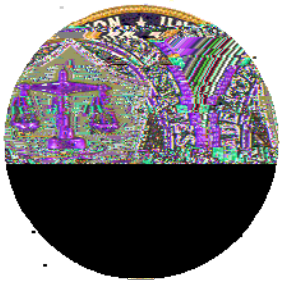

# Federal Trade Commission

**DECEPTIVE AND UNFAIR ACTS AND PRACTICES PRINCIPLES: EVOLUTION AND CONVERGENCE**

**J. Thomas Rosch**[1]
**Commissioner, Federal Trade Commission**

**at the**

**California State Bar**
**Los Angeles, California**
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## Introduction

As most of you know, this is my second stint at the FTC. From 1973 to 1975, I served as Director of the agency's Bureau of Consumer Protection. "BCP" (as it has always been called) was a different world back then. The principal statute we enforced – Section 5 of the FTC Act – was the same as the one that is enforced today. And the words of the statute were the same. Then, as now, it prohibited "unfair or deceptive acts or practices." But what was meant by the terms "deceptive" and "unfair" in 1973 or 1975 was very different from what these words mean now. And today they cover acts and practices that we couldn't then imagine might occur.

From 1975 until the beginning of 2006, when I returned to the FTC, I was back in California – where I practiced in San Francisco. Although my practice was predominantly

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[1] The views stated here are my own and do not necessarily reflect the views of the Commission or other Commissioners. I would like to express my gratitude to Beth Delaney and Serena Viswanathan, my attorney advisors, for their contributions to this speech.

[5] *Feil v. F.T.C.*, 285 F.2d 879, 892 n.19 (9th Cir. 1960).

[6] *Aronberg v. F.T.C.*, 132 F.2d 165, 167 (7th Cir. 1942)*; Florence Mfg. Co. v. J.C. Dowd & Co.*, 178 F. 73, 75 (2d Cir. 1910); *see also F.T.C. v. Standard Educ. Society* 1T8tCir1Tj1937)("The fact

> *Third*, the 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.

Two dissenting Commissioners argued that this description of the elements presented a sharp departure from the "tendency or capacity" standard and the "credulous consumer" standard. And it surely did. The former standard was replaced by a standard requiring "likely" misleading. The latter standard was then enhanced by a second standard linking the likelihood of misleading to "a consumer acting reasonably in the circumstances."

Additionally, in 1984, the Commission issued a Statement on Advertising Substantiation.[9] That statement adopted prior cases in which the Commission had held that the failure to have a reasonable basis for a claim at the time a claim is made may render the claim deceptive.[10] But the Statement went beyond the prior case law by making it clear that the substantiation requirement applied to implied as well as express claims and that the prior substantiation required would have to be sufficient to satisfy the relevant scientific community about the claim's proof.[11] This meant, for example, that claims that impliedly promised a level of scientific substantiation would have to be supported by well-controlled, double-blind clinical

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[9] Appended to *Thompson Medical Co.*, 104 F.T.C. 648, 839 (1984), *aff'd*, 791 F.2d 189 (D.C. Cir. 1986), *cert. denied*, 479 U.S. 1086 (1987).

[10] *Firestone Tire & Rubber Co. v. F.T.C.*, 481 F.2d 246, 251 (6th Cir. 1973).

[11] *Removatron International Corp.*, 111 F.T.C. 206, 306-07 (1988), *aff'd*, 884 F.2d 1489 (1st Cir. 1989).

testing.[12]

Why these changes in the FTC's principles of deception? First, the Policy Statement on Deception was issued during President Reagan's first term. It undoubtably reflected the view of a more conservative majority of Commissioners that the application of the old principles could result in unwarranted federal government challenges to advertising. Second, truth be told, the old principles were an anachronism. When I was at BCP in the early 1970s, we never challenged advertising that merely had a tendency or capacity to deceive the credulous consumer. Our challenges were to advertising that was likely to deceive a reasonable consumer.

The reasons for the Statement on Advertising Substantiation were essentially the same. Even in the early 1970s, we were anxious to shift from the federal government to private entities as much as policing as possible, and one way to do that was to require advertisers to substantiate their claims before the claims were made. In 1984, the Reagan FTC doubtless felt that was also philosophically sound.

B&P C Section 17200 (and 17500) Standards for Deception

The evolution of the deception standard under § 17200 somewhat mirrors the evolution at the FTC. Back in the late 1970s, when I returned to California, deception under § 17200 was

[12] *Id.* at 311.

[13] *Leoni v. State Bar*, 39 Cal. 3d 609, 626 (1985)(noting that Sections 17200 and 17500 are "interpreted broadly to embrace not only advertising which is false, but also advertising which although true, is either actually misleading or which has a capacity, likelihood or tendency to deceive or confuse the public"); *Payne v. United California Bank*, 23 Cal. App. 3d 850, 856 (1972)("The statute affords protection against the probability or likelihood as well as the actuality of deception or confusion"); *see also People ex re. Mosk v. National Research Co. of Cal.*, 201 Cal. App. 2d 765 (1962)(affirming lower court decision finding practices directed at consumer debtors had 'tendency and capacity' to mislead).

[14] *Day v. AT&T Corp.*, 63 Cal. App. 4th 325, 332-333 (1998).

[15] *Lavie v. Procter & Gamble*, 105 Cal. App. 2d 496, 504-07 (2003); *Haskell v. Time*, 857 F. Supp. 1392, 1399 (E.D. Ca. 1994); *Freeman v. Time, Inc.*, 68 F.3d 285, 289 (9th Cir. 1995).

[16] *Lavie, supra*, 105 Cal. App. 4th at 507 (citations omitted). The Attorney General argued in *Lavie*

Deception was incorporated into the § 17200 case law.

Second, in a couple of respects, California law has been more demanding than the FTC case law in terms of proving deception. For one thing, California's False Advertising Act, Section 17500, not only mimics § 17200, but requires proof that the alleged actionable statement "is known, or which by the exercise of reasonable care should be known, to be untrue or misleading . . . ."[17] It makes little sense to require proof of this state of mind on the part of the defendant making an allegedly deceptive statement, on the one hand, and then on the other hand, to require proof only of a tendency or capacity to deceive a credulous consumer, when it comes to proof of the statement's effect.

For another thing, California (and federal) case law have been very demanding in terms of the kind of evidence needed to proved the likelihood of deception.[18] Thus, in *Haskell v. Time*, the court found that declarations from a "few" consumers and a professor of rhetoric to be insufficient.[19] In *William H. Morris Co. v. Group W, Inc.*, the Ninth Circuit concluded that the plaintiff had not carried its burden where the evidence consisted of testimony from two out of 300 recipients.[20] It would be hard to square these proof requirements with a substantive rule requiring only proof of a "tendency or capacity" to deceive a credulous consumer.

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[17] Cal. Bus. & Prof. Code § 17500 (Deering 2007).

[18] *See S. Bay Chevrolet v. GM Acceptance Corp.*, 72 Cal. App. 4th 861, 896 (1999)(requiring "substantial evidentiary support").

[19] 965 F. Supp. 1398, 1407-08 (E.D. Cal. 1997).

[20] 66 F.3d 255, 258 (9th Cir. 1995).

explored had few limiting principles. Chief among these was the so-called "Kid Vid" initiative, which tried to define unfair practices in marketing products to children and which was buried under a heap of scorn – the Washington Post accused us of trying to be the "National Nanny."[27]

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[27] Editorial, "*The FTC as National Nanny*," Wash. Post., Mar. 1, 1978 at A14.

[28] Reprinted in H.R. Rep. No. 98-156 at 33 (1983) and 4 Trade Reg. Rep. (CCH) ¶ 13,203.

[29] *In the Matter of International Harvester Company*, 104 F.T.C. 949 (1984).

[30] *Id.* at 1064 and 1073 n.12.

[31] *Id.* at 1073; *see also* H.R. Rep. No. 98-156 at 33 (1983).

[32] 104 F.T.C. at 1066.

[33] 15 U.S.C. § 45(n).

[34] An example of such a case might include a situation where a business has failed to adequately secure the sensitive, but not financial, information of consumers; while such a breach of privacy may not result in financial harm, it could embarrass or have a significant

[35] 136 Cal. App. 4th 1255 (2006).

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The other line of cases, led by *Scripps Clinic v. Superior Court*[41] and *Gregory v. Albertson's Inc.*,[42] hold that the public policy which is the basis for an unfair competition action under the "unfair" prong must be "tethered to specific constitutional, statutory, or regulatory provisions."[43] This formulation essentially embraces the judgment made by the Commission in 1980 and the Congress in 1994.

The reason for this schizophrenic state of the law is easy to discern. It is rooted in the California Supreme Court's decision in *Cel-Tech Communications Inc. v. Los Angeles Cellular Telephone Co.*[44] As the court in *Bardin* states correctly, on the one hand, the *Cel-Tech* decision severely criticized the untethered definition of unfairness in several cases brought by consumers.[45] On the other hand, however, after severely criticizing an untethered definition of unfairness in the case before it – which was brought by a competitor – the court declared that "nothing we say relates to actions by consumers."[46]

To date, neither the California Supreme Court nor the Legislature has provided the clarification requested in *Bardin* but I will hazard speculation that ultimately the FTC view of

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[41] 108 Cal. App. 4th 917 (2003).

[42] 104 Cal. App. 4th 845 (2002).

[43] *Bardin*, 136 Cal. App. 4th at 1261 (citing *Scripps*, 108 Cal. App. 4th 917 and *Gregory*, 104 Cal. App. 4th 845).

[44] 20 Cal. 4th 163 (1999).

[45] *Bardin*, 136 Cal. App. 4th at 1266.

[46] *Id.* at 1267.

unfairness will prevail. Why? First, as I've previously said, § 17200 is regarded as a "baby FTC Act," and the way that the agency and the Congress have interpreted the Act will probably be followed in the case of unfairness as it has been in the case of deception. Indeed, the recent *Camacho* decision by the appellate court supports this prediction.[47] After an extensive discussion of the two lines of authority considered in *Bardin*, the court adopted the modern FTC Section 5 definition of unfairness, noting that this definition "is on its face geared to consumers"

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[47] *Camacho v. Automobile Club of California*, 142 Cal. App. 4th 1394 (2006).

[48] *Id.* at 1403. The court, in fact, declined to adopt the limiting principle found in the last two sentences of Section 5(n): 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. *Id.* at 1405.

[49] *Id.* at 1404.

Other Unanswered Questions

Several other questions remain unanswered. One is whether the failure to have a reasonable basis for a claim is "unfair or deceptive" under § 17200. The answer to that question seems clear. If § 17200 is really a "baby FTC Act," the Commission's 1984 statement on that score will almost certainly be endorsed. The second question is whether, and to what extent, §