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FTC Announces Broader Vision of Its Section 5 Authority to Address Unfair Methods of Competition

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On November 10, 2022, the Federal Trade Commission released a new policy Statement setting forth its view of its enforcement authority under Section 5 of the FTC Act, 15 U.S.C. § 45, and announcing it will no longer focus on the "rule of reason" framework commonly used in Sherman and Clayton Act enforcement to determine liability. Instead, the FTC intends to broaden its enforcement of Section 5 to focus "on stopping unfair methods of competition in their incipiency based on their tendency to harm competitive conditions."[1] This new Statement reflects a significant departure from the FTC's previous position and reflects a general trend within the Biden Administration toward broadening the scope of its perceived authority and pursuing novel antitrust enforcement efforts.[2] While it remains to be seen how aggressively the FTC invokes this new approach to investigate and potentially challenge business practices not otherwise covered by the antitrust laws under Section 5, this development at a minimum adds uncertainty for businesses that heightens the need for vigilance in how they operate.[3]

Background: Section 5 of the FTC Act

In 1914, Congress passed the FTC Act, establishing the Commission and granting it authority to enforce fair competition law.[4] The FTC largely derives its enforcement authority from Section 5 of the FTC Act, which has two prongs: the first addresses consumer protection, based on the "unfair or deceptive acts or practices" statutory language, and the second addresses primarily antitrust, based on the "unfair methods of competition" ("UMC") statutory language.[5] This new Statement addresses Section 5's second prong, and explains the FTC's view on how the scope of Section 5 relates to the FTC's authority to enforce other antitrust laws, most notably the Sherman and Clayton Acts.

The Evolution of the FTC's Prior Views on Section 5's Scope

In 2015, the FTC released a one-page policy statement about principles of its UMC authority, explaining that it would (1) follow the consumer welfare standard, (2) evaluate acts under "a framework similar to the rule of reason," and (3) align FTC Act Section 5 enforcement with the scope of the Sherman and Clayton Acts.[6] Under new leadership, on July 1, 2021, the FTC rescinded this 2015 policy statement.[7] On November 10, 2022, in a sixteen-page statement, the FTC announced its newly broadened view of the scope of Section 5.[8]

The FTC's New Broader Position on Section 5's Scope

This new Policy Statement is hardly a model of clarity. It starts by explaining the FTC's view that "Section 5 reaches beyond the Sherman and Clayton Acts to encompass various types of unfair conduct that tend to negatively affect competitive conditions."[9] The Statement provides the FTC's justification of this view from its reading of judicial precedents,[10] the FTC Act's legislative history,[11] and congressional purpose[12].

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Then, it turns to the FTC's reading of Section 5's UMC language,[13] its analysis of potential cognizable justifications,[14] and closes with a long list of historical examples of unfair methods of competition.[15]

Analyzing the statutory language, the Statement explains that conduct must be a method of competition, i.e., "conduct undertaken by an actor in the marketplace [that] implicate[s] competition."[16] This includes indirectly implicating competition, and the FTC provides an example: "misuse of regulatory processes that can create or exploit impediments to competition (such as those related to licensing, patents, or standard setting)."[17]

Addressing what "unfair" means, the Statement explains that there are two criteria to determine if conduct goes beyond competition on the merits if the conduct is (1) "coercive, exploitative, collusive, abusive, deceptive, predatory, or involve[s] the use of economic power of a similar nature . . . [, or is] otherwise restrictive or exclusionary, depending on the circumstances" and (2) if the conduct "tend[s] to negatively affect competitive conditions."[18] The Statement emphasized that because "Section 5 analysis is purposely focused on incipient threats to competitive conditions, this inquiry does not turn to whether the conduct directly caused *actual* harm in the specific instance at issue."[19] Rather, the focus is on "whether the respondent's conduct has a tendency to generate negative consequences; for instance, raising prices, reducing output, limiting choice, lowering quality, reducing innovation, impairing other market participants, or reducing the likelihood of potential or nascent competition."[20]

In concluding its analysis of the statutory language, the Statement emphasized that Section 5, unlike virtually all other antitrust statutes, "does not require a separate showing of market power or market definition" when evidence indicates a tendency of anticompetitive effects.[21] Finally, the FTC noted that it would not utilize a rule of reason framework of analysis in its Section 5 enforcement.?[22]

In all, this newly announced interpretation of Section 5 is much broader than the previous administration's and is notable for its repetitious emphasis on "stopping unfair methods of competition in their incipiency." This perspective means that the FTC may launch investigations of practices before any anticompetitive harm or impact has arisen at all, much less one that causes market-wide injury. Additionally, the Statement only lightly touches on what may constitute a potential defensive justification, but suggests it intends to circumscribe companies' abilities to justify their business practices. For example, the FTC notes that "it would be contrary to the text, meaning, and case law of Section 5 to justify facially unfair conduct on the grounds that the conduct provides the respondent with some pecuniary benefits."?[23] Similarly, the Statement rejects a "numerical cost-benefit analysis" that would show the benefits of a practice outpace any potential harm, noting that the UMC framework "explicitly contemplates a variety of non-quantifiable harms."[24] Thus, the FTC contemplates broader liability under Section 5 along with narrower available defenses.

Examples of Unfair Methods of Competition that the FTC Highlighted

The Statement provides a "non-exclusive" list of examples that would constitute a Section 5 violation, including practices that (1) violate the Sherman and Clayton Act, (2) are "incipient violation[s] of the antitrust laws," and (3) violate "the spirit of the antitrust laws."?[25] The list follows:

1. Practices deemed to violate Sections 1 and 2 of the Sherman Act or the provisions of the Clayton Act, as amended (the antitrust laws).
2. Conduct deemed to be an incipient violation of the antitrust laws. According to the FTC, incipient violations include conduct by respondents who have not gained full-fledged monopoly or market power, or by conduct that has the tendency to ripen into violations of the antitrust laws. Past examples of such use of Section 5 of the FTC Act include:

- invitations to collude that have not resulted into an agreement between competitors,
- mergers, acquisitions, or joint ventures that have the tendency to ripen into violations of the antitrust laws,
- “serial” mergers, acquisitions, or joint ventures that tend to bring about the harms that the antitrust laws were designed to prevent, but individually may not have violated the antitrust laws, and
- loyalty rebates, tying, bundling, and exclusive dealing arrangements that have the tendency to ripen into violations of the antitrust laws by virtue of industry conditions and the respondent’s position within the industry.

3. Conduct that violates “the spirit of the antitrust laws.” This includes conduct that tends to cause potential harm similar to an antitrust violation, but that may or may not be covered by the literal language of the antitrust laws or that may or may not fall into a “gap” in those laws. As such, the analysis may depart from prior precedent based on the provisions of the Sherman and Clayton Acts. Examples of such violations identified in the new Policy, to the extent not covered by the antitrust laws, include:

- practices that facilitate tacit coordination,
- parallel exclusionary conduct that may cause aggregate harm,
- conduct by a respondent that is undertaken with other acts and practices that cumulatively may tend to undermine competitive conditions in the market,
- fraudulent and inequitable practices that undermine the standard-setting process or that interfere with the Patent Office’s full examination of patent applications,
- price discrimination claims such as knowingly inducing and receiving disproportionate promotional allowances against buyers not covered by the Clayton Act,
- de facto tying, bundling, exclusive dealing, or loyalty rebates that use market power in one market to entrench that power or impede competition in the same or a related market,
- a series of mergers or acquisitions that tend to bring about the harms that the antitrust laws were designed to prevent, but individually may not have violated the antitrust laws,
- mergers or acquisitions of a potential or nascent competitor that may tend to lessen current or future competition,
- using market power in one market to gain a competitive advantage in an adjacent market by, for example, utilizing technological incompatibilities to negatively impact competition in adjacent markets,
- conduct resulting in direct evidence of harm, or likely harm to competition, that does not rely upon market definition,
- interlocking directors and officers of competing firms not covered by the literal language of the Clayton Act,
- commercial bribery and corporate espionage that tends to create or maintain market power,
- false or deceptive advertising or marketing which tends to create or maintain market power, or
- discriminatory refusals to deal which tend to create or maintain market power.[26]

Commissioner Statements and Dissents

The Commission vote to approve the statement was 3-1, along party lines.

Commissioner Wilson, the lone currently seated Republican on the FTC, dissented, arguing that the new Statement "abandons bedrock principles of antitrust that long have been accepted by the Commission, the courts, the business community, and enforcers across the globe."[27] In particular, she noted that the Statement did not: (1) provide clear guidance to the business community on how to comply with the law, (2) establish an approach of what "unfair" means "that matches the economic and analytical rigor . . . in the consumer protection context," (3) provide a framework that will result in credible enforcement, or (4) address the legislative history "that both demands economic content for the term 'unfair' and cautions against an expansive approach to enforcing Section 5."[28]

Takeaways

This new policy statement is part of a larger trend toward more vigorous enforcement by the FTC and thus a broader risk of antitrust enforcement, as we have noted in previous Client Alerts addressing interlocking directorates, no-poach and non-solicit agreements, and criminal monopolization.

In light of this increasingly aggressive and unpredictable regulatory environment, it is important for companies to review their practices for any similar to those flagged by this policy statement. Gibson Dunn attorneys are closely monitoring these developments and are available to discuss these issues as applied to your particular business.

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[1] Policy Statement Regarding the Scope of Unfair Methods of Competition Under Section 5 of the Federal Trade Commission Act, Fed. Trade Comm'n (Nov. 10, 2022) ("UMC Policy Statement" or just the "Statement"). The Commission vote was 3-1 along party lines. Chair Khan and Commissioners Slaughter and Bedoya released a joint statement. *See* Joint Statement, Fed. Trade Comm'n (Nov. 10, 2022). Commissioner Wilson dissented. *See* Dissenting Statement of Commissioner Christine S. Wilson, Fed. Trade Comm'n (Nov. 10, 2022) (criticizing the new Statement as threatening due process and leaving "businesses in the dark on how to structure their conduct to avoid a challenge by the Commission").

[2] The Democratic-appointed Commissioners have recently made public statements about their views that the FTC has broader enforcement authority than it has traditionally purported to have. *See e.g.,* Chair Lina Khan, Prepared Statement of the Federal Trade Commission Before the United States Senate Committee on the Judiciary Subcommittee on Antitrust, Competition Policy and Consumer Rights, "Oversight of the Enforcement of the Antitrust Laws," Sep. 20, 2022, at 1 (noting that the FTC's focus is on "reactivating the full set of authorities" available to it); Commissioner Alvaro M. Bedoya, Prepared Remarks Before the Midwest Forum on Fair Markets, "Returning to Fairness," Sep. 22, 2022, at 8 (outlining Commissioner Bedoya's desire to see antitrust law move away from a focus on "efficiency" and toward a focus on "fairness"). As for enforcement priorities, the Statement's language closely reflects that contained in earlier omnibus resolutions approved by the FTC in a 3-2 vote. *See* FTC Authorizes Investigations into Key Enforcement Priorities, Fed. Trade Comm'n (July 1, 2021) ("Specifically, the resolutions direct agency staff to use 'compulsory process,' such as subpoenas, to investigate seven specific enforcement priorities. Priority targets include repeat offenders; technology companies and digital platforms; and healthcare businesses such as pharmaceutical companies, pharmacy benefits managers, and hospitals.").

[3] Many states have their own unfair competition laws, and the construction and scope of those laws is typically a matter of individual state law, so the impact of the FTC policy statement will not necessarily alter state unfair competition enforcement.

[4] FTC Act of 1914, Pub. L. No. 63-203, 38 Stat. 717 (codified as amended at 15 U.S.C. § 41– 58).

[5] *Id. See* A Brief Overview of the Federal Trade Commission's Investigative, Law Enforcement, and Rulemaking Authority, Fed. Trade Comm'n (last revised May 2021).

[6] Statement of Enforcement Principles Regarding "Unfair Methods of Competition" Under Section 5 of the FTC Act, Fed. Trade Comm'n (Aug. 13, 2015).

[7] Statement on the Withdrawal of the Statement of Enforcement Principles Regarding "Unfair Methods of Competition" Under Section 5 of the FTC Act, Fed. Trade Comm'n (July 9, 2021).

[8] UMC Policy Statement.

[9] *Id.* at 1.

[10] *Id.* at 1 n.3 (citing twelve Supreme Court opinions).

[11] *Id.* at 2–6 ("Congress wanted to give the Commission flexibility to adapt to changing circumstances.")

[12] *Id.* at 6–8 ("Congress intended for the FTC to be entitled to deference from the courts as an independent, expert agency.").

[13] *Id.* at 8–10.

[14] *Id.* at 10–12 ("In the event that conduct prima facie constitutes an unfair method of competition, liability normally ensues under Section 5 absent additional evidence. There is limited caselaw on what, if any, justifications may be cognizable in a standalone Section 5 unfair methods of competition case, and some courts have declined to consider justifications altogether.") (citing *Atlantic Refining Co. v. Fed. Trade Comm'n*, 381 U.S. 357, 371 (1965) and *Fed. Trade Comm'n v. Texaco*, 393 U.S. 223, 230 (1968), and *L.G. Balfour Co. v. Fed. Trade Comm'n*, 442 F.2d 1, 15 (7th Cir. 1971)).

[15] *Id*. at 12–16.

[16] *Id*. at 8.

[17] *Id*. at 8.

[18] *Id*. at 9–10.

[19] *Id*. at 10.

[20] *Id*.

[21] *Id*.

[22] *Id*.

[23] *Id*. at 11.

[24] *Id*.

[25] *Id*. at 12.

[26] *Id*. at 12–15 (edited for clarity) (citing cases).

[27] *See* Dissenting Statement of Commissioner Christine S. Wilson, Fed. Trade Comm'n (Nov. 10, 2022).

[28] *Id*. at 3.

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Gibson Dunn's lawyers are available to assist in addressing any questions you may have regarding the issues discussed in this update. Please contact the Gibson Dunn lawyer with whom you usually work, any member of the firm's Antitrust and Competition, Privacy, Cybersecurity and Data Innovation, Mergers and Acquisitions, Private Equity, or Securities Regulation and Corporate Governance practice groups, or the following practice leaders and members:

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