



Federal Trade Commission

THE FEDERAL TRADE COMMISSION
AND
CONSUMER PROTECTION
IN
THE UNITED STATES OF AMERICA

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COMMISSIONER

FEDERAL TRADE COMMISSION

before the
THIRD INTERNATIONAL CONFERENCE ON CONSUMER LAW
Rio Grande do Sol, Brazil

Wednesday, March 11, 1992

The views expressed are those of the Commissioner and do not necessarily reflect those of the Federal Trade Commission or the other Commissioners.

REMARKS OF
COMMISSIONER MARY L. AZCUENAGA
BEFORE THE
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Thank you. I am delighted to be here today in these beautiful surroundings and to have this opportunity to speak to you about consumer protection in the United States. Before continuing, however, I must tell you that I am one of five members of the Federal Trade Commission, and the views I will express here will be my own and are not necessarily those of the Commission or any of the other commissioners.

My subject today, "consumer protection," is a concept that is at the base of a truly competitive market: stated more broadly, in the United States, we tend to believe that a competitive or free market will thrive in direct proportion to consumers' ability to inform themselves about the relative merits of various purchasing alternatives and consumers' ability to choose freely among those alternatives to buy the products and services best suited to their needs.

In an ideal world, those offering goods and services would advertise and market them in ways that would permit consumers to evaluate what is being offered and to make educated purchasing decisions. Unfortunately, that is not always what happens. When participants in the market fail to inform consumers truthfully and nondeceptively about products and services, consumers cannot protect themselves from injury in the form of higher prices or

inferior goods and services. It is the prevention of this injury that our federal law seeks to address.

I will confine my remarks today to Section 5 of the FTC Act,¹ which is the primary law that the Federal Trade Commission enforces. Many states, however, have statutes, known as "little FTC Acts," that are similar in many respects to the federal law. I see that Attorney General Burson of the State of Tennessee will be addressing this conference tomorrow, and he is better qualified than I to describe the workings of state laws. Suffice it to say that many of the little FTC Acts specify that state courts should give deference in their interpretation of state law to the decisions and policies of the Federal Trade Commission.

Consumer protection law in the United States, therefore, consists of a web of state laws that are limited in applicability to their respective states and a federal statute with national application that yields interpretations and decisions from which the state courts can, and often do, take guidance. In addition, the federal and state authorities often cooperate in their enforcement efforts, making those efforts more economical and effective.

Section 5 of the FTC Act

Section 5 of the FTC Act, although not the only federal

¹ 15 U.S.C. § 41.

consumer protection law,² is perhaps the most widely applicable. It makes unlawful, among other things, unfair or deceptive acts or practices.³ The Act gives the Federal Trade Commission broad enforcement powers including authority to issue complaints and, after trial on the record, to issue cease and desist orders. It gives the Commission authority to issue regulations of general applicability that may be enforced through the courts with monetary penalties and the authority to issue its own interpretive guidelines and policy statements to guide the public and encourage voluntary compliance with the law.

Specifically, Section 5 empowers the Commission to investigate possible unfair or deceptive conduct. If warranted, the Commission may issue an administrative complaint against the person or company involved. The matter then is assigned to an administrative law judge who conducts a trial and issues an decision that may be appealed to the Commission. The Commission then decides the case, and if it concludes that the respondent has violated the law, it may issue a cease and desist order to halt the wrongdoing and prevent its recurrence. This order may

² See e.g. the Consumer Products Safety Act, 15 U.S.C. § 2051; the Federal Food, Drug and Cosmetics Act, 21 U.S.C. § 301; the Clean Air Act, 42 U.S.C. § 7401; and numerous particularized statutes administered by the FTC such as the Comprehensive Smokeless Tobacco Education Act, 15 U.S.C. § 4401; the Wool Products Labeling Act, 15 U.S.C. § 68; the Fur Products Labeling Act, 15 U.S.C. § 69; and the Textile Fiber Products Identification Act, 15 U.S.C. § 70.

³ Section 5 also makes unlawful unfair methods of competition. Under this antitrust authority, the Commission acts to prevent anticompetitive business practices -- another form of "consumer protection."

be appealed to the federal courts. Once an order is final, violations may be punished by substantial penalties ordered by a federal court judge.⁴

In some cases, especially those involving fraud, the Commission also may bring suit directly in federal court. In such actions, the judge may issue an order for injunctive and monetary relief, including consumer redress or disgorgement to the United States Treasury of illegally earned profits.

Sometimes, the Commission issues rules of general applicability known as Trade Regulation Rules that define unfair or deceptive practices for an entire industry. These Rules have the force and effect of a law as if enacted by the Congress. If a party is found by a court to have violated any of these Rules, it may be required to pay civil penalties at the rate of \$10,000 per violation. Because each day of unlawful conduct can count as a violation, these penalties can be sizeable. For example, the Commission recently obtained a civil penalty of \$900,000 against a company and its principals for violations of the Commission's

⁴ The Commission does not act on behalf of individual consumers who have, or believe they have, sustained injury from unfair or deceptive marketing practices. Instead, the Commission encourages consumer complaints, which it uses to focus its investigatory and enforcement efforts and to help identify classes of consumers who may have been harmed by unscrupulous marketers and who may be entitled to redress if the marketers' liability for unlawful conduct under Section 5 is established.

Trade Regulation Rule governing mail order sales.⁵ In addition to issuing the Mail Order Rule, the Commission has exercised its rulemaking authority to issue rules requiring disclosures of cost and other information by funeral directors, used car dealers and those selling franchises or business opportunities, to name a few.

In addition, the Commission can issue "guides," or interpretative rules, that advise the public how the FTC interprets the statutes it enforces. Commission guides may apply to a specific industry -- such as guides for the jewelry industry -- or they may apply to commercial activity generally -- such as guides against deceptive pricing or endorsement and testimonial advertising guides.⁶

Because guides are merely interpretative rules, they are not binding like Trade Regulation Rules. Conduct inconsistent with such guides does not trigger a civil penalty. Nevertheless, they help parties know what they must do to avoid action by the Commission.

For example, the Commission now is considering whether it should issue guides governing environmental advertising to respond to a growing number of claims about the environmental

⁵ Philip Goutell, FTC File No. 832 3014, Civ. No. 85 Civ. 130 (TPG) (Apr. 12, 1988) and Phillipe La France, Ltd., FTC File No. 832 3014, Civ. No. 85 Civ. 130 (TPG) (S.D. N.Y. Aug. 13, 1987).

⁶ See, e.g., Guides for the Jewelry Industry, 16 C.F.R. Part 23 (1991); Guides Against Deceptive Pricing, 16 C.F.R. Part 233 (1991); Guides Concerning the Use of Endorsements and Testimonials in Advertising, 16 C.F.R. Part 255 (1991).

benefits of products as sellers have responded to consumer interest in purchasing products that will not damage the environment. Unfortunately, some advertisers have used deceptive environmental claims to sell their products. So far, the Commission has responded to deceptive environmental claims on a case-by-case basis.⁷

Some groups have asked the Commission to issue guidelines. They argue that even non-binding environmental guidelines will help provide uniform standards that are needed to eliminate confusion about what various terms mean. They suggest that one uniform federal standard is better than state standards that are different one from another. Others question the value of guidelines. Guidelines are not binding rules, and there is no penalty for violating a guideline. The Commission would still have to enforce them on a case-by-case basis. The arguments for

⁷ Over the past year, the Commission has accepted six consent agreements resolving allegations that these firms made false or unsubstantiated environmental claims about their products. A consent order is for settlement purposes only and does not constitute an admission of a law violation.

Three of these consents resolved allegations that the companies made false and unsubstantiated claims that their products would not harm the earth's ozone layer. Jerome Russell Cosmetics, Inc. et al., C-3341 (Aug. 21, 1991); Zipatone, Inc. et al., C-3336 (July 9, 1991); Tech Spray, Inc. et al., File No. 902 3309 (Consent Accepted for Public Comment Jan. 2, 1992). The other three consents settled charges that the companies made deceptive claims about their products' biodegradability. First Brand Corporation, C-3358 (Jan. 30, 1992); RMED Corp., File No. 902 3112 (Consent Accepted for Public Comment Feb. 19, 1992); American Enviro Products, Inc., File No. 902 3110 (Consent Accepted for Public Comment Aug. 30, 1991). In addition to these cases, Commission staff is conducting a number of other investigations.

and against guides are much more complicated than my brief explanation. As you can see from the example of environmental advertisements, the Commission has a range of options for addressing claims. It can bring individual cases, issue binding Trade Regulation Rules, or publish informal guides.

LEGAL STANDARDS UNDER SECTION 5

The Commission seeks to ensure maximum compliance with the law, while avoiding unduly invasive and costly regulation of the market. Good policy designed to empower consumers to make educated purchasing choices without unduly burdening those who offer products and services also makes good policy for encouraging competition and maintaining a free market economy.

Let me turn now to the three concepts underlying the Commission's authority: deception, advertising substantiation and unfairness.

Deception

The Commission will find an act or practice "deceptive" if there is a representation, omission or practice that is likely to mislead consumers acting reasonably under the circumstances, and if the representation, omission or practice is material -- that is, likely to affect a consumer's decision about a product or service.⁸ This is a long definition, and I will address each part in turn. For ease of explanation, I will speak today in

⁸ Policy Statement on Deception, Letter of Oct. 14, 1983, from the Commission to The Honorable John D. Dingell, Chairman, Committee on Energy and Commerce, U. S. House of Representatives, reprinted in Appendix, Cliffdale Associates, Inc., 103 F.T.C. 110, 174-83 (1984).

terms of advertising claims, although marketing practices other than advertising may be deceptive as well.

1. Likely To Mislead

First, we decide whether a claim is likely to mislead. The Commission need not find actual deception in order to take action but may act to prevent or halt claims that have the potential to deceive. This authority to prevent harm before it has occurred distinguishes the Commission's deception cases from private cases. In private cases, which a consumer usually must show actual injury.

2. The Reasonable Consumer

If a claim is likely to mislead, the Commission considers which consumers are likely to be misled. The Commission will consider only reasonable interpretations of advertising claims in determining whether deception has occurred. The Commission does not attempt to correct interpretations that will be reached by only an insignificant and unrepresentative group of persons to whom the advertisement is addressed. For example, let us take a popular saying in the United States: "An apple a day keeps the doctor away." It is unlikely that an ordinary consumer would interpret that claim as promising that apples will prevent the need for any medical care, although a very few consumers might actually take the claim literally. If the Commission were to impose a standard that no person possibly could be deceived -- even the few who believe the apple claim to be literally true --

the general public would be deprived of much information that is truthful and useful in guiding purchasing decisions.

First, the Commission expects that consumers will interpret claims to mean what they actually saw (an "express" claim), and it presumes that these interpretations are reasonable. For example, a claim that a food product is low in fat will be read exactly as it is stated. On the other hand, the claim that an apple-a-day keeps the doctor away should not be taken literally because it defies common sense, and most consumers would recognize that the advertiser did not intend consumers to take the claim literally.

Deciding whether other interpretations are reasonable is often more complex. For example, the apple-a-day claim might well imply that eating apples is a good way to stay healthy. Indeed, this implication is so strong as to be "virtually express," the Commission could determine on its own what interpretations consumers would reasonably take from the advertisement.

In other instances, where advertising claims are not so clear, the Commission may look for extrinsic evidence to help it determine how to assess consumers' interpretation of the representations made. Such evidence might include consumer surveys, copy tests in which the actual advertising is exposed to samples of consumers for reactions, and testimony or scholarly research of experts in the field of marketing.

To violate the FTC Act, a deceptive claim need not be the only interpretation of an advertisement. Almost all advertisements convey more than one message -- some express and some implied. Even if many consumers reasonably may interpret an advertisement in a nondeceptive way, a seller may be held liable for deception if another reasonable interpretation of the same advertisement is found likely to mislead reasonable consumers.

3. Materiality

The Commission must find not only that a representation in an advertisement is likely to mislead reasonable consumers, but also, that it is "material." In other words, it must be likely to affect consumer conduct or decisionmaking.

The Commission presumes several types of claims to be material: These include express claims -- if the advertiser says something explicitly, we assume it is important to a consumer's decision. For the same reason, when there is evidence that a seller *intended* to make a particular implied claim, the Commission will presume the claim is material.

This, in a nutshell, is the theoretical framework that the Commission uses to assess deceptive acts and practices. Let me show you how it works in practice.

4. Examples

Consider a recent case involving an advertisement for Coffee-mate Liquid, a non-dairy creamer that some consumers use in coffee instead of milk or cream. The advertisement shows a woman pouring a small amount into a cup of coffee and then

filling a bowl of cereal with about a half a cup (or about 1/4 liter) of the same product. As she does so, the woman says:

I like rich, creamy tasting things. But I also like to stay away from cholesterol and saturated fat. I found a smart new way to do both. New Coffee-mate non-dairy creamer. All the rich, creamy taste of half-and-half [a competing product containing half milk and half cream], but 75% less saturated fat and no cholesterol. In coffee, over fruit or cereal, Coffee-mate is a smart new way to have the taste you like without the fat and cholesterol you don't.

The picture shows a one-liter carton of Coffee-mate Liquid, a cup of coffee, a bowl of cereal and a bowl of fruit.

Let's look more closely at this advertisement:

The Commission believed it likely that consumers would understand the message of the advertisement to be that the product was low in fat for the serving size and that it would be a lower fat substitute for the usual dairy products used in coffee, cereal and other foods.

Just what are the facts about this product? First, a standard serving size for use in coffee is only 1 tablespoonful or about 14.78 milliliters. The standard serving size for use with cereal, however, is 1/2 cup or about 1/4 liter. The amount a consumer would use on cereal has nearly twice the amount of fat as the same amount of whole milk and nearly four times the amount of fat as the same amount of low-fat milk.

At the very small serving size for coffee, the product might be considered a low fat product because it contains fewer than 2 grams of fat per serving. At the larger serving size for use with cereal or fruit, however, Coffee-mate contains 8.5 grams of fat, including 1.8 grams of saturated fat. This overall level of

fat is far above the level the United States Food and Drug Administration considers appropriate for a product labeled "low in fat." Can it truthfully be said, then, that Coffee-mate is a good "low-fat" substitute for all the dairy products it competes with? The Commission thought not, and the consent order signed by the company bars it from making these or similar claims in the future.⁹

Advertising Substantiation

The FTC's advertising substantiation doctrine (also referred to as the "reasonable basis" doctrine) is a refinement of the Commission's policy on deceptive advertising. Under the Advertising Substantiation Doctrine, objective product claims -- that is, claims about a product's features, performance or effectiveness -- require a certain level of proof or support. As a matter of law, claims that cannot be adequately supported by advertisers at the time they are made are deceptive.

What is adequate substantiation? And how does the Commission decide whether an advertiser has met this requirement? The amount of substantiation needed depends on the advertisement itself -- that is, the Commission considers the type of claim, the type of product, the benefits of a truthful claim, the

⁹ A consent order is part of a settlement of a case. In agreeing to such a settlement, the Commission makes no finding of wrongdoing, and the company makes no admission that the facts alleged by the Commission are true or that the company violated the law.

dangers of a false claim, and the amount of substantiation experts generally believe is reasonable.

For example, an advertisement expressly or impliedly claiming that "clinical tests confirm that a certain product cures a problem" sets its own standard. The advertiser must have clinical tests that definitely prove its claim. On the other hand, a claim that "most medical experts agree one brand is better than another brand" must be supported by valid survey evidence of doctors that shows that result. In addition, to qualify as a reasonable basis for such claims, the studies or surveys relied on to support claims must have been conducted and evaluated in an objective manner by qualified persons using procedures generally accepted in the scientific community as giving accurate and reliable results. This means that advertisers cannot meet the standard with a study that is methodologically flawed or that contradicts generally held scientific beliefs. If test results or other substantiation are limited, claims based on them may not go beyond these limitations.

Returning once again to my apple-a-day claims, the simple claim, "An apple a day keeps the doctor away," would require proof that apples are good for you. Please keep in mind that this statement is a very old and familiar folk saying in my country. But assume a more specific claim: "Regular apple-eaters make 30% fewer visits per year to the doctor." This is not a common claim in my country, and we would require the advertiser

to have survey or other statistical evidence that supports the specific assertion of 30% fewer visits to the doctor.

Because it balances a number of considerations, the reasonable basis standard is inherently flexible and responsive to the circumstance of each case. When the consequences of a false claim are serious -- for example, if a false health claim for an over-the-counter drug is likely to cause consumers not to get appropriate medical treatment -- the Commission will require greater substantiation than it might for a claim that will not result in serious injury -- for example, "Most tennis champions favor a particular racquet."

In evaluating the level of substantiation needed to support a claim the Commission recognizes that the public will not benefit if the substantiation burden is too high. Such a standard might discourage advertisers from making truthful claims and providing useful information. Consumers then would have less basis for making purchasing decisions.¹⁰

Unfairness

The Commission has referred to the unfairness doctrine as "the FTC's general law of consumer protection, for which deception is one specific but particularly important application."¹¹ Because the concept of unfairness potentially

¹⁰ For a detailed explanation of how the FTC applies the reasonable basis standard, see Thompson Medical Co., Inc., 104 F.T.C. 648 (1984), aff'd, 791 F.2d 189 (D.C. Cir. 1986), cert. denied, 479 U.S. 1086 (1987).

¹¹ International Harvester, Inc., 104 F.T.C. 949, 1064 (1984).

is so expansive that it could include any practice that Commissioners do not like for one reason or another, it is important that the Commission have a well-articulated standard for delineating this authority. Otherwise, the law could result in having the government make choices it thinks are good for consumers, instead of allowing consumers to make decisions for themselves.

The FTC's definition of unfairness has evolved over its history. Since its early days, the United States Supreme Court has upheld the authority of the FTC to challenge conduct that was not specifically deceptive or violative of the antitrust laws.¹² The Commission's first formal articulation of its unfairness standard was set forth in 1964 as one of the justifications for a rule that would have required cigarette manufacturers to include a warning of health risks in all cigarette advertising and on each cigarette pack.¹³

The Commission, in a definition noted by the Supreme Court in 1972,¹⁴ identified three elements of unfairness: whether the

¹² FTC v. R.F. Keppel & Bros. Inc., 291 U.S. 304 (1934) (holding that the merchandising of penny candy to children by lottery unfairly exploited consumers to the prejudice of the respondent's competitors).

¹³ 16 C.F.R. § 408.1. Congress subsequently preempted the Cigarette Rule by enacting its own cigarette warning scheme. See 15 U.S.C. §§ 1331-1340 (1976). The statute specifically stated, however, that it was not intended to cast doubt on the Commission's jurisdictional authority to have promulgated the rule. Id. § 1336. See S. Rep. No. 566, 91st Cong., 1st Sess. 2652, 2664 (1969); H.R. Rep. No. 222, 91st Cong., 1st Sess. 93, 95 (1969).

¹⁴ FTC v. Sperry & Hutchinson, 405 U.S. 223, 244-45 n. 5.

practice offends public policy; whether it is immoral, unethical, oppressive, or unscrupulous; and whether it causes substantial injury to consumers (or competitors or other businessmen)."¹⁵

In 1980, the FTC elaborated and shifted the emphasis in its unfairness standard.¹⁶ The Commission again stated a three-part test, but it focused primarily on the "injury" portions of the earlier standard. An act or practice is considered unfair under that test if (1) it causes substantial consumer injury; (2) the injury is not outweighed by offsetting benefits to consumers or to competition; and (3) the injury is not reasonably avoidable by consumers.

Although public policy, is one of the three elements in the old standard, the Commission noted in 1980 that this element is used primarily as a means of providing additional evidence about the degree of consumer injury caused by specific practices. That is, statutory policies and established judicial policies may assist in helping the Commission ascertain whether a particular form of conduct does in fact harm consumers.¹⁷

¹⁵ Id. at 8354-55.

¹⁶ Letter to the Consumer Subcommittee of the Senate Committee on Commerce, Science and Transportation Commission Statement of Policy on the Scope of Consumer Unfairness Jurisdiction, 4 Trade Reg. Rep. (CCH) ¶ 13,203 (Dec. 17, 1980) (hereafter "Unfairness Letter").

¹⁷ The Commission found the third S&H criteria -- "unethical or unscrupulous conduct" -- to be largely duplicative of the first two criteria and unnecessary in its unfairness analysis: "Conduct that is truly unethical or unscrupulous will almost always injure consumers or violate public policy as well." Id. at 12.

The 1980 injury test is the standard the Commission currently uses to define unfairness under the FTC Act. The first step of our unfairness analysis is to determine whether there is substantial injury caused by the alleged unfair practice. Most often the Commission finds substantial injury in the form of monetary harm. Sales practices that impose health or safety risks, however, also can support a finding of unfairness. Injury may be "substantial" if the practice causes large injury to a small number of people, or a small injury to a great number of people. The Commission does not concern itself with trivial or merely speculative harms.

The second step is to see if the practice provides benefits that offset the harm to consumers or to competition. The Commission recognizes that most business practices provide a mixture of costs and benefits for consumers. In considering whether a practice causes net injury, the Commission considers not only costs to the parties directly before the agency, but also burdens on society in general that may result from regulatory action.

For example, in the recent case of Orkin Exterminating Company, Inc.,¹⁸ the company had entered into contracts with consumers providing that, for a fixed yearly fee, the company would guarantee homeowners that their houses would be free of wood-eating termites. Although the contracts did not allow for

¹⁸ Orkin Exterminating Co., Inc., 108 F.T.C. 263 (1986), aff'd, 849 F.2d 1354 (11th Cir. 1988).

increasing the yearly fee, the company unilaterally imposed an increase that affected over 200,000 consumers. The Commission decided that the company's conduct in breaching the contracts was an unfair practice. In ordering that the fee increase be rescinded, the Commission found that the consumer injury caused by the added fee was substantial (collectively, millions of dollars) and unavoidable, and that it conferred on consumers no benefits in terms of better or increased services. The Commission also decided that the company's unilateral and systematic breach of its service contracts undermined the contracting process by discouraging reliance on contract terms and thereby injured competition as well as individual consumers.

The third step in the Commission's unfairness analysis is to consider whether consumers could reasonably avoid the injury. This step acts as a check on regulatory action. For example, if Orkin's customers had been able to switch to another pest control company without incurring additional costs, there might not have been a need for the Commission to intervene.

In another sense, this third step recognizes that ensuring informed consumer choice is one of our primary goals. We look at whether a challenged practice unreasonably inhibits consumers from making independent and informed purchasing decisions, regardless of whether so-called "better" choices may be available. In a very real sense, the best choice for a consumer is that consumer's informed and independent choice. "Better"

choices, in this sense, simply refer to the choice that someone else would make.

For example, if Orkin's contracts had provided for periodic increases in the annual fee, the Commission would not have viewed the company's fee increase as unfair. We would likely have presumed that Orkin's customers had made informed choices to enter into the flexible contracts knowing that the fee could increase and knowing that they could choose another provider who might have offered a lower or a fixed price.

Future Enforcement Trends

Now that I have described what the FTC's consumer protection authority is and how the FTC implements it, let me talk for a moment about the future. My forecast can be summed up in just a few words: just as advertising and marketing responds to consumer concerns, so do the Commission's enforcement priorities.

I would like to touch on a few areas, although certainly this list should not be viewed as exhaustive.

First, I fully expect that the Commission's interest in environmental claims -- green marketing -- will continue. This remains an area of substantial interest both to consumers and sellers, and I do not see any significant decrease in that interest in the next few years. Second, consumers are very interested in the nutritional benefits of the foods they eat. As scientists have uncovered evidence linking specific diseases to diet, health claims in food advertising have proliferated, some truthful and some deceptive.

Nutritional and environmental claims often rely on complicated science that most consumers cannot evaluate for themselves. These claims often are referred to as "credence" claims. It is more important for the FTC to examine these credence claims and to ensure that they are adequately supported than to focus on claims the truth of which consumers may judge for themselves. For example, a claim that a particular food product will confer a health benefit is a claim that consumers reasonably might be unable to evaluate, while a claim that the same food product tastes good can easily be assessed. I expect, therefore, that the Commission will continue to pay more attention to nutritional and environmental claims in the months and years to come.

Conclusion

In closing, I believe that the Commission's challenge is to maintain a vigorous enforcement program designed to eliminate unfair and deceptive conduct while at the same time permitting sufficient flexibility for sellers to respond informatively and creatively to consumer concerns. The free flow of information in the market is the best safeguard of a competitive market economy, and the Commission takes seriously its responsibility for protecting and fostering such a free market.

Thank you -- Obrigado.