

Brief

FTC Finally Offers ‘Principles’ Governing Section 5 Powers, but Specific Guidance to Businesses Still Lacking

By Carl Hittinger and M. Mitchell Oates



In 1914, Congress passed the FTC Act, creating the Federal Trade Commission. Section 5 of the FTC Act declared “unfair methods of competition in or affecting commerce” to be unlawful and gave the FTC enforcement power over such “unfair methods.” More than 100 years later, that key language in Section 5 underlying the agency’s competition-related powers had never been the subject of any formal FTC guidance. Clearly, “unfair methods of competition” include Sherman and Clayton Act violations, and some argue that Section 5 reaches beyond those statutes. But exactly what kind of additional conduct falls within the FTC’s Section 5 powers has been a long-unsettled question.

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On Aug. 13, 2015, the FTC finally issued a “Statement of Enforcement Principles” setting forth the general considerations to guide the FTC’s decision whether to exercise its “standalone” Section 5 authority, i.e., “unfair methods of competition” that would not otherwise violate the Sherman or Clayton Act. According to the Statement, the FTC, when exercising its standalone Section 5 authority:

- Will be guided by the public policy underlying the antitrust laws—the promotion of consumer welfare;
- Will evaluate conduct using a framework “similar to the rule of reason,” meaning that challenged conduct “must cause, or be likely to cause, harm to competition or the competitive process, taking into account any associated cognizable efficiencies and business justifications”; and,
- Will be less likely to act if enforcement under the Sherman or Clayton Act would be sufficient.

The Commission voted 4-1 to adopt these principles, with a dissenting vote from Commissioner Maureen Ohlhausen, who, like recently departed Commissioner Joshua Wright, has been outspoken about the need for formal Section 5 guidance. Commissioner Ohlhausen stated that she could not sign on to this particular policy statement for various reasons, including its “abbreviated” nature, the lack of meaningful guidance provided, and the agency’s failure to seek public comment.

Chairwoman Edith Ramirez emphasized that the guidelines do not reflect any change in the agency’s priorities or policies but merely formalize the approach already followed by the agency.

The explicit recognition that standalone Section 5 enforcement is directed toward conduct that harms consumers and the competitive process should provide some assurance that the FTC will not use Section 5 to pursue policy goals unrelated to competition.

In announcing the Statement, Chairwoman Edith Ramirez (who has been under pressure from Congress to issue guidelines) repeatedly emphasized that it did not reflect any change in the agency’s priorities or policies. She said the Statement merely formalized the approach already followed by the agency. These core principles, she claimed, would have been readily evident to FTC observers in recent years. However, as Commissioner Wright had repeatedly and pointedly stressed, neither the Section 5 forest nor the trees were clear and certainly not readily evident.

The New Section 5 Guidance Does Include Substantive Constraints on FTC Authority

Given that absence of any guidance on Section 5 for more than a century, the principles adopted last week are undoubtedly a positive development. Stakeholders, the courts, and FTC staff now have, at least, a starting point from which to analyze potential Section 5 investigations, within some defined legal principles and framework.

Unfortunately, the Enforcement Principles lack the specificity required to give the business community adequate certainty about what might draw FTC scrutiny under Section 5.

The Statement’s explicit recognition that standalone Section 5 enforcement is directed toward conduct that harms consumers and the competitive process should provide some assurance that the FTC will not use Section 5 to pursue policy goals unrelated to competition. While Chairwoman Ramirez characterized this as a constraint, its importance should not be overstated. It is true that former FTC Chairman Michael Pertschuk decades ago indicated his belief that the FTC’s competition mission encompassed such things as “resource depletion, energy waste, environmental contamination,” and “worker alienation.” However, such an expansive view of the agency’s mission has not seriously been proposed in recent years, except possibly by the N-Data majority (including later-Chairman Jon Leibowitz), which noted older Supreme Court language suggesting that Section 5 might include “practices that the Commission determines are against public policy for other reasons.” Because there has been consensus for some time now that Section 5 was intended for antitrust enforcement, the political reality is that this “limitation” has little practical significance.

The Enforcement Principles also make explicit that the FTC will use a framework “similar” to the rule of reason in deciding whether to assert its standalone Section 5 authority. As Commissioner Wright has stressed, this is a significant acknowledgment. The rule of reason standard is used regularly and is well-understood in antitrust jurisprudence. Importantly, the framework takes into account “cognizable efficiencies and business justifications” associated with a given practice. The fact that potentially offsetting efficiencies are formally factored into the analysis is important, as it confirms that the FTC’s processes will include some safeguard against stifling pro-competitive activity. It remains unclear, though, whether an analysis “similar” to the rule of reason means that the FTC will depart from the rule of reason in some respects and – if so – exactly how and why. Stay tuned there.

Uncertainty Remains Because of the Absence of Concrete Guidance and Specificity

Unfortunately, the Enforcement Principles lack the specificity required to give the business community adequate certainty about the risk that a proposed course of conduct might draw FTC scrutiny under Section 5. Most notably, the Principles include no specific examples of activity that will, or will not, constitute a standalone Section 5 violation, even though past FTC guidelines in other areas have usually included such examples.

During Chairwoman Ramirez's announcement, the chairwoman cited invitations to collude, competitors' exchange of competitively sensitive non-price information, and patentees' breaches of their commitments to license certain patents on fair and reasonable terms as examples of past FTC enforcement actions illustrating the application of the announced principles beyond the Sherman Act. Notably, however, neither of these examples nor any others were part of the written Statement adopted by the Commission, so it is unclear whether the other commissioners agreed with these examples. Even invitations to collude, which Chairwoman Ramirez called an "accepted fixture" of Section 5 authority, do not fit well with the principles articulated. A rejected offer to fix prices does not injure consumer welfare or harm the competitive process, and it is unclear what meaningful damages or injunctive relief could be sought in such cases in any event. Although some commentators may believe that offers to collude should be discouraged, it is well-established law that an agreement is required to violate Section 1 of the Sherman Act – put simply, there is no such thing as "attempted price fixing" under the Sherman Act. Using Section 5 to capture Sherman Act "near misses" seems inconsistent with the FTC's third guiding principle: that standalone authority will not be used when the Clayton or Sherman Act is on point.

Merely stating that the FTC's inquiry will be guided by the "rule of reason" provides little direction to the business community regarding what is and is not prohibited. The rule of reason is a notoriously fact-specific and unpredictable inquiry, one that U.S. Supreme Court Chief Justice John Roberts has described as "unruly." And while Chairwoman Ramirez stated her belief that the Principles are entirely consistent with the FTC's standalone enforcement activity in recent decades, Commissioner Ohlhausen noted in her dissent that certain conduct that courts have already rejected would seem to be appropriate under the Principles. Given the disagreement within the FTC itself as to whether numerous types of conduct pass the rule of reason test, it will no doubt be difficult for companies to make this assessment for themselves with any degree of certainty.

In her speech, Chairwoman Ramirez acknowledged that some might find the Statement "too general" to provide guidance for the business community but explained that the "concise" nature of the Principles was justified because of the use of well-understood antitrust terms defined over 125 years of interpretation of the Sherman and Clayton Acts. She acknowledged that the Statement did not include a detailed list of proscribed conduct but stated that this was consistent with the common-law approach generally used in antitrust law. It is true that there exists a substantial body of case law applying the rule of reason to particular examples of business activity challenged under the Sherman Act. However, because a standalone Section 5 violation is, by definition, outside the Sherman Act, it is unclear how the common-law refinement of the rule of reason will be of significant assistance to Section 5 doctrine, particularly given the examples given by Chairwoman Ramirez that are contrary to Sherman Act jurisprudence, like invitations to collude.

This observation frankly highlights the problem with Chairwoman Ramirez's oft-stated position that a common-law approach based in prior FTC consent decrees and complaints is the best way to define the boundaries of the FTC's Section 5 powers. In the case of Section 5, the analogy to the common law is problematic. When a party loses to the FTC on summary judgment, we can say it is because its conduct violated the law. When a party enters into a consent decree, by contrast, we can say nothing – it is a black box. Parties investigated by the FTC might choose to enter into a consent decree for any number of reasons. One cannot assume with any confidence that a party chose to settle a standalone Section 5 claim based on an informed determination that its conduct was an unlawful "unfair method of competition." That assumption is especially questionable when no one knows what constitutes an "unfair method of competition" – the state of affairs for the past hundred years.

There is value in flexibility, especially in the antitrust context, but flexibility must be balanced against the need to inform the business community regarding what type of conduct might trigger an FTC investigation. Section 5 should not be a "gotcha" game

Following the announcement, Commissioner Wright noted that no U.S. Court of Appeals had weighed in on a Section 5 question in 50 years and that some judicial interpretation to "help define the contours" would be beneficial. With some formal principles now in place, perhaps more Section 5 enforcement actions will reach the courts. Reasoned opinions from judges schooled in Sherman Act jurisprudence will be of great value in helping answer the many open questions regarding Section 5. Uncertainty will continue under the current system, in

which the FTC's criteria for enforcement must be divined from an accumulated body of consent decrees, which may, for practical purposes, reflect only the FTC's view of its authority. Stay tuned there as well.

Not Perfect, but an Improvement Over the Status Quo

Even acknowledging their shortcomings, the Section 5 Enforcement Principles are historic. The need for the FTC to issue formal guidance had become a hotly debated issue, culminating with Commissioner Wright's keynote speech at the BakerHostetler Symposium on Section 5 of the FTC Act earlier this year. At that symposium, Commissioner Wright called for his fellow Commissioners to vote on formal Section 5 guidelines and offered three proposals, any of which, he said, would get his support. While the recently announced Principles do not correspond precisely to the options presented by Commissioner Wright, they incorporate elements of those proposals, as one would expect in any political debate in which compromise is necessary to move forward. For that reason, Commissioner Wright voted to adopt last week's Principles and stood behind them following the announcement, calling them a "significant constraining force."

Moreover, while the Principles do not provide a great deal of concrete guidance to stakeholders regarding what falls within the FTC's standalone Section 5 authority, this was likely not the Commission's instant intent. The Statement expressly states that Congress did not want "to define the specific acts and practices" that violate Section 5, in recognition of the need for application to "evolve with changing markets and business practices," leaving the FTC to exercise its authority "on a flexible case-by-case basis." Chairwoman Ramirez echoed this sentiment in her announcement.

Further Reading

The Past, Present, and Future of Section 5 of the FTC Act: Perspectives from the Commission, the Judiciary, and Congress – Carl Hittinger

There is value in flexibility, especially in the antitrust context, but flexibility must be balanced against the need to inform the business community regarding what type of conduct might trigger an FTC investigation, which is extremely expensive to defend, and which delays and potentially prevents activity in which resources have been invested and which may be pro-competitive on balance. Section 5 should not be a "gotcha" game. We shall see whether the Enforcement Principles lead to more frequent judicial input on the scope of Section 5. Until then, businesses would be wise to take measure before launching actions on the fringes of the Sherman or Clayton Act or similar to those previously targeted under Section 5, and be certain that they can ultimately demonstrate substantial efficiencies resulting from such actions. Stay tuned.

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