally was anticipated early on by the antitrust enforcement community (agency officials, scholars, members of the antitrust bar, the business community, and others). Solutions were sought through a variety of institutions and processes. Existing frameworks for international coordination to identify and minimize these costs and complexities (primarily the ICN, created in 2001, and the Competition Committee of the OECD, whose institutional pedigree traces back to the Marshall Plan, as well as a broad web of both ad hoc and formalized bilateral interagency relationships) offer some scope for discussion and reform. These networks of bilateral and multilateral relationships have been active for decades. Over time, this interaction has consistently encouraged the broader adoption of enforcement modalities of, such as criminal procedures and remedies, leniency programs, surreptitious surveillance and other sophisticated investigation techniques, as well as systems of private redress, including possibilities for collective actions similar to class actions. But harmonization and/or amelioration of conflicting elements of international enforcement remains challenging, and many conflicts remain to be resolved.

The Agencies have contributed enormously to the progress of competition law and procedure, and we believe they can improve the effectiveness of their efforts. From at least the early 1980s, the Division generally included international matters within the portfolio of a specific Deputy Assistant Attorney General (“DAAG”), eventually making this the sole responsibility of an “international” DAAG. But that dedicated position no longer exists. By contrast, the FTC has assembled and maintained a well-staffed, experienced and focused International Division. There has long been a Foreign Commerce Section at the Division, but it is much smaller and appears to be active at a more technical level in recent years, relative to the FTC International Division. In the meantime, the international antitrust enforcement landscape has rapidly grown more complex, suggesting that restoring the position of the International DAAG would give the Division a clearer voice and facilitate more coordination in the Agencies’ approach to this critical area.

There is no self-evident formula for strengthening current international antitrust assistance and reform efforts by the United States. One option that should be considered is to establish a transparent, formal, and consistent process for coordinating the two Federal enforcement agencies’ efforts in the field of international antitrust policy. The agencies should be encouraged to:

- (5) Develop a mechanism to coordinate their efforts to monitor global developments;
- (6) Anticipate the adverse effects of flawed foreign legislation;
- (7) Identify ill-advised and conflicting mandates embodied in underlying substantive law, inadequate procedural protections, institutional arrangements, and other troublesome features of international competition-law regimes that adversely affect U.S. consumers and businesses, the U.S. economy, and the world economy; and
- (4) Identify or open appropriate channels to engage the Executive Branch when necessary to resolve elevated disputes.¹⁹⁹

¹⁹⁹ There is some history of successful attempts to escalate pressing current international antitrust enforcement frictions up through the Executive Branch: leading examples include the merger of Boeing with McDonnell-Douglas and addressing recent and serious due process issues in Asian jurisdictions. These tend to be ad hoc interventions, where essential, to address enterprise-threatening problems that agency-to-agency contacts have failed to resolve. There appears to be no formal mechanism to invoke Executive Branch assistance outside of crisis-generating events.

B. Clarify the Jurisdictional Character of the FTAIA

Congress adopted the Foreign Trade and Antitrust Improvements Act (FTAIA) in response to concerns from U.S. businesses that strict application of U.S. antitrust law to their foreign conduct would disadvantage them in competition against non-U.S. companies. Although the law has been criticized for its lack of clarity, it was clear in the legislative history and to those involved in consideration of these proposals that the FTAIA was intended to create a jurisdictional limit, rather than an additional substantive element of a Sherman Act violation.²⁰⁰ Other potential bases for limiting the reach of U.S. antitrust law—substantive law and comity—were explicitly excluded from the FTAIA’s intended scope. Although its precedential force is subject to debate, the Supreme Court accepted the jurisdictional character of the FTAIA in its first decision construing the law.²⁰¹

More recently, however, several Federal appellate courts have opined that FTAIA is substantive, not jurisdictional.²⁰² This evolution emerged adventitiously from a civil rights decision, *Arbaugh v. Y & H Corp.*²⁰³ In that context, the Court adopted the simple rule that limitations placed on statutory rights would be regarded as substantive unless specifically declared jurisdictional by the Congress. The Court did not, however, consider whether its opinion would or should have retroactive effect on the FTAIA’s specific limitations on antitrust law.

Classifying the FTAIA as substantive shifts the question of extraterritorial reach from the early pleading stage to merits discovery, later pleading stages, and/or trial. Eliminating the possibility of early dismissal of antitrust claims against foreign parties and conduct subjects defendants to the well-recognized expense, burden, and delay characteristic of U.S. antitrust litigation, even with regard to claims falling outside U.S. jurisdiction.²⁰⁴

In prior litigation, including as recently as 2011, the Agencies have taken the position that the FTAIA is a jurisdictional limit.²⁰⁵ The Section urges the Administration and the Agencies to continue to help clarify that the FTAIA is a jurisdictional statute by means of advocacy, legal positions taken in agency cases and *amicus* briefs submitted to courts presiding in private and/or state antitrust cases, and/or through legislation if appropriate. Congress’s intent is abundantly clear to those familiar with the history of the policy debate and the legislative record of the FTAIA. The foreign reach of U.S. antitrust is a critical policy question that is better settled by direct confrontation of the key issues, rather than by requiring a search for “magic words” in prior legislation.

Parties should not be forced to engage in discovery and merits defense of claims where it can be determined at the outset that the impugned conduct lacks the defined material nexus with U.S. economic interests specified in the FTAIA. A substantive construction of FTAIA is contrary to these bedrock considerations, while a jurisdictional construction supports them.

C. Encourage Direct Agency Intercession in Foreign Agency Proceedings

3. Background

U.S. agencies characteristically engage in a great deal of substantive analysis—concerning the law, theoretical and empirical economics, and antitrust policy—in connection with matters that they investigate. It is an increasingly frequent pattern in international antitrust enforcement that similar transactions and conduct arise in many jurisdictions—and fall to be considered by antitrust agencies in a variety of jurisdictions—at about the same time. Multinational merger enforcement is an obvious example, but the same should be said of matters involving cartels, joint ventures, intellectual property activity, and dominant-firm conduct.

It is widely appreciated that the U.S. agencies are often in direct communication with foreign counterparts where investigations involve similar parties, industries, or competitive practices. It appears that such discussions can improve case outcomes—by clarifying the economic theory of a case, by improving the accuracy of the factual conclusions underlying a decision, or by harmonizing remedies adopted in different

²⁰⁰ See, e.g., Abbott B. Lipsky, Jr. & Kory Wilmot, *The Foreign Trade Antitrust Improvements Act: Did Arbaugh Erase Decades of Consensus Building?*, ANTITRUST SOURCE at 7–9 (2013), available at www.americanbar.org/content/dam/aba/publishing/antitrust_source/aug13_lipsky_7_30/authcheckdam.pdf.

²⁰¹ See *F. Hoffman-La Roche Ltd. v. Empagran S.A.*, 542 U.S. 155, 162 (2004).

²⁰² E.g., *Minn-Chem, Inc. v. Agrium Inc.*, 683 F.3d 845 (7th Cir. 2012); *Animal Sci. Prods., Inc. v. China Minmetals Corp.*, 654 F.3d 462 (3d Cir. 2011).

²⁰³ 546 U.S. 500 (2006).

²⁰⁴ See, e.g., Lipsky & Wilmot, *supra* note 203, at 1–2.

²⁰⁵ See, e.g., *Br. for the United States of America* at 6–7, *United States v. AU Optronics Corp., et al.*, No. CR–09–0110 (N.D. Cal. Apr. 8, 2011).

jurisdictions and thereby reducing their collective burden on parties involved in cases of cross-border conduct.

6. The Agencies Should Enhance Efforts to Communicate with Foreign Counterparts on Issues Affecting U.S. Industries and Firms

The Agencies should demonstrate an increased willingness to communicate directly with foreign antitrust agencies considering matters involving U.S. industries and firms. Where appropriate legal grounds exist, and where otherwise consistent with U.S. policy, the Agencies should actively seek to intercede in foreign enforcement proceedings involving U.S. firms. Where there are existing bilateral channels, they should be used for this purpose, but the agencies should not hesitate to explore new channels, as may be feasible and appropriate in particular circumstances. This is particularly important for cases where basic procedural standards are materially deficient, or where foreign agency actions (or proposed actions) are contrary to sound substantive law, to consensus notions of territoriality, or to other practices that enjoy broad consensus support among antitrust enforcement authorities in numerous jurisdictions.

D. Engage in a Critical Self-Assessment of U.S. Antitrust Procedures

The international antitrust community has engaged in extensive critical examination of a wide variety of topics in antitrust enforcement, including substantive law, institutional design, and many other aspects of competition law. Recently there has been a surge of interest in the question of antitrust procedure—which procedures best support accurate, impartial, and efficient antitrust decisions? On May 22, 2015, the Section issued a Report on Best Practices for Antitrust Procedure, covering all main phases of government antitrust proceedings: investigation, alleging infringement, conducting proceedings to assess and render judgment upon such allegations and formulation of remedies for infringements, including the process of appeal and review.²⁰⁶ The ICN recently adopted Guidance regarding Investigative Procedure, covering issues of this character that arise in the pre-complaint investigation phase of government antitrust investigations.

VII. CONCLUSION

The ABA Section of Antitrust Law is grateful for the opportunity to present this Report to the Administration. The Section looks forward to working closely with the Division and the FTC over the next four years, and stands ready to be of service to the Administration and the Agencies in the critical task of promoting and preserving free and open competition in the Nation's economy.

²⁰⁶ AM. BAR ASSOC. SECTION OF ANTITRUST LAW, BEST PRACTICES FOR ANTITRUST PROCEDURE (2015), available at http://www.americanbar.org/content/dam/aba/directories/antitrust/dec15_lipsky_tritell_12_11f.authcheckdam.pdf.

FILE NOS. 1623079, 1623080, 1623081, & 1623082

COMMENTS OF WASHINGTON LEGAL FOUNDATION
TO THE FEDERAL TRADE COMMISSIONCONCERNING PROPOSED CONSENT AGREEMENTS AND REQUEST
FOR PUBLIC COMMENTS IN ZERO-VOC PAINT CLAIMS CASESIN RESPONSE TO THE PUBLIC NOTICE PUBLISHED AT 82 FED. REG. 32,818
(JULY 18, 2017)

Dear Commissioners:

As set forth below, the Washington Legal Foundation (“WLF”) strongly objects to the Federal Trade Commission’s (the “FTC,” the “Commission”) proposed efforts to re-open and “harmonize” the consent orders issued in the PPG Architectural Finishes, Inc. (Docket No. C-4385) and The Sherwin-Williams Company (Docket No. C-4386) cases, with the consent orders the FTC recently entered into with Benjamin Moore & Co, Inc. (File No. 1623079), ICP Construction, Inc. (File No. 1623081), Imperial Paints (File No. 1623080), and YOLO Colorhouse (File No. 1623082), which the FTC published on July 11, 2017 (“New Orders”).

WLF believes that the proposed New Orders and related harmonization proposal run a grave risk of sacrificing many of the benefits derived from the previously consensus-based Green Guides, whereby the agency exhibited regulatory humility and filled gaps in its knowledge and expertise by working with industry and consumers. WLF believes that “[t]hose regulated by an administrative agency are entitled to ‘know the rules by which the game will be played.’”¹ Accordingly, modifying the Green Guides with respect to emissions and VOC-free claims, in WLF’s view, requires further notice-and-comment proceedings. The Green Guides create what are essentially substantive rules, requiring that they be amended directly only through a notice-and-comment process.² Changing the Green Guides outside of the notice-and-comment process erodes the FTC’s effectiveness and undermines its ability to successfully defend its use of agency discretion.³

Even if such notice-and-comment proceedings are not required, such proceedings would be a better way to avoid disrupting the settled expectations of the industry. Notice-and-comment proceedings would also serve to rein in critics’ perceptions that the Commission has overstepped its bounds through the sweeping embrace of a new “common law” of negotiated settlements, especially in this particular case where the latest proceedings, if approved by the Commission, would have the effect of changing substantive law without explanation.

WLF submits this comment to the FTC with respect to all of the above-referenced proposed New Orders published on July 11, 2017.

I. Interests of WLF

Founded in 1977, WLF is a nonprofit, public-interest law firm and policy center based in Washington, DC, with supporters throughout the United States. WLF devotes a substantial portion of its resources to defending free enterprise, individual rights, limited government, and the rule of law. To that end, WLF regularly appears before Federal administrative agencies, including the FTC, to ensure adherence to the rule of law.⁴ Likewise, WLF has participated as *amicus curiae* in litigation challenging the scope of the FTC’s regulatory authority under the FTC Act.⁵ In addition,

¹*Alaska Prof’l Hunters Ass’n v. FAA*, 177 F.3d 1030, 1035 (D.C. Cir. 1999) (citations omitted).

²See *infra* notes 43–46 and accompanying text.

³*Perez v. Mortgage Bankers Assoc.*, 135 S. Ct. 1199, 1209 (2015) (citing *FCC v. Fox Television Stations, Inc.*, 556 U.S. 502, 515 (2009)) (“[T]he APA requires an agency to provide more substantial justification when ‘its new policy rests upon factual findings that contradict those which underlay its prior policy; or when its prior policy has engendered serious reliance interests that must be taken into account. It would be arbitrary and capricious to ignore such matters.’”) See also Elizabeth McGill, *Agency Self-Regulation*, 77 GEO. WASH. L. REV. 859, 875 (2009).

⁴See, e.g., In re: FTC’s Proposed Information Requests to Patent Assertion Entities and Other Entities Asserting Patents in the Wireless Communications Sector, Project No. P131203 (Dec. 16, 2013) (responding to the FTC’s decision to investigate Patent Assertion Entities and contending that the proposed information requests were consistent with the requirements of the Paperwork Reduction Act, 44 U.S.C. § 3501 *et seq.*).

⁵See, e.g., *Ross v. FTC*, 135 S. Ct. 92 (2014) (challenging FTC’s authority to obtain monetary restitution under § 13(b) of the FTC Act); *FTC v. Wyndham Worldwide Corp.*, 799 F.3d 236 (3d Cir. 2015) (challenging the FTC’s authority to regulate cybersecurity breaches under the “unfairness” prong of § 5 of the FTC Act).

WLF's Legal Studies Division, the publishing arm of WLF, frequently produces articles and hosts discussions on a wide array of legal issues related to FTC activities.⁶

These proceedings raise issues that sweep much more broadly than the FTC's efforts to regulate paint manufacturers' VOC-free claims for architectural coatings. The central challenge of administrative law over the past several decades has been to "narrow[w] the category of actions considered to be so discretionary as to be exempted from review."⁷ As the size of the administrative state continues to expand, it is more imperative than ever that agencies play by the rules—especially the rule of fair notice—and that affected stakeholders continue to have a meaningful opportunity to participate in the operation of their government. Courts have criticized the increasing use of agency-created legislative rules whereby "[l]aw is made, without notice and comment, without public participation, and without publication in the Federal Register of the Code of Federal Regulations."⁸ The FTC's recent actions in the zero-VOC paint-claims cases implicate these core concerns.

II. Background

A. The FTC's Statutory Authority

Section 5 of the FTC Act authorizes the Commission to take steps to prevent businesses and individuals (with certain limited exceptions) from using "unfair or deceptive acts or practices in or affecting commerce."⁹ The FTC may use formal rule-making procedures to issue binding rules that regulate unfair or deceptive acts or practices.¹⁰ The FTC may act less formally by publishing guidance, enforcement policies, and other public statements to further its statutory objectives. Alternatively, the FTC may investigate, commence civil actions against, and obtain agreement to consent orders with businesses and individuals that allegedly engage in unfair or deceptive acts or practices.¹¹

B. The FTC's Efforts to Regulate VOC-Free Claims for Architectural Coatings

The FTC Issues the Green Guides. In 1992, the FTC issued the "Guides for the Use of Environmental Marketing Claims,"¹² which later became known as the "Green Guides." The Green Guides represented the FTC's best understanding of how § 5 of the FTC Act applied to environmental advertising and marketing practices. The FTC updated the Green Guides in 1996, 1998, and 2012. As a basis for originally issuing and later directly amending the Green Guides, the FTC held public hearings and workshops, completed a consumer perception study, and followed notice-and-comment procedures.

The FTC Agrees to Consent Orders and Issues Green Guides Enforcement Policy. On March 6, 2013, the FTC approved consent orders with PPG Architectural Finishes, Inc. ("PPG") and The Sherwin-Williams Company ("Sherwin-Williams") to settle alleged violations of § 5 for marketing "zero VOC" paints.¹³ At the same time, the FTC published the "Enforcement Policy Statement Regarding VOC-Free Claims for Architectural Coatings" ("Enforcement Policy") without an opportunity for the public and industry to weigh in as it had with the guides themselves.¹⁴ The Enforcement Policy stated that the Commission was replacing the definition of "trace amounts of a substance" in the Green Guides with a new definition that applied specifically to VOC-free claims for architectural coatings. The Enforcement Policy also introduced the element of human safety as a factor in the advertising claim analysis. The announced Enforcement Policy signaled to the remainder of the architectural coatings industry the Commission's policy going forward.

⁶See, e.g., Kurt Wimmer, et al., *Data Security Best Practices Derived from FTC § 5 Enforcement Actions*, WLF WORKING PAPER (January 2017); John G. Greiner & Zoraida M. Vale, *FTC Intensifies Scrutiny of "Native Advertising"*, WLF LEGAL OPINION LETTER (April 15, 2016); Christopher Cole, Jerry Schwartz, & Natalia Medley, *Sustainable "Green Advertising": Implications of FTC's Guidelines for Public, Private, & Self-Regulation*, WLF WEBINAR (February 21, 2013).

⁷Martin Shapiro, *Administrative Discretion: The Next Stage*, 92 Yale L.J. 1487, 1489 n.11 (1983).

⁸*Appalachian Power Co. v. EPA*, 208 F.3d 1015, 1020 (D.C. Cir. 2000).

⁹15 U.S.C. § 45(a)(2).

¹⁰15 U.S.C. § 57a.

¹¹15 U.S.C. §§ 45(b), 57b.

¹²16 C.F.R. Part 260.

¹³Fed. Trade Comm'n, Press Release, *FTC Approves Final Orders Settling Charges Against The Sherwin-Williams Co. and PPG Architectural Finishes, Inc.; Issues Enforcement Policy Statement on "Zero VOC" Paint Claims* (Mar. 6, 2013), <https://www.ftc.gov/news-events/press-releases/2013/03/ftc-approves-final-orders-settling-charges-against-sherwin>.

¹⁴Fed. Trade Comm'n, *Enforcement Policy Statement Regarding VOC-Free Claims for Architectural Coatings* (Mar. 6, 2013), <https://www.ftc.gov/sites/default/files/documents/cases/2013/03/130306ppgpolicystatement.pdf>.

The FTC Agrees to Additional Consent Orders and Proposes to “Harmonize” All Consent Orders. On July 11, 2017, the FTC issued complaints and the New Orders with four more companies in the architectural coatings industry.¹⁵ The New Orders added yet another definition of “trace amounts” (now three) for the purposes of assessing “free-of” claims for architectural coatings. The FTC also stated that it will “propose harmonizing” these four New Orders with the PPG and Sherwin-Williams consent orders: “Specifically, the Commission plans to issue orders to show cause why those [PPG and Sherwin-Williams] matters should not be modified pursuant to Section 3.72(b) of the Commission Rules of Practice, 16 CFR 3.72(b).”¹⁶ WLF is aware of no consumer-perception studies (FTC-commissioned or otherwise) that justify the Commission’s new positions in the consent orders or the Enforcement Policy.

III. To Provide Clarity and Address Due Process and Equal Protection Concerns, the FTC Should Treat the Green Guides as Substantive Rules

The FTC Published the Green Guides Using a Rulemaking Process. The FTC published the Green Guides using a process very similar to the substantive rulemaking procedure prescribed by the Administrative Procedure Act (“APA”).¹⁷ For example, the FTC’s Green Guide-related activity included performing research on consumer understanding and perceptions, undertaking a notice-and-comment process, submitting the resulting guidance for approval by the full Commission, and—most significantly—publishing the final Green Guides in the Code of Federal Regulations.¹⁸ The FTC’s decision to formally publish the Green Guides in the Code of Federal Regulations should not be overlooked or ignored, given that the Code of Federal Regulations is “the codification of the general and permanent rules published in the Federal Register by the departments and agencies of the Federal Government.”¹⁹ Although the Commission lacks traditional APA notice-and-comment rulemaking authority, by using a process that in many respects resembled typical APA rulemaking, the Commission exercised significant regulatory humility in issuing the Green Guides, a characteristic notably absent in other areas of recent FTC activity (e.g., privacy and data security enforcement).²⁰

Industry Relies on the Green Guides as an Authoritative Rule. Although the Green Guides bear all of the hallmarks of an APA rulemaking, including publication in the Code of Federal Regulations, the FTC also suggests that the Green Guides have no substantive effect and attempts to disavow their legislative nature: “[The Green Guides] do not confer any rights on any person and do not operate to bind the FTC or the public. The Commission, however, can take action under the FTC Act [only] if a marketer makes an environmental claim inconsistent with the guides.”²¹ But surely the Commission cannot have it both ways. Interpretive guidance by an agency can and often does become binding.²² While the FTC’s reserving prosecutorial dis-

¹⁵ Fed. Trade Comm’n, Press Release, *Paint Companies Settle FTC Charges That They Misled Consumers; Claimed Products Are Emission-and VOC-free and Safe for Babies and other Sensitive Populations*, <https://www.ftc.gov/news-events/press-releases/2017/07/paint-companies-settle-ftc-charges-they-misled-consumers-claimed>.

¹⁶ See, e.g., Benjamin Moore & Co., Inc.; Analysis to Aid Public Comment, 82 Fed. Reg. 32818, 32820 (July 18, 2017), https://www.ftc.gov/system/files/documents/cases/benjamin_moore_analysis.pdf.

¹⁷ 5 U.S.C. § 553.

¹⁸ 16 C.F.R. Part 260.

¹⁹ U.S. Gov’t Publishing Office, Code of Federal Regulations (Annual Edition), <https://www.gpo.gov/fdsys/browse/collectionCfr.action?collectionCode=CFR>. 44 U.S.C. § 1510 (a) limits publication in that code to rules “having general applicability and legal effect.” See *Brock v. Cathedral Bluffs Shale Oil Co.*, 796 F.2d 533, 539 (D.C. Cir.1986) (Scalia, J.).

²⁰ See Brief of Petitioner, LabMD, Inc., at 38–43, *LabMD, Inc. v. FTC*, No. 16-16270 (11th Cir. Dec. 27, 2016) (arguing “as a matter of law consent decrees cannot provide parties with fair notice, for Due Process Clause purposes, of an agency’s interpretation of its governing statute or one of its regulations.”); *Amicus Curiae* Brief of Washington Legal Foundation, at 7, *FTC v. Wyndham Worldwide Corp.*, 799 F.3d 236 (3d Cir. Oct. 6, 2014) (arguing that “the FTC’s ‘catch-as-catch-can’ approach to regulatory enforcement under § 5 is not only deeply unfair to the business community, but it also fails far short of satisfying the legal standard for fair notice”); Appellant’s Opening Brief and Joint Appendix Vol. 1, pp JA1–55, at 41, *FTC v. Wyndham Worldwide Corp.*, 799 F.3d 236 (3d Cir. Oct. 6, 2014) (arguing that because a complaint or a consent decree “is not a decision on the merits and therefore does not adjudicate the legality of any action by any party thereto, it does not and cannot provide fair notice of what the law either requires or proscribes.”). The House of Representative Committee on Oversight and Government reform also held hearings to hear testimony on the FTC’s use of consent decrees in the privacy and data security space. Access to video of the hearings is available at <https://oversight.house.gov/hearing/federal-trade-commission-section-5-authority-prosecutor-judge-jury-2/>.

²¹ 16 C.F.R. § 260.1.

²² See *infra* note 43 and accompanying text.

cretion and exercising self-restraint through the Green Guides is admirable, stakeholders have come to rely upon the guides as authoritative and binding. The danger this incoherent approach presents was not lost on then-FTC Commissioner Azcuenaga, who dissented based on the Commission's efforts to mask these substantive provisions as "guidance."²³

The FTC cannot maintain that the Green Guides, Enforcement Policy, and even its consent orders are not substantive, while simultaneously insisting that they provide constitutionally sufficient fair notice to those entities regulated by them how to comport with the law. While the Commission frequently seeks to provide guidance, it consistently equivocates on what are best practices and what are legal requirements.²⁴ Here, in the event of a challenge, the Commission is almost certain to point to the Green Guides as authoritative sources of notice for due-process purposes.²⁵ While the Green Guides do an admirable job at addressing due-process considerations related to notice, recent efforts to modify them through enforcement proceedings create serious jurisprudential and policy concerns. On the one hand, the guides are authoritative and serve important due-process functions. On the other hand, the FTC's effort to disavow the binding nature of the guidance, which would provide some protection to regulated entities, leaves industry and the public guessing as to what the law may require at any given moment in time. As the Supreme Court has emphasized, "[i]t is one thing to expect regulated parties to conform their conduct to an agency's interpretations once the agency announces them; it is quite another to require regulated parties to divine the agency's interpretations in advance or else be held liable when the agency announces its interpretations for the first time in an enforcement proceeding and demands deference."²⁶

The Green Guides Lose Authoritativeness When Amended by Consent Orders. Amending the Green Guides through means other than directly via the previously used notice-and-comment process diminishes their authoritativeness, which may negatively impact the deference courts give them and leaves them more susceptible to attack if the Commission attempts to use them as a basis for an enforcement action. Agency deference by courts is based, in part, on an agency's formality, thor-

²³ Commissioner Azcuenaga stated, "As the guides expressly state, the majority of the Commission does not view its guides as having the force and effect of law but as explanations of existing statutory terms and obligations. . . . I cannot agree. By stating definitively, for example, that a particular act 'is deceptive' or that particular conduct 'would be deceptive,' or that under specified circumstances, firms 'must' or 'should' act in a particular way, language that appears throughout the document, I believe that the document has 'defined with specificity' a deceptive act or practice as set forth in section 18(a)(1)(B) [requiring Magnuson-Moss rule-making]." Dissenting Statement of Commissioner Mary L. Azcuenaga Concerning Issuance of Commission Guides on Environmental Marketing Claims, 57 Fed. Reg. 36363, 36368 (Aug. 13, 1992).

²⁴ See, e.g., FED. TRADE COMM'N, PROTECTING CONSUMER PRIVACY IN AN ERA OF RAPID CHANGE: RECOMMENDATIONS FOR BUSINESSES AND POLICYMAKERS, at vii (2012), <http://ftc.gov/os/2012/03/120326privacyreport.pdf> ("The final privacy framework is intended to articulate best practices for companies that collect and use consumer data. These best practices can be useful to companies as they develop and maintain processes and systems to operationalize privacy and data security practices within their businesses. The final privacy framework contained in this report is also intended to assist Congress as it considers privacy legislation. To the extent the framework goes beyond existing legal requirements, the framework is not intended to serve as a template for law enforcement actions or regulations under laws currently enforced by the FTC."); FED. TRADE COMM'N, FACING FACTS: BEST PRACTICES FOR COMMON USES OF FACIAL RECOGNITION TECHNOLOGIES, at iii (2012), https://www.ftc.gov/sites/default/files/documents/reports/facing-facts-best-practices-common-uses-facial-recognition-technologies/121022facial_tech_rpt.pdf ("The recommended best practices contained in this report are intended to provide guidance to commercial entities that are using or plan to use facial recognition technologies in their products and services. However, to the extent the recommended best practices go beyond existing legal requirements, they are not intended to serve as a template for law enforcement actions or regulations under laws currently enforced by the FTC.")

²⁵ Whether FTC guidance can provide authoritative notice that satisfies constitutional fair-notice requirements remains unanswered. In a case against LabMD, Inc., the FTC has asserted that its guidance "Protecting Personal Information: A Guide for Business" provided the defendant with notice of reasonable security standards. See Brief of the Federal Trade Commission at 50–52, *LabMD, Inc. v. FTC*, No. 16–16270 (11th Cir. Feb. 9, 2017) (referencing the Guide for Business, complaints, and consent decrees related to data security, and published guides by other Federal agencies). In the FTC's case against Wyndham, the district court held that the FTC is not required to promulgate formal rules before enforcing § 5, and noted that some of the other publications by the FTC (including complaints and consent orders) provide some guidance. *FTC v. Wyndham Worldwide Corp.*, 10 F. Supp. 3d 602, 617–21 (D.N.J. 2014). On appeal, the Third Circuit also did not reach the question of whether the FTC's guidance provides authoritative notice of the FTC's interpretation of "reasonable security." *FTC v. Wyndham Worldwide Corp.*, 799 F.3d 236 (3d Cir. 2015). The appellate opinion in the LabMD case may provide greater clarity.

²⁶ *Christopher v. SmithKline Beecham Corp.*, 576 U.S. 142, 158–59 (2012).

oughness in its consideration, and consistency of its statements.²⁷ These factors may not be met when settlement agreements with private parties repeatedly change the substantive legal requirements and interpretations without justifying departing from the formal notice-and-comment process, as is the case here. By reducing the formality used when changing substantive rules and failing to use a process that incorporates industry and consumer input, the FTC has undermined the likelihood that courts will accord the agency deference when evaluating environmental-marketing decisions under the arbitrary and capricious standard.²⁸

The Green Guides' Effectiveness Is Diminished When They Are Amended Outside of the Notice-and-Comment Process. Amending the Green Guides without justification or explication through negotiated consent decrees via enforcement investigations rather than using the previously established notice-and-comment process also reduces the guides' effectiveness as interpretive guidance for regulated businesses, thereby undercutting the Commission's goal in publishing them in the first place. Instead of looking solely to the Green Guides, businesses must now look to the Green Guides, the Enforcement Policy, and myriad settlement agreements negotiated without the participation of all relevant industry stakeholders to try to ascertain the FTC's expectations. Accordingly, businesses wishing to make environmental-marketing claims arguably do not have fair notice of the law. Moreover, they face the risk of arbitrary regulatory enforcement because the FTC could change its mind at any time. In contrast, treating the Green Guides like an agency rule would allow businesses and entities to know that changes will not be made without the opportunity to participate in an open and transparent process that provides a full opportunity to be heard.

The Green Guides are imperfect, but at least they are relatively clear, authoritative statements developed with industry and consumer participation—and fundamentally they derive from efforts to understand precisely how consumers view and interpret certain types of environmental claims. Such participation is the foundation of both due process and regulatory humility. Assuming the FTC wants the Green Guides to be authoritative and followed by businesses and individuals, the Commission should treat them as authoritative statements, thereby reassuring the public that the Green Guides will be updated in a transparent, predictable, and participatory manner.

IV. Case-By-Case Legislation by Consent Decree Is Inappropriate

The FTC Can Choose Between Rulemaking and Adjudication to Execute Congressionally Delegated Powers. Generally, Federal agencies have discretion to choose between rulemaking and enforcement to execute their statutory responsibilities.²⁹ The FTC's rulemaking authority is specifically circumscribed by Congress. To use its rulemaking authority, the FTC must follow additional requirements that are more cumbersome than the routine APA process.³⁰ Congress has imposed additional requirements on the Commission because of its "grossly overreaching proposal" to regulate advertising to children in the 1970s.³¹ Unfortunately, history may be repeating itself with the Commission's increasing commitment to legislation-by-negotiated-consent-decree. The FTC's use of its adjudicatory authority generally is understandable. But here, where the Commission has seemingly abandoned—without expla-

²⁷ "The fair measure of deference to an agency administering its own statute has been understood to vary with circumstances, and courts have looked to the degree of the agency's care, its consistency, formality, and relative expertness, and to the persuasiveness of the agency's position." *United States v. Mead Corp.*, 533 U.S. 218, 228 (2001) (internal citations omitted); *Chevron U.S.A. Inc. v. Natural Res. Def. Council, Inc.*, 467 U.S. 837, 844 (1984). "The weight [accorded to an administrative] judgment in a particular case will depend upon the thoroughness evident in its consideration, the validity of its reasoning, its consistency with earlier and later pronouncements, and all those factors which give it power to persuade, if lacking power to control." *Skidmore v. Swift & Co.*, 323 U.S. 134, 140 (1944).

²⁸ *Perez v. Mortgage Bankers Assoc.*, 135 S. Ct. 1199, 1209 (2015) (citing *FCC v. Fox Television Stations, Inc.*, 556 U.S. 502, 515 (2009)) ("[T]he APA requires an agency to provide more substantial justification when 'its new policy rests upon factual findings that contradict those which underlay its prior policy; or when its prior policy has engendered serious reliance interests that must be taken into account. It would be arbitrary and capricious to ignore such matters.'").

²⁹ See *SEC v. Chenery Corp.*, 332 U.S. 194, 203 (1947). Congress may limit or provide rulemaking and/or enforcement authority. *Id.* at 196, 207.

³⁰ See Lydia B. Parnes & Carol J. Jennings, *Through the Looking Glass: A Perspective on Regulatory Reform at the Federal Trade Commission*, 49 ADMIN. L. REV. 989, 995 (1997).

³¹ Fed. Trade Comm'n, *Advertising to Kids and the FTC: A Regulatory Retrospective That Advises the Present*, 8 (Mar 2, 2004), <https://www.ftc.gov/sites/default/files/documents/public-statements/advertising-kids-and-ftc-regulatory-retrospective-advises-present/040802adstokids.pdf>.

nation—use of an interpretive process that was working well, it leaves much to be desired.

The FTC Has Abandoned Its Rulemaking Procedures in Favor of Guidance and Adjudication. The inefficient and time-consuming process Congress imposed through the Magnuson-Moss Act has led the FTC to all but abandon even its statutorily prescribed rulemaking authority.³² Instead, the Commission appears in recent years to have begun legislating through consent decree (*e.g.*, in the area of data privacy and security)³³ or using a quasi-rulemaking process such as the one previously used to issue and directly amend the Green Guides. After the FTC's rulemaking authority was so substantially restricted by Congress, the Commission undermines whatever authority it retains by overreaching in its use of enforcement-action settlements as a substitute for substantive and binding lawmaking processes like those used to publish the Green Guides.

The FTC's Guidance and Adjudication Process Has Taken the Place of Rulemaking. The FTC's recent Green Guides enforcement activity against the architectural coatings industry appears to be an end-around the rigorous rulemaking procedures that Congress assigned to the FTC. Until these latest order-related changes to the rules, the FTC utilized a "guide-making" process that closely resembles the APA's notice-and-consent rulemaking process to issue and directly amend the Green Guides. This process provides clear due process, equal protection, and related policy benefits, including the kind of broad-based participation and transparency that bolsters the Commission's stature as the premier consumer-protection law enforcement agency. But the FTC's subsequent Enforcement Policy and two sets of consent orders dramatically change the Green Guides without those same procedural safeguards and policy benefits. Inexplicably, the FTC now seeks to "harmonize" all of the consent orders to require six members of the architectural coatings industry to comply with consistent "rules" on emissions and VOC-free claims. This is *de facto* legislation through consent orders and, under FTC's proposed process, no effective negotiation is available among and by the public, non-parties, and arguably even parties to the prior orders whose settled expectations will now be upended.

The FTC's Regulatory Approach to the Architectural Coatings Industry Raises Practical Challenges. The FTC has not indicated what it will do with the seemingly obsolete Enforcement Policy. Under the FTC's recently proposed order-related changes, anticipating precisely what the law is for architectural coatings emissions and VOC-free claims seems virtually impossible. The PPG and Sherwin-Williams orders and Enforcement Policy differ markedly from the Green Guides, in that they introduce the concept of protecting human health to change how the VOC-level would be measured. And because the New Orders drastically expand the scope of coverage from only VOCs to *any* emissions, they are inconsistent with the PPG and Sherwin-Williams orders and Enforcement Policy—hence the FTC's stated desire to obtain "harmonization."

The FTC's approach also creates competition-policy concerns triggered by the FTC's having closed-door meetings with some industry participants during consent-order negotiations and providing them with informal guidance not provided to other industry participants. As a result, architectural coatings businesses have a confusing array of FTC regulatory guidance, enforcement policies, consent orders, and other informal guidance to decipher. Moreover, the Environmental Protection Agency ("EPA") also regulates the architectural coatings industry, potentially creating conflicting obligations.³⁴ Thus, the Commission's proposed labeling requirements regarding the VOC content and emissions of architectural coatings have the potential to create the very problems that it sought to avoid by treading carefully when it released the Green Guides. WLF urges the Commission to reconsider the wisdom of regulating so specifically in an area already squarely addressed by EPA regulations. In sum, the situation strongly suggests that regulators, businesses, and consumers would all be better off using a notice-and-comment process that involves all affected stakeholders.

The FTC's Guidance and Adjudication Process in the Architectural Coatings Industry Raises Constitutional Questions. FTC's preference for using individually ne-

³² Prepared Statement of the Federal Trade Commission on Data Security: Hearing Before the Subcomm. on Commerce, Mfg., and Trade of the H. Comm. on Energy and Commerce, 112th Cong. 11 (2011) (statement of Edith Ramirez, Comm'r, Federal Trade Commission) ("[E]ffective consumer protection requires that the Commission be able to promulgate these rules in a more timely and efficient manner.").

³³ Solove & Hartzog, *The FTC and the New Common Law of Privacy*, 114 COLUMBIA L. REV. 583 (2014).

³⁴ The EPA has addressed VOC emissions from architectural coatings in a final published rule, 40 C.F.R. Part 59 Subpart D ("National Volatile Organic Compound Emission Standards for Architectural Coatings").

gotiated settlement agreements to amend and clarify broad and often very precise and specific formal guidance raises serious due process and equal protection questions.³⁵ Constitutional due process and equal protection requirements and basic administrative-law principles require adequate and fair notice of laws and regulations before agency enforcement occurs. As the D.C. Circuit has said, “Those regulated by an administrative agency are entitled to ‘know the rules by which the game will be played.’”³⁶ An agency’s reliance upon negotiated FTC settlements to provide such notice and signal agency interpretations has been seriously questioned and is currently being actively litigated.³⁷ How should businesses not under an FTC order decipher the inconsistencies of the Green Guides, Enforcement Policy, and consent orders not directly applicable to them?

Such an inscrutable approach to regulatory enforcement is not only deeply unfair to affected industry stakeholders, but it falls far short of satisfying the legal standard for fair notice. To begin with, it is widely understood that a consent decree binds only the parties to the agreement.³⁸ Such private settlements in no way constrain the FTC’s future enforcement decisions; unlike formal rulemaking, they do not even purport to lay out general enforcement principles. “Nor is a consent decree a controlling precedent for later Commission action.”³⁹ Rather, the “function of filling in the interstices of [a statute] should be performed, as much as possible, through quasi-legislative promulgation of rules to be applied in the future.”⁴⁰

Only one of the Commission’s actions—issuing and directly updating the Green Guides—involved a multi-year effort with numerous revisions that directly and specifically addressed consumer and industry input in commentary accompanying the guides when they were published in the Federal Register. To meet due process and fair notice obligations, the proposed changes to the Green Guides through the harmonization of the New Orders seem *at least* as deserving of public participation and commentary.⁴¹ Otherwise, there can be little faith that the FTC’s action is anything other than arbitrary.

As a result, the FTC seriously risks losing any judicial deference when it alters or, more generously, “discovers” new specific requirements in formal guidance that no reasonable party could have reason to know existed.⁴²

V. The Commission Should Update the Green Guides Using the Notice-and-Comment Process

Given the pragmatic and constitutional concerns with ad hoc legislation-by-consent-decree, the Commission should directly amend the Green Guides to incorporate its latest interpretations of § 5 of the FTC Act as applied to environmental marketing claims.

The FTC Should Treat the Green Guides as a Substantive Rule and Use the Notice-and-Comment Process to Update It. The FTC should enforce the Green Guides as written until it takes appropriate steps to directly amend and otherwise explain and justify the Commission’s changes. Given the strong similarities between the issuance of the Green Guides and the issuance of substantive rules under the APA, the FTC should consider how courts have viewed agency changes to substantive

³⁵The Green Guides state that certain terminology related to “free-of” claims may be tailored on a case-by-case basis. 16 C.F.R. § 260.9 (“Trace contaminant” and “background level” are imprecise terms, although allowable manufacturing “trace contaminants” may be defined according to the product area concerned. What constitutes a trace amount or background level depends on the substance at issue, and requires a case-by-case analysis.”). But mere notice that a change may occur is not fair notice of what that change will be.

³⁶*Alaska Prof'l Hunters Ass'n v. FAA*, 177 F.3d 1030, 1035 (D.C. Cir. 1999) (citations omitted).

³⁷*LabMD, Inc. v. Federal Trade Commission*, No. 16–16270 (11th Cir.), is currently pending decision before the Eleventh Circuit following oral argument. The appellant argues that the FTC did not provide fair notice of the data security standards that were allegedly violated. *See, e.g., Stegmaier & Bartnick, Physics, Russian Roulette, and Data Security: The FTC's Hidden Data-Security Requirements*, 20 GEO. MASON L. REV. 673, 719 (2013) (“Entities have not been given proper notice of what data-security practices are ‘reasonable’ and ‘adequate’” through the FTC’s use of enforcement actions rather than rulemaking).

³⁸*See, e.g., Altria Group, inc. v. Good*, 555 U.S. 70, 89 n.13 (2008) (acknowledging that a “FTC consent order is . . . only binding on the parties to the agreement”).

³⁹*Beatrice Foods, Co. v. FTC*, 540 F.2d 303, 312 (7th Cir. 1976).

⁴⁰*SEC v. Chenery Corp.*, 332 U.S. 194, 202 (1947).

⁴¹Inviting comment on this consent order is not the same as undertaking the notice-and-comment process previously used to amend the Green Guides, because the consent decree itself is non-binding precedent to everyone but the party agreeing to it, and this comment is only intended to highlight the procedural infirmity of seeking to change the law when an authoritative interpretation *already* exists.

⁴²*See* Kristine Cordier Karnezis, Annotation, *Construction and Application of “Chevron Deference” to Administrative Action by United States Supreme Court*, 3 A.L.R. FED. 2d 25, 39 (2005); 2 AM. JUR. 2D ADMINISTRATIVE LAW § 77 (2002).

rules implemented under the APA. An agency is bound by its regulations until it changes them via a process that is reasonable, non-arbitrary, and supported by the record.⁴³ To change a substantive rule issued through notice-and-comment procedures, an agency must repeat those notice-and-comment process.⁴⁴ Agencies cannot avoid the notice-and-comment process by simply couching a change as a new interpretation.⁴⁵ Of course, post-hoc explanations for changes to substantive rules that did not go through a notice-and-comment process (such as through consent orders with private parties) are especially vulnerable to attack through the courts because there is no record by which to rationalize the changes.⁴⁶

Because the Green Guides were created like a substantive rule, directly amended like a substantive rule, and enforced like a substantive rule, the FTC should continue to directly amend the Green Guides as an agency would any substantive rule under the APA—through the notice-and-comment process. The FTC describes the Green Guides as interpretive guidance, but they constitute a substantive rule because they provide a specific and definite interpretation of the FTC’s broad scope of authority under § 5 of the FTC Act, they were issued through the notice-and-comment process, and they were published in the Code of Federal Regulations. Once the FTC determined to use these processes to promulgate the Green Guides, its choice was not without consequence. Here, because the Commission has undertaken such rigorous procedures to promulgate the Green Guides, its decision to change them without resort to those same procedural safeguards seems arbitrary and capricious. Addressing these concerns would help permit the FTC to retain the clear authoritativeness of the Green Guides and likely receive the deference from courts it desires. Such a process would also afford businesses with a crucial opportunity to provide expert input into the regulatory process and receive fair notice of obligations under the law.⁴⁷

VI. Conclusion

The Commission should conform the New Orders to the previously established requirements and not otherwise amend the Green Guides without using a notice-and-comment process that takes into account the specific considerations present in the architectural coatings industry. Pending the completion of such a process, the FTC should, at least with respect to non-parties to the consent orders or other parties, hold its enforcement authority in abeyance. Rather than seeking to bootstrap the updated requirements from the New Orders immediately onto certain other busi-

⁴³*Motor Vehicle Mfrs. Ass’n v. State Farm Mut. Ins. Co.*, 463 U.S. 29, 41 (1983) (holding that the rescission or modification of a rule promulgated using the APA notice-and-comment process must not be “arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law.”); *United States v. Nixon*, 418 U.S. 683, 696 (1974) (“So long as this regulation remains in force the Executive Branch is bound by it.”); *Vitarelli v. Seaton*, 359 U.S. 535, 540 (1959) (“[T]he Secretary of the Interior] here . . . was bound by the regulations which he himself had promulgated for dealing with such cases. . . .”); *Service v. Dulles*, 354 U.S. 363, 388 (1957) (“[T]he Secretary of State] could not, so long as the Regulations remained unchanged, proceed without regard to them.”); *United States ex rel. Accardi v. Shaughnessy*, 347 U.S. 260, 267 (1954) (“As long as the regulations remain operative, the Attorney General denies himself the right to sidestep the Board or dictate its decision in any manner.”).

⁴⁴5 U.S.C. § 551(5). See e.g., *Perez v. Mortgage Bankers Assoc.*, 135 S.Ct. 1199, 1206 (2015) (citing *FCC v. Fox Television Stations, Inc.*, 556 U.S. 502, 515 (2009) (The APA mandates “that agencies use the same procedures when they amend or repeal a rule as they used to issue the rule in the first instance.”); *Nat’l Family Planning and Reprod. Health Assoc. v. Sullivan*, 979 F.2d 227, 231 (D.C. Cir. 1992) (requiring the use of notice-and-comment rulemaking to issue a “directive” significantly altering the meaning of a regulation originally issued through notice-and-comment rulemaking).

⁴⁵E.g., *Shell Offshore, Inc. v. Babbitt*, 238 F.3d 622, 629 (5th Cir. 2001) (“Interior’s new policy is a substantive rule for purposes of the APA, and Interior was required to submit their new rule for notice and comment.”); *Appalachian Power Company v. EPA*, 208 F.3d 1015, 1024 (D.C. Cir. 2000) (“It is well-established that an agency may not escape the notice-and-comment requirements. . . by labeling a major substantive legal addition to a rule a mere interpretation.”).

⁴⁶E.g., *Christopher v. SmithKline Beecham Corp.*, 567 U.S. 142, (2012) (explaining that deference is “unwarranted” when “the agency’s interpretation conflicts with a prior interpretation or when it appears that the interpretation is nothing more than a convenient litigating position or a ‘post-hoc rationalization’ advanced by an agency seeking to defend past agency action against attack”); *Motor Vehicle Mfrs. Ass’n v. State Farm Mut. Ins. Co.*, 463 U.S. 29, 42 (1983) (“The courts may not accept appellate counsel’s post hoc rationalizations for agency action.”).

⁴⁷The FTC may consider working with the EPA on studies relevant to VOC-related claims and labels. Recently, the FTC and U.S. Department of Agriculture completed a joint consumer perception study of “recycled content” and “organic” claims. FED. TRADE COMM’N, *Consumer Perception of “Recycled Content” and “Organic” Claims* (Aug. 10, 2016), https://www.ftc.gov/system/files/documents/reports/consumer-perception-recycled-content-organic-claims-joint-staff-report-federal-trade-commission/consumer_perception_of_recycled_content_and_organic_2016-08-10.pdf.

nesses in the industry, the FTC should consider using regulatory self-restraint to seek to provide the public, including consumers and other agencies whose regulations may overlap or even conflict, with an opportunity to comment upon and participate in an open and public discussion. This process will permit affected constituencies to have appropriate time and opportunity to seek clarification on the requirements without the threat of immediate fines (for those already under order) and investigation (for the remainder of the industry). This approach addresses practical considerations, constitutional due-process concerns, and competition policy concerns with some parties having more information than others about the FTC's compliance expectations for the Green Guides.

Respectfully submitted,

CORY L. ANDREWS,
RICHARD A. SAMP,
Washington Legal Foundation.

ELECTRONIC PRIVACY INFORMATION CENTER
Washington, DC, September 26, 2017

Hon. JERRY MORAN, Chairman,
Hon. RICHARD BLUMENTHAL, Ranking Member,
U.S. Senate Committee on Commerce, Science, and Transportation,
Subcommittee on Consumer Protection, Product Safety, Insurance, and Data Security,
Washington, DC.

RE: Hearing on "FTC Stakeholder Perspectives: Reform Proposals to Improve Fairness, Innovation, and Consumer Welfare"

Dear Chairman Moran and Ranking Member Blumenthal:

We write to you regarding the upcoming hearing on "FTC Stakeholder Perspectives: Reform Proposals to Improve Fairness, Innovation, and Consumer Welfare."¹ As evidenced by recent massive data breaches, data protection is perhaps the most important consumer welfare issue facing the FTC today. The FTC must do more to safeguard American consumers. The FTC's continued failure to act against the growing threats to consumer privacy and security could be catastrophic.

EPIC is a public interest research center established in 1994 to focus public attention on emerging privacy and civil liberties issues.² EPIC is a leading advocate for consumer privacy and has appeared before this Committee on several occasions.³ EPIC has fought for privacy rights for Internet users at the Federal Trade Commission for more than two decades. We filed landmark complaints about privacy violations by Uber, Microsoft, Facebook, and Google.⁴

The FTC's Current Approach is Insufficient to Protect Consumer Privacy and Security

American consumers face unprecedented privacy and security challenges. The recent data breach by consumer credit reporting agency Equifax exposed the personal information—including names, addresses, phone numbers, dates of birth, social se-

¹ *FTC Stakeholder Perspectives: Reform Proposals to Improve Fairness, Innovation, and Consumer Welfare*, 115th Cong. (2017), S. Comm. on Commerce, Science, and Trans., Subcomm. on Consumer Protection, Product Safety, Insurance, and Data Security, <https://www.commerce.senate.gov/public/index.cfm/2017/9/ftc-stakeholder-perspectives-reform-proposals-to-improve-fairness-innovation-and-consumer-welfare> (September 26, 2017).

² See EPIC, *About EPIC*, <https://epic.org/epic/about.html>.

³ See, e.g., Marc Rotenberg, EPIC Executive Director, Testimony before the U.S. Senate Committee on Commerce, Science, and Transportation, *Internet Privacy and Profiling* (June 13, 2000), <https://epic.org/privacy/internet/senate-testimony.html>; Letter from EPIC to the U.S. Senate Committee on Commerce, Science, and Transportation on Oversight of the FTC (Sept. 26, 2016), <https://epic.org/privacy/consumer/EPIC-Letter-Sen-Comm-CST-FTC-Oversight.pdf>.

⁴ See Complaint, Request for Investigation, Injunction, and Other Relief, *In the Matter of Uber Technologies, Inc.* (Jun. 22, 2015), <https://epic.org/privacy/internet/ftc/uber/Complaint.pdf>; Complaint and Request for Injunction, Request for Investigation and for Other Relief, *In the Matter of Microsoft Corporation*, (July 26, 2001), https://www.epic.org/privacy/consumer/MS_complaint.pdf; see also Complaint, Request for Investigation, Injunction, and Other Relief, *In the Matter of Facebook, Inc.*, (Dec. 17, 2009), <https://epic.org/privacy/inrefacebook/EPIC-FacebookComplaint.pdf>; Complaint, Request for Investigation, Injunction, and Other Relief, *In the Matter of Google, Inc.*, (Feb. 16, 2010), https://epic.org/privacy/ftc/googlebuzz/Google_Buzz_Complaint.pdf.

curity numbers, and driver’s license numbers—of 143 million people.⁵ This the latest in a growing number of high-profile hacks that threaten the privacy, security, and financial stability of American consumers. Far too many organizations collect, use, and disclose detailed personal information without following proper procedures for safeguarding that information. Our government must respond with comprehensive, baseline privacy protections that ensure Fair Information Practices—an internationally recognized set of informational privacy practices⁶—are applied across the Internet ecosystem.

At this time, the FTC is simply not doing enough to safeguard the personal data of American consumers. While we respect the efforts of the Commission to protect consumers, the reality is that the FTC lacks the statutory authority, the resources, and the political will to adequately protect the online privacy of American consumers.

The FTC’s privacy framework—based largely on “notice and choice”—is simply not working. Research shows that consumers rarely read privacy policies; when they do, these complex legal documents are difficult to understand. Nor can industry self-regulatory programs provide realistic privacy protections when they are not supported by enforceable legal standards.

Even when the FTC reaches a consent agreement with a privacy-violating company, the Commission rarely enforces the Consent Order terms.⁷ American consumers whose privacy has been violated by unfair or deceptive trade practices do not have a private right of action to obtain redress. Only enforceable privacy protections create meaningful safeguards, and the lack of FTC enforcement has left consumers with little recourse.

Fundamentally, the FTC is not a data protection agency. Without regulatory authority, the FTC is limited to reactive, after-the-fact enforcement actions that largely focus on whether companies honored their own privacy promises. Because the United States currently lacks comprehensive privacy legislation or an agency dedicated to privacy protection, there are very few legal constraints on business practices that impact the privacy of American consumers.

EPIC’s Recommendations

Maintaining the status quo imposes enormous costs on American consumers and businesses. Consumers face unprecedented threats of identity theft, financial fraud, and security breach.⁸ Privacy protections based on industry self-regulation and burdensome “notice and choice” policies do not provide meaningful safeguards for consumers. The FTC must issue effective guidance and use its Section 5 enforcement authority to ensure adequate protection of consumer privacy in the digital age.

Moreover, the FTC must promptly investigate business practices, pursue complaints, enforce existing Consent Orders, and modify proposed settlements to reflect public comments. The Commission’s ongoing failure to fulfill these obligations is (1) contrary to the explicit purpose of the statutory provision that allows the Commission to request comments from the public;⁹ (2) contrary to the broader purpose of the Commission to police unfair and deceptive trade practices;¹⁰ and (3) contrary to the interests of American consumers.

We urge Congress to consider the Commission’s use of Section 5 authority in the context of the greater American legal landscape. Because the U.S. lacks a comprehensive privacy law or an agency dedicated to privacy protection, there are very few legal constraints on business practices that impact the privacy of Americans. The FTC’s already modest Section 5 authority helps to deter and penalize the abuse of data. Any effort to limit the Commission’s authority—coupled with Congress’ failure to update America’s privacy laws—is a disservice to the vast majority of Americans who are increasingly concerned about their loss of privacy and want their government to do more to protect this important democratic value.

⁵ Equifax Inc., *Equifax Releases Details on Cybersecurity Incident, Announces Personnel Changes*, <https://investor.equifax.com/news-and-events/news/2017/09-15-2017-224018832> (Sept. 15, 2017).

⁶ See EPIC, *Code of Fair Information Practices*, https://www.epic.org/privacy/consumer/code_fair_info.html.

⁷ See *EPIC v. FTC*, No. 12–206 (D.C. Cir. Feb. 8, 2012).

⁸ See, e.g., FED. TRADE COMM’N, *Consumer Sentinel Network Data Book* (Feb. 2016), <https://www.ftc.gov/system/files/documents/reports/consumer-sentinel-network-data-book-january-december-2015/160229csn-2015databook.pdf>.

⁹ Commission Rules of Practice, 16 C.F.R. § 2.34 (C) (2014).

¹⁰ Federal Trade Commission Act, 15 U.S.C. § 46 (2006).

We ask that this letter be submitted into the hearing record. We look forward to working with you to improve the FTC's authority in this field and to develop rules to provide meaningful and much-needed protections for consumer privacy.

Sincerely,

MARC ROTENBERG,
EPIC President.
CAITRIONA FITZGERALD,
EPIC Policy Director.
CHRISTINE BANNAN,
EPIC Policy Fellow.

