Federal Trade Commission

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at

The Economics of Access to Civil Justice:
Consumer Law, Mass Torts and Class Actions

George Mason University Law & Economics Center
and
Alliance of California Judges

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I. Introduction

Good evening. It is wonderful to see you here tonight and it is always a great pleasure for me to participate in a Law and Economics Center program. I would like to thank the Alliance of California Judges, the Law and Economics Center, and Henry Butler for inviting me to speak with you all tonight.

* The views stated here are my own and do not necessarily reflect the views of the Commission or other Commissioners. I am grateful to my advisor, Beth Delaney, for her invaluable assistance in preparing this speech.

The theme of tonight's event – The Economics of Access to Civil Justice – is one of particular interest to me both because it was an important part of my research agenda an academic lawyer and economist at George Mason and because it is an important aspect of the Federal Trade Commission's mission. I have been at the Commission a little over a year now and have had the opportunity to get a closer look at some of the agency's advocacy work that touches upon the topic of access to civil justice. Tonight I would like to highlight some of the work we have done under our Class Action Fairness Project; discuss some of our notable advocacy efforts aimed at reducing state barriers to entry and restrictions on competition among lawyers – which have the effect of reducing access to the civil justice system for many consumers of legal services; and finally, consider an additional area – reform of State Consumer Protection Acts – where the Commission might be able to make a useful contribution to improve access to civil justice while promoting consumer welfare.

II. Class Action Fairness Project

Under the leadership of former Chairman Tim Muris, the Commission in 2002 initiated its "Class Action Fairness Project" – a program aimed at having the Commission file amicus briefs commenting on class action settlements pending in either state or federal courts that raised consumer protection concerns. Private litigation often serves the important purpose of compensating injured consumers and deterring wrongful conduct. And class actions can be a useful vehicle in achieving these goals

efficiently and effectively. However, as many have recognized, at the time of settlement, the interests of the plaintiffs' counsel and defendants may diverge from those of the class. If class counsel and defendants' interests are too closely aligned, there is not much adversarial process left to assist the trial judge in evaluating the terms of the settlement. Accordingly, the Commission can play an important role in identifying problems and advocating for a settlement that protects consumers' interests.

As a general matter, the Commission submits an amicus brief in instances where it has an actual involvement in a related matter or where there are issues that may benefit from our particular expertise and experience. For example, the Commission may offer assistance by evaluating the relief offered by consumer redress programs; examining consumer understanding of notices; analyzing the scope and import of releases; and identifying provisions that might otherwise be detrimental to the class.

Some of our earliest amicus briefs addressed the issue of "coupon" settlements. Commentators have long been critical of coupon settlements because they are thought to be especially conducive to settlements that are not in the interests of consumers. Because the lawyers' compensation is usually based in part upon the value of the remedy to the class, lawyers argue that the coupons are worth approximately their face value despite the fact that many will not be used.[1] If successful, the lawyers will

[1] *See* Geoffrey P. Miller & Lori S. Singer, *Nonpecuniary Class Action Settlements*, 60 LAW & CONTEMP. PROBS. 97 (1997). Coupon settlements have been subject to a variety of other economic criticism. *See* A. Mitchell

obviously be rewarded; however, the costs imposed upon the defendant of the settlement will be relatively low and consumers will receive a remedy of little value.

In *Erikson v. Ameritech Corporation*, for example, the Commission opposed a settlement arguing that the proposed relief and compensation was inadequate.[2] The underlying case involved the allegation that Ameritech had failed to disclose that some consumers would incur additional costs over their monthly subscription charges when they used voicemail. The Commission, in its amicus filing, alerted the court to the fact that the settlement failed to require Ameritech to provide disclosures that would correct this deficiency. Furthermore, the Commission pointed out that the proposed compensation of one free month of speed dial service not only had little practical or economic value, but also contained a so-called "negative option" that undercut the value of the settlement: class members would be billed for the service on a monthly basis if they failed to affirmatively cancel it after the first free month.

The court subsequently rejected the settlement, leading Ameritech to propose a revised settlement that required disclosures in writing and when consumer service representatives were speaking with customers. The revised settlement also provided

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Polinsky & Daniel L. Rubinfeld, *The Deadweight Loss of Coupon Remedies for Price Overcharges*, 56(2) J. INDUS. ECON. 402 (2008); Severin Borenstein, *Settling for Coupons: Discount Contracts as Compensation and Punishment in Antitrust Lawsuits*, 39 J.L. & ECON. 379 (1996).

[2] Fed. Trade Comm'n's Memorandum of Law as Amicus Curiae, Erikson v. Ameritech Corp., No. 99 CH 18873 (Cook County Cir. Ct. Ill. County Dept. Chancery Div. June 21, 2002), *available at* http://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-amicus-curiae-brief-filed-erikson-v.ameritech-corp.no.99ch-18873/eriksonmemo.pdf.

actual consumer redress – rather than the questionable benefit of one month of free speed dialing service, consumers were given either credits to their telephone bill or cash refunds.

The Commission filed another amicus brief in *Chavez v. Netflix, Inc.*, a class action brought in California state court which involved allegations that Netflix had failed to provide "unlimited" DVD rentals and "one day delivery" of DVDs as promised in its advertising.[3] The proposed settlement offered current Netflix subscribers a free service upgrade (for example, five DVDs a month rather than three) for one month and offered former Netflix customers a month of free service. However, under the terms of the settlement, class members who opted in to the settlement would automatically be enrolled in a negative option plan whereby the services would continue after the first month, and class members would then be charged for these services each month unless they cancelled the upgrade or the new service.

The Commission has a long history of examining issues related to negative options. The FTC has challenged deceptive free trial offers used to market various goods and services, including credit monitoring services, buying club memberships, computer software, dietary supplements and Internet access services. The Commission also promulgated and enforces a trade regulation rule specific to the use of negative

[3] Fed. Trade Comm'n's Memorandum of Law as Amicus Curiae, Chavez v. Netflix, No. CGC-04-434884 (Cal. Super. Ct. San Francisco County Jan. 5, 2006), *available at* http://www.ftc.gov/sites/default/files/documents/amicus_briefs/chavez-v.netflix-inc./netflixamicusbrief.pdf.

option plans.[4] As a general matter, these types of offers may be valuable to consumers because they offer a free trial offer or merchandise as well as the added convenience of uninterrupted service. For example, a cable company may offer a free month of HBO service upon the condition that after one month the extra service will continue and be billed to the consumer unless the consumer cancels within a certain amount of time. For some consumers, the negative option adds value – they can try a new service and don't have to do anything to continue the service on an uninterrupted basis if they are enjoying it. Conversely, some consumers who don't wish to continue and pay for the service must take action to cancel. The negative option imposes costs upon the consumer to cancel the service. While negative options have the potential to increase consumer welfare if their terms are properly disclosed, in the *Netflix* case, the Commission was concerned that the existence of the negative option plan itself, as well as its terms, were not adequately disclosed to the class members.[5]

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[4] Use of Prenotification Negative Option Plans Rule, 16 C.F.R. § 425 (2013).

[5] Recently, the Commission has engaged in challenging "failures to disclose" in another area that fits squarely within access to civil justice -- overbroad release language in class action settlements. In Vassalle v. Midland Funding, LLC, No. 3:11-cv-00096 (N.D. Ohio 2011), a consolidated class action consisting of an estimated 1.4 million consumers and certified solely for settlement purposes, focused on allegations that Midland – a debt buyer – had filed form affidavits in debt collection cases in which the affiant falsely attested to having personal knowledge of the challenged debt. Under the proposed settlement, in exchange for a *de minimis* payment of $10, class members who did not opt out would release Midland and its agents from <u>all</u> claims relating to their use of affidavits in debt collection lawsuits. The Commission identified concerns with the apparent breadth of the release -- noting that not only would class members lose their rights to bring affirmative claims relating to the false affidavits under the Fair Debt Collection Practice Act and analogous state laws, but also might be precluded from using the affidavits in other pending lawsuits or challenges to improperly obtained judgments. Arguably, the release also was broad enough to cover any type of affidavit, such as an affidavit of service.

Economic analysis plays a critical role in understanding the consequences of negative option plans – providing a lens through which to evaluate the potential benefits to consumers on the one hand against the losses imposed upon consumers when the negative option is inadequately disclosed. In *Netflix*, for example, the Commission's analysis recognized that a class member's willingness to accept the settlement benefit would depend on a weighing of the benefit received against the cost incurred absent a timely cancellation and the amount of time or effort needed to cancel. The Commission emphasized that only with the clear disclosure of cost and cancellation information could such an analysis occur.

The Commission also analyzed the actual monetary value of the benefits offered by the *Netflix* settlement – ranging from $3 for current subscribers to $17.99 for former subscribers. The Commission concluded that acceptance of the negative option terms was fairly unattractive and might lead many class members – the very individuals that the class action litigation was supposed to benefit – to forgo compensation altogether.

The Commission has also used empirical analysis of coupon redemption rates to demonstrate their inadequacy.[6] In *Schneidner v. CitiMortgage, Inc.*, the defendants allegedly made undisclosed payments to mortgage brokers when the brokers induced consumers to agree to above-market-rate mortgage loans, thereby violating the Real

[6] Memorandum of Fed. Trade Comm'n as Amicus Curiae Regarding the Proposed Class Action Coupon Settlement, Schneider v. Citicorp Mortgage, Inc., CV 97-837 (NG)(CLP) (E.D. N.Y. Mar. 17, 2004), *available at* http://www.ftc.gov/sites/default/files/documents/amicus_briefs/allen-and-sharon-schneider-v.citicorp-mortgage-inc.and-citicorp/040317citicorpmemorandum.pdf.

Estate Settlement Procedures Act ("RESPA"). The proposed settlement offered class members a nontransferable coupon worth $100 for each loan that they had obtained during the class period.

The coupons offered by the settlement would reduce by $100 the cost of obtaining a new first mortgage from CitiMortgage within two years of the approval of the final settlement. In objecting to the coupon, the Commission recognized the face value of the coupon did not reflect its real economic value because it couldn't be converted to cash, would expire in two years, had limited transferability, and could only be used for a first mortgage or refinance, something most class members were unlikely to do again within the following two years. The coupon also could not be used in conjunction with any other offers. For example, CitiMortgage was at the time of settlement also offering a $500 closing credit for consumers using an online application – a much more attractive discount than the $100 coupon offered to the class members. The FTC also analyzed coupon redemption rates in other class action settlements as evidence that redemption rates for consumer class action settlements were generally quite low, and accordingly, should be taken into account when valuing the worth of the settlement to consumers. The brief provided specific redemption rates for settlements involving other consumer goods and services, highlighting the discrepancy between

purported settlement amounts and actual payouts.[7] The FTC also examined the statistical likelihood that any significant portion of the class would be again purchasing or refinancing within the following 24 months, and proposed an alternative of a fixed payment to consumers and noted, that in the event the court did approve the proposed settlement, that it require CitiMortgage counsel to submit detailed information about the number and percentage of coupons redeemed in order to assist courts, legislators, government agencies and legal scholars in assessing the efficacy of non-pecuniary coupon settlements.

III. The FTC's Competition Advocacy Efforts and Access to Civil Justice

I would now like to turn to another facet of the Commission's agenda that touches upon access to civil justice and the legal system – our competition advocacy efforts. This program is spearheaded by our Office of Policy & Planning, which coordinates closely with the Bureaus of Competition, Consumer Protection and Economics to inform state and federal entities, the judiciary, as well as trade groups such as bar associations, on the potential competitive impact of proposed rules and regulations. This is another FTC program that was re-invigorated under the leadership of former Chairman Muris and Chairman Deborah Majoras, and the supervision of

[7] FTC staff also cited to a RAND study that urged judges to apply heightened scrutiny when coupons comprise a substantial portion of the settlement value and to require estimates of the rate of coupon redemption. *See* DEBORAH R. HENSLER, ET AL., CLASS ACTION DILEMMAS: PURSUING PUBLIC GOALS FOR PRIVATE GAIN 32 (1999).

Commissioner Ohlhausen, in her previous capacity as Director of OPP, and my George Mason colleague Todd Zywicki. I want to focus tonight primarily upon the agency's efforts to inform legislators, judges, and regulators about the economic consequences of regulations relating to attorney advertising and the unauthorized practice of law.

A. Legal Advertising

The Commission's advocacy in this area is grounded on the economic foundation that advertising is a form of competition and thus "performs an indispensable role in the allocation of resources in a free enterprise system" by allowing consumers to compare the price and quality of services offered by competitors.[8] The Commission has long held the view that while false or misleading advertising by lawyers should be prohibited, any restriction on advertising needs to be narrowly tailored to prevent deceptive claims while not impeding the flow of truthful information.

Accordingly, the blanket prohibition of the participation of lawyers in legal rating programs has been one area where the Commission has offered advice to regulators. In 2006, the Committee on Advertising Appointed by the Supreme Court of New Jersey issued an opinion prohibiting attorneys from participating in the "Super Lawyers" and "Best Lawyers in America" rating programs. The Committee based its opinion on its interpretation of the language of New Jersey's Rules of Professional Conduct, which defined as misleading a communication that "compares the lawyer's

[8] Bates v. Ariz. State Bar, 433 U.S. 350, 364 (1977).

service with other lawyers' services" or "is likely to create an unjustified expectation about the results the lawyer can achieve."[9] The Opinion noted that the simplistic use of "Best Lawyer" and "Super Lawyer" as a "media-generated sound bite title clearly has the capacity to materially mislead the public."[10]

On appeal to the Supreme Court of New Jersey, the Commission filed an amicus brief in support of vacating the Opinion, and used the opportunity to explain the competitive benefits of allowing the free flow of truthful and non-misleading information to consumers.[11] The amicus brief pointed out that in an earlier decision the Court itself had recognized that consumers of legal services benefit from information about the legal system that can help them choose a lawyer, and that "attorney advertising is one of the best ways to foster price competition."[12] The brief further acknowledged the harmony between competition principles and the First Amendment's commercial speech doctrine, both of which encourage the flow of commercial information and call for restrictions to be carefully tailored.

The Commission also set forth empirical evidence that demonstrated that restrictions on advertising in professions – including the legal profession – lead to

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[9] Opinion 39, *appended to* Brief of the Fed. Trade Comm'n as Amicus Curiae, In re Petition for Review of Committee on Attorney Advertising (N.J. Sup. Ct. May 8, 2007), *available at* http://www.ftc.gov/sites/default/files/documents/amicus_briefs/re-petition-review-committee-attorney-advertising-opinion-39/v070003opinion39.pdf.

[10] *Id*.

[11] FTC Brief, *supra* note 9.

[12] *Id*. at 5, *citing* In the Matter of Felmeister & Issacs, 104 N.J. 515, 523-24 (1986).

higher prices and had either a negative or no effect on quality.[13] The Commission highlighted the fact that an FTC Staff Report – cited by the court in the same decision mentioned above -- had studied specifically the effects of different commercial speech restrictions on attorneys and had concluded that "there appears to be a continuous relationship between prices and regulations, with the lowest prices associated with the fewest restrictions."[14] The Commission believed that there was no evidence that the comparative advertising at issue had or would harm consumers,[15] but also encouraged the Court – if it did become aware of such evidence -- to instead consider carefully tailoring the restrictions as an alternative to the prohibition.

The Commission has also challenged as unnecessarily restricting truthful speech prohibitions against certain selected forms of advertising such as actor portrayals; depictions and similar dramatic techniques; endorsements and testimonials; and

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[13] FTC Brief, *supra* note 9, at 8 and n.15 *citing, inter alia*, Timothy J. Muris, *California Dental Association v. Federal Trade Commission: The Revenge of Footnote 17*, 8 SUP. CT. ECON. REV. 265, 293-304 (2000); Timothy J. Muris & Fred S. McChesney, *Advertising and the Price and Quality of Legal Services: The Case for Legal Clinics*, 1 AMERICAN BAR FOUND. RES. J. 179, 184 (1979); Frank H. Stephen & James H. Love, *Regulation of the Legal Professions*, 5860 ENCYCLOPEDIA OF L. & ECON. 987, 997 (1999).

[14] FTC Brief, *supra* note 9, at 8, *citing* William W. Jacobs, Brenda W. Doubrava, Robert P. Weaver, Douglas O. Stewart & Eric L. Prahl, *Improving Customer Access to Legal Services: The Case for Removing Restrictions on Truthful Advertising*, FTC Staff Report, 126-7 (1984).

[15] Rather, the Commission pointed to a study conducted in the United Kingdom that indicated that professional quality marks clearly aided consumer decision-making; quality marks based on objective testing resulted in attorneys seeking to improve the quality of their services (thereby promoting competition); and consumers benefitted most when advertisements contained information about an attorney's quality, especially when coupled with pricing terms. *See* Department of Constitutional Affairs, United Kingdom, Quality in the Legal Service Industry: A Scoping Study (Aug. 2005), *available at* http://www.dca.gov.uk/pubs/reports/legalservicesmarketstudy.pdf.

advertisements that look like legal pleadings.[16] As with the amicus brief I just discussed, Commission staff advised these regulatory bodies that although these broad provisions might be based on a concern that such advertising could mislead consumers about the results lawyers are likely to achieve, these concerns would be better addressed through the adoption of advertising restrictions that are narrowly tailored to prevent deceptive claims. Similarly, in a letter to the New York State Unified Court System, FTC staff articulated the various mechanisms through which advertising might enhance competition and thus benefit consumers. For example, dramatization may be an effective way of reaching consumers who do not know how legal terminology corresponds to their experiences and problems. Notably, when New York promulgated revised rules, it incorporated nearly all of FTC staff's recommendations.

Online attorney matching services is another area of interest to the Commission. In letters to courts and bar associations in Indiana, New York and Texas, Commission staff has pointed out that online legal matching services are a valuable option for consumers – likely to reduce their costs for finding legal representation and having the

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[16] *See, e.g.*, Letter from Fed. Trade Comm'n Staff to the Supreme Court of Tenn. (Jan. 24, 2013), *available at* http://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-staff-letter-supreme-court-tennessee-concerning-proposed-amendments-tennessee-rules-professional/130125tennesseadvertisingletter.pdf; Letter from Fed. Trade Comm'n Staff to the Rules of Professional Conduct Committee, La. State Bar Association (Mar. 14, 2007), *available at* http://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-staff-comment-louisiana-state-bar-association-concerning-proposed-rules-lawyer-advertising-and/v070001.pdf; Letter from Fed. Trade Comm'n Staff to the Office of Court Administration, Supreme Court of N.Y. (Sept. 14, 2006), *available at* http://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-staff-comment-office-court-administration-new-york-state-unified-court-system-concerning/v060020-image.pdf.

potential to increase competition among legal service providers.[17] Indeed, online platforms and matching services are a growing part of the modern economy across a broad variety of goods and services. Efficiently matching buyers to sellers brings intuitively obvious economic benefits. For example, studies show that consumers using online services that matched them with car dealers were able to pay approximately 2% less for the same car than those that did not use the service. The consumers likely to pay the highest prices – those with poor negotiating skills, for example – are also the most likely to use these matching services. In the absence of any evidence that these online matching services had harmed consumers, staff cautioned against these prohibitions.

The unifying economic theme of both restrictions on lawyer advertising and restrictions on the use of online attorney matching services is that both are well understood to restrict competition, increase prices, reduce output, and therefore harm consumers. The examples also have in common that the anticompetitive restrictions are most likely to harm the consumers most sensitive to price and thus, their elimination is

[17] *See* Letter from Fed. Trade Comm'n Staff to Lilia G. Judson, Ind. Supreme Court (May 11, 2007), *available at* http://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-staff-comment-ms.lilia-g.judson-executive-director-indiana-supreme-court-concerning-proposed-rules-attorney-advertising/v070010.pdf; Letter from Fed. Trade Comm'n Staff to the Office of Court Administration, Supreme Court of New York (Sept. 14, 2006), *available at* http://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-staff-comment-office-court-administration-new-york-state-unified-court-system-concerning/v060020-image.pdf; Letter from Fed. Trade Comm'n Staff to Mr. W. John Glancy, Professional Ethics Committee for the State Bar of Tex. (May 26, 2006), *available at* http://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-staff-comment-professional-ethics-committee-state-bar-texas-concerning-online-attorney-matching/v060017commentsonarequestforanethicsopinionimage.pdf.

highly likely to increase consumer access to legal services and access to the civil justice system.

B. Unauthorized Practice of Law

The Commission has also been active in advocating for maintaining and increasing competition between attorneys and lay providers for a variety of services in an effort to give consumers access to a broader range of service options and lower prices.[18] The Commission's advocacy efforts are premised upon the Commission's long-standing position that non-lawyers should be permitted to compete with lawyers in areas where no specialized legal knowledge or training is demonstrably necessary to protect the interests of consumers and no attorney-client relationship is present. Indeed, there is ample empirical evidence that suggests that lay people competently perform many of the services that might be limited to lawyers under some proposed state restrictions on the scope of authorized practice.[19] Empirical studies also show that

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[18] Most frequently, the FTC has advocated in the context of regulations that would impact whether non-lawyers should be able to provide real estate settlement services. *See, e.g.*, Fed. Trade Comm'n and Dep't of Justice Comment to the Hon. Helene E. Weinstein, N.Y. State Assembly (Apr. 27, 2007), *available at* http://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-and-department-justice-comment-hon.helene-e.weinstein-concerning-new-york.b.a01837-establish-certain-real-estate-services-may-be-provided-only-attorneys/v070004.pdf.

[19] *See, e.g.*, Joyce Palomar, *The War Between Attorneys and Lay Conveyancers – Empirical Evidence Says "Cease Fire!"*, 31 CONN. L. REV. 423, 520 (1999) ("the evidence does not substantiate the claim that the public bears a sufficient risk from lay provision of real estate settlement services to warrant blanket prohibition of those services under the auspices of preventing the unauthorized practice of law"); HERBERT M. KRITZER, LEGAL ADVOCACY: LAWYERS AND NONLAWYERS AT WORK 50-51(1998) (finding that there were no clear differences between the success of lawyers and agents in unemployment compensation appeals before the Wisconsin Labor and Industry Review Commission).

consumers have faced little harm from non-lawyer competition in many areas, and that lay specialists in the areas of bankruptcy and administrative agency hearing representation perform as well or better than lawyers.[20]

In a joint letter the Commission and the Department of Justice commented on the Hawaii State Bar Association's proposal to create a new rule to define the practice of law.[21] The comment identified the potential problems with unduly restricting competition between lawyers and non-lawyers and highlighted the evidence discussed above. The comment also pointed to empirical evidence illustrating that in communities where there was competition between lawyers and non-lawyers to close real estate transactions, consumers using lawyers paid less for those services than consumers in communities where lay closings were not common.

As with attorney advertising and access to online matching services, Commission advocacy in this area stands upon the long-accepted economic foundation that it is competition that leads to the best outcomes for consumers in terms of prices, quality, and variety of goods and services. Some restrictions upon competition from non-lawyers have the obvious and predictable effect of increased prices and reducing the choices available to consumers in the legal services market. The Commission's

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[20] Deborah Rhode, *Access to Justice: Connecting Principles to Practice*, 17 GEO. J. LEGAL ETHICS 369, 407-08 (2004).

[21] Fed. Trade Comm'n and Dep't of Justice Comment before the Supreme Court of Haw. (Jan. 25, 2008), *available at* http://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-and-department-justice-comment-supreme-court-hawaii-concerning-proposed-definition-practice-law/v080004letter.pdf.

competition advocacy efforts aiming to increase healthy competition in the legal services market coincide nicely with the aim of increasing access to civil justice by discouraging states from adopting rules that would increase the cost of that access to some consumers and deprive others of it altogether.

III. A Potential Target for Future FTC Advocacy: State Consumer Protection Acts

In thinking about additional ways in which the Commission might add value in its advocacy efforts, one item that comes to mind is the opportunity to offer guidance in the area of state consumer protection acts ("CPAs").

By way of background, every state as well as the District of Columbia has some sort of consumer protection regulatory regime, most of which can be categorized in one of two ways: either states have adopted the "Uniform Deceptive Trade Practices Act" or they have enacted statutes modeled after Section 5 of the FTC Act -- the so-called "little FTC Acts."[22] One would imagine that if a state legislature had modeled its statutory regime after the FTC's statute – often copying its exact language – such a legislature would have intended that Commission and federal court interpretations of Section 5(a) of the FTC Act should help guide the state in enforcing its own statute. Well, you be would correct: indeed, states that use Section 5 as the template for their consumer protection law commonly include a provision that explicitly makes that

[22] ABA SECTION OF ANTITRUST LAW, CONSUMER PROTECTION LAW DEVELOPMENTS 375 (2009).

intention clear, or they have a judicial ruling to the same effect.[23] As some have noted, it was "understood that the federal government, through the FTC, would continue to have the primary policymaking role in determining unfair and deceptive practices."[24]

Despite this intention, and as many legal scholars and commentators have recognized, it is now generally understood that state CPAs have evolved inconsistently – often widely deviating from FTC and federal court precedent. While the deviation of state CPAs from the FTC standard was generally perceived, the magnitude of this departure had not been studied. A few years ago, Butler and I tried to answer the question of whether and to what extent little FTC Acts are employed in a manner that is similar or different than the FTC Act. We put together a "shadow Commission," comprised of a bipartisan group of consumer protection experts with FTC experience, and after providing them with excerpts of a range of actual FTC and state consumer protection cases, we had them evaluate the merits of the claims to determine whether they would constitute legally enforceable action under FTC precedent. Under this

[23] *Id*. at 378 (noting that state consumer protection statutes "commonly include a provision along the lines of, '[i]t is the intent of the legislature that in construing this Act, the courts will be guided by the interpretations given by the Federal Trade Commission and the federal courts to Section 5(a)(1) of the Federal Trade Commission Act.'").

[24] Victor E. Schwartz, Cary Silverman & Christopher E. Appel, *That's Unfair!*, 47 WASHBURN L.J. 93, 99 (2007).

construct, 78% of a sample of actual state CPA claims would not satisfy the FTC standard.[25]

Furthermore, most "little FTC Act" states continue to determine the scope of "unfair" practices using a standard that has been formally abandoned by the FTC.[26] Even though the Commission adopted a Policy Statement on Unfairness in 1980, which was subsequently codified by Congress in 1994, most states use the outdated, "Cigarette Rule" standard for unfairness.[27] This older, unbounded standard gives more weight to vague and unspecified public policy considerations, opines on whether practices are "immoral, unethical, oppressive, or unscrupulous," and uses a substantial injury prong that is devoid of economic analysis – that is, it does not consider whether the injury is "outweighed by countervailing benefits to consumers or competition."

The Commission has a significant history with this unbounded unfairness standard. At the Commission, application of the earlier unfairness standard resulted in "a series of rulemakings relying upon broad, newly found theories of unfairness that often had no empirical basis, could be based entirely upon the individual Commissioner's personal values, and did not have to consider the ultimate costs to

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[25] Henry N. Butler & Joshua D. Wright, *Are State Consumer Protection Acts Really Little-FTC Acts*?, 63 FLA. L. REV. 163, 187 (2011).

[26] CONSUMER PROTECTION LAW DEVELOPMENTS, *supra* note 22, at 378.

[27] Set forth in Sperry v. Hutchinson, Co., 405 U.S. 233, 244 n.5 (1972), the standard includes an examination of "whether the practice, without necessarily having been previously considered unlawful, offends public policy," whether the practice is "immoral, unethical, oppressive, or unscrupulous," or "whether it causes substantial injury to consumers (or competitors or other businessmen)."

consumers of foregoing their ability to choose freely in the marketplace."[28] As others have pointed out, untethered from a rigorous cost-benefit analysis, the unfairness standard fails to "reflect the underlying philosophy that [the] ultimate objective of consumer protection is consumer welfare, and that the role of consumer protection laws is to supplement market forces, rather than to entirely displace them."[29]

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.[30] As a former Bureau Director and economist Howard Beales 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."[31] It is also well established that one

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[28] 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 II.A (May 2003), *available at* http://www.ftc.gov/public-statements/2003/05/ftcs-use-unfairness-authority-its-rise-fall-and-resurrection.

[29] Henry N. Butler & Jason S. Johnston, *Reforming State Consumer Protection Liability: An Economic Approach*, 2010 COLUM. BUS. L. REV. 1, 10 (2010).

[30] Int'l Harvester Co., 104 F.T.C. 949, 1070 (1984).

[31] Beales, *supra* note 28, § III.

of the primary benefits of performing a cost-benefit analysis is to ensure that government action does more good than harm.[32]

This leads me to the question of whether, in certain circumstances, it would be beneficial for the Commission to play a more fulsome role in sharing its economics expertise. In particular, in light of the fact that many states continue to utilize a version of the unfairness test that does not incorporate a cost-benefit analysis, and in light of empirical analysis suggesting that these different consumer protection standards result in state CPAs reaching conduct that may not harm consumers, I think it would be worthwhile for the FTC to advocate for a more principled approach in order to maximize consumer welfare.

FTC advocacy aimed at state competition and consumer protection laws is a common endeavor for the Commission when grounded in economic theory and empirical evidence. In other contexts -- for example, when examining state antitrust legislation prohibiting predatory pricing, the Commission has repeatedly submitted comment letters advocating that, to the extent that state law governing competition is weaker than the federal antitrust standard, it is likely to harm competition and

[32] Int'l Harvester, 104 F.T.C. at 1070. *See also*, Dissenting Statement of Commissioner Joshua D. Wright, In the Matter of Apple, Inc., FTC File No. 1123108 at 14 (Jan. 15, 2014), *available at* http://www.ftc.gov/sites/default/files/documents/public_statements/dissenting-statement-commissioner-joshua-d.wright/140115applestatementwright.pdf ("To justify a finding of unfairness, the Commission must demonstrate the allegedly unlawful conduct results in net consumer injury.").

consumers.[33] The gap between FTC and state CPA interpretation of the scope of actionable unfairness, and perhaps even deception, seems to justify precisely such an approach here as well.[34]

IV. Conclusion

These three examples of Federal Trade Commission enforcement and advocacy efforts – the Class Action Fairness Project, state laws insulating attorneys from competition from attorneys and non-attorneys, and current interpretations of state CPAs that deviate significantly from federal standards – are based firmly upon the belief that competition is critical to improving access to civil justice. But perhaps more importantly, and certainly an appropriate note to close on this evening for this conference, is that each of these efforts demonstrates firmly the important role that economic analysis can play in developing a coherent approach to access to civil justice that is in the best interests of consumers.

Thank you for your time.

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[33] Letter from Fed. Trade Comm'n Staff to Rep. Shirley Krug, Wis. State Assembly (Oct. 15, 2003), *available at* http://www.lb7.uscourts.gov/documents/09-1883.pdf; Letter from Fed. Trade Comm'n Staff to the Hon. Robert F. McDonnell, House of Delegates, Commonwealth of Va. (Feb. 15, 2002), *available at* http://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-staff-comment-honorable-robert-f.mcdonnell-concerning-virginia-s.b.458-prohibit-below-cost-retail-sale-motor-fuel/v020011.pdf.

[34] Indeed, some commentators in have argued that even without a harmonization provision, in some circumstances the state should still look to Section 5 for guidance. *See* Matthew W. Sawchak & Kip D. Nelson, *Defining Unfairness In "Unfair Trade Practices*," 90 N.C. L. REV. 2033 (2012) (arguing that "reasonably avoided" language should be added to the North Carolina statute).