Attachment—Additional Questions for the Record

Subcommittee on Consumer Protection and Commerce
Hearing on
"The Consumer Protection and Recovery Act: Returning Money to Defrauded Consumers."
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The Honorable Kelly Armstrong (R-ND)

1. The courts have found the Commission need not prove actual knowledge: "Congress unambiguously referred the district court to the state of mind of a hypothetical reasonable person, not the knowledge of the defendant. The standard is objective, not subjective."[1] The dishonest or fraudulent standard was met in Figgie. That case may have taken an extended time to prosecute, but doesn't it serve as an example that the Commission is capable of proceeding, and succeeding, under the dishonest and fraudulent standard?

   RESPONSE: The Commission can proceed, and succeed, under the dishonest and fraudulent standard. Indeed, the 9th Circuit's opinion should facilitate the use of Section 19. The Court held that the Commission need not establish actual knowledge that a violator knew its practices were dishonest or fraudulent, because "the issue of law is what a reasonable person would have known, not what Figgie's executive knew. The statute is unambiguous."[2] Moreover, the Court was clear that the Commission's findings were conclusive; the district court resolved both liability and damages on summary judgment motions.

   Although the Figgie case took time, additional cases are unlikely to take as long. First, since Figgie the Commission has revised its rules to speed up its administrative litigation. Second, Figgie was the first case to address the dishonest or fraudulent standard, a circumstance that inevitably provoked additional litigation. In the Telebrands case,[3] one of the few other cases under the Section 19 process, the case settled some 16 months after the Commission's Section 19 complaint in 2007. In contrast, the Section 19 portion of the Figgie litigation took 5 years to resolve.

[1] FTC v. Figgie Int'l, Inc., 994 F.2d 595, 603 (9th Cir. 1993).

[2] Id. at 603.

[3] FTC v. Telebrands Corp., 2:07-cv-3525 (D.N.J. 2008).

Moreover, most FTC cases settle, and a settlement resolving both liability and monetary relief is no more complicated or time-consuming under Section 19 than it is under Section 13(b). Prominent cases mentioned at the hearing, such as the case against Volkswagen,[4] were settlements that could have cited Section 19 as easily as they cited Section 13(b). There is no reason to think either that the outcome would have been different, or that the process would have been longer.

2. FTC v. Credit Bureau Ctr., LLC, 937 F.3d 764 (7th Cir. 2019), involved "websites [that] offered a 'free credit report and score' while obscuring a key detail in much smaller text: that applying for this 'free' information automatically enrolled customers in an unspecified $29.94 monthly 'membership' subscription."[5] "The subscription was for Brown's credit-monitoring service, but customers learned this information only when he sent them a letter after they were automatically enrolled."[6] Although the Commission proceeded under 13(b) and the "unfair or deceptive" standard in this case, the Seventh Circuit declared this a "fraudulent scheme."[7] Is there a reason the Commission could not have proven a case under the dishonest or fraudulent standard?

   RESPONSE: There is no reason to think that the FTC would have any difficulty in meeting the "dishonest or fraudulent" standard in the Credit Bureau case. In that case, the judge issued an ex parte asset freeze, an extraordinary form of relief. It is hard to imagine any case in which a district court judge is willing to freeze assets that would not involve conduct that a reasonable person would know is dishonest or fraudulent.

   The important question for a case like Credit Bureau Ctr. is procedural, not substantive. Will judges still be willing to freeze assets to preserve funds for relief under Section 19 when they will lose control of the case as it moves into administrative litigation? If not, the money will likely disappear before the FTC can make the showing that the conduct was indeed dishonest or fraudulent. In a recently published article that I coauthored, we show that Section 19 will not work against true fraudsters.[8]

3. The Commission obtained $14.7 billion, by far its largest ever monetary remedy, from Volkswagen in a 2016 settlement. The Commission alleged the company had

[4] FTC v. Volkswagen Group of America, Inc., No. 3:16-cv-1534 (N.D. Cal).

[5] FTC v. Credit Bureau Ctr., LLC, 937 F.3d 764 (7th Cir. 2019).

[6] *Id.*

[7] *Id.*

[8] J. Howard Beales, III, Benjamin M. Mundel, and Timothy J. Muris, Section 13(b) of the FTC Act at the Supreme Court: The Middle Ground, theantitrustsource, www.antitrustsource.com, December, 2020.

intentionally installed, in millions of vehicles sold in the U.S., "illegal software designed to enable the vehicle to cheat emissions tests" to allow "emissions at as much as 4,000 percent above the legal limit." If intentional falsification of a product quality, which is both required by law and also valued by environmentally sensitive consumers, does not qualify as dishonest or fraudulent conduct, what type of conduct would meet this standard?

RESPONSE: Although the precise contours of the dishonest or fraudulent standard will no doubt be subject to litigation, I can see no plausible interpretation of the standard that would fail to find Volkswagen liable. There will be difficult cases, but Volkswagen is not one of them.

4. H.R. 2668 contains a provision that "a court may not order equitable relief under this subsection with respect to any violation occurring before the period that begins on the date that is 10 years before the date on which the Commission files the suit in which such relief is sought."

    a. Is 10 years an appropriate period? Please explain.

REPONSE: Statutes of limitations can trace their roots back for centuries. They must balance two important, competing goals. One goal, favoring a long period, is to encourage resolution of all claims on their merits. A competing goal, favoring a shorter limitation, is to provide repose, to protect against surprises through the assertion of claims long after the conduct, when evidence may be stale or no longer available, and to encourage the timely filing of claims by regulatory agencies.[9] The general federal statute of limitations limits penalties to conduct in the previous 5 years. I see nothing unique about the FTC that would argue for a longer statute of limitations than what applies to other agencies. If anything, the risk of harm to consumers because the Commission fails to take timely action to address violations would argue for a shorter period.

5. The Commission's 2003 Policy Statement on Monetary Equitable Remedies in Competition Cases (commonly called the Disgorgement Policy Statement) said: "The Commission will ordinarily seek monetary disgorgement only when the violation is clear." "The Commission will assess whether a violation is 'clear' by means of an objective, not a subjective, standard, i.e., a reasonableness test. 'Naked' restraints of trade, such as price-fixing or horizontal market division, are presumptively clear cases. The list of 'clear' cases, however, goes beyond traditional per se violations."

    a. Is "clarity" the right standard in some cases?

RESPONSE: In my view, clarity is an appropriate standard in all cases of monetary relief. When legal requirements are uncertain, parties subject to those

[9] See Tyler T. Ochoa and Andrew J. Wistrich, The Puzzling Purposes of Statutes of Limitation, 28 Pacific Law Journal 453-514 (1997).

requirements may avoid conduct that would benefit consumers because it might expose them to the risk of significant monetary sanctions. As explained in my written statement, the advertising substantiation program is a prime example. Monetary liability for claims that the Commission eventually finds unsubstantiated may chill the provision of truthful information that is valuable to consumers. The dishonest or fraudulent standard in Section 19 avoids this problem for consumer protection cases. As the Commission's policy statement notes, a limitation to cases where "a reasonable party should expect that the conduct at issue would likely be found to be illegal"[10] avoids the problem in antitrust cases.

b. If so, when is it appropriate?

RESPONSE: A clarity standard would be appropriate for cases involving antitrust violations or unfair methods of competition. For matters involving unfair or deceptive practices, I believe the dishonest or fraudulent standard that already exists in the law is more appropriate, and serves the same policy purpose.

c. The Policy Statement said that deterrence "can best be served when the violator can determine in advance that its conduct would probably be considered illegal." Do you agree?

RESPONSE: Yes. Overdeterrence that chills valuable conduct is a significant risk when potential violators cannot determine with reasonable certainty whether their course of action is legal or illegal.

d. The Policy Statement also noted that "when significant consumer harm will not (for one reason or another) be redressed through a private action … , the Commission might therefore consider seeking restitution even if the conduct at issue does not otherwise meet our definition of a 'clear' violation." Is that the right standard?

RESPONSE: Yes. Commission enforcement is vital, because in many instances private remedies are inadequate or impractical to pursue. The Commission should allocate its resources to complement, not compete with, private remedies.

e. If so, how should Congress codify it to avoid duplication of remedies with other causes of action?

REPONSE: Avoiding duplication of private remedies will likely rely to a considerable extent on the agency's discretion regardless of any statutory standard. A statute, for example, might limit the Commission's monetary relief to cases in which there is no practical private remedy, but making that determination would leave much to the agency's discretion. A brighter line test might make monetary relief available only if no private class action cases have been filed, but

[10] 68 Fed. Reg. 45821 (2003).

that restriction would place a priority on the FTC acting first. Moreover, in many instances, particularly in antitrust, class actions that follow on an FTC case finding liability may provide entirely adequate monetary relief, even though the government filed first. Oversight of when the agency seeks money may be a more finely tuned way to prevent needless duplication.

6. What economic principles should guide the Commission in calculating (a) consumer redress and (b) disgorgement?

   RESPONSE: Regarding redress, there are two sources of injury to consumers from deceptive claims. First, some consumers purchase the product would not have purchased at all had they known the truth. For these consumers, the price they paid for the product is an appropriate measure of redress. In fraud cases, essentially all consumers purchase only because of the fraudulent claim, so total revenue is an appropriate redress amount. In other cases, a full refund should apply only to those who purchased because of the claim. Second, all consumers may pay a higher price for the product because they mistakenly believe it has a feature or attribute that it does not. For these consumers, the appropriate amount of redress is the increase in price attributable to the deceptive claim.

   Regarding disgorgement, the goal is to remove the profit from a violation in order to reduce the incentive to engage in such violations in the first place. The only difference is that the remedy is confined to the profits from the activity, rather than the harm to consumers. Disgorgement based on avoided compliance costs can be appropriate when damages are difficult to determine and civil penalties are not available.

7. The Bureau of Economics has published a detailed analysis of how it calculates remedies. It also frequently weighs in on settlements and cases with calculations of the likely injury and proper redress.

   a. What principles does it apply in such opinions that could guide Congress in modifying 13(b)?

   RESPONSE: Codifying an approach to calculating remedies in FTC cases is likely to prove exceedingly challenging, particularly since there has been little public or academic analysis of alternative approaches and their implications. As a general matter, however, remedies should be limited to redressing the incremental impact of the practice at issue on total revenue (or total profit in the case of disgorgement), rather than total revenue from all sales (or profits). As noted in response to question 6, total revenue is an appropriate measure in a subset of cases, most notably involving fraud.

   b. Is it important that the Commission's monetary remedies be offset by the value that a consumer receives from the product or service at issue?

RESPONSE: Consideration of offsetting value from a product or service that is subject to misrepresentations depends on the circumstances. When the misrepresented characteristic is essentially the only reason most consumers bought the product, there is no reason to consider offsetting value. In *FTC v. Bronson Partners, LLC*, 654 F. 3d 359 (2d Cir. 2011), for example, Chinese Diet Tea was promoted as a weight loss remedy, and it seems unlikely that any appreciable number of consumers purchased the product for its value as a beverage. Ignoring any possible offsetting value is therefore appropriate. In the Commission's settlement with Kellogg regarding nutritional claims for Frosted Mini Wheats and Rice Krispies,[11] however, the overwhelming majority of sales of products that had long been marketed were likely for reasons that had nothing to do with the challenged claims. Although the Commission did not obtain monetary relief in that case, any attempt to seek monetary remedies in such cases should be limited to the incremental sales attributable to the claim.

c. What methodologies are appropriate for calculating monetary remedies under the "dishonest or fraudulent" standard?

RESPONSE: The principles are the same as those discussed in response to question 6. In fraud cases, total revenues from sale of the product (net of refunds or returns) are an appropriate measure of damages. In other cases, monetary remedies should be limited to the incremental revenue or profit attributable to the violative practice.

[11] Press Release, Fed. Trade Comm'n, Order Modifying Order, Kellogg Co. (June 3, 2010) (modifying order to cover additional claims).