

TESTIMONY OF HENRY MCMASTER

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BEFORE THE UNITED STATES SENATE COMMITTEE ON COMMERCE,
SCIENCE & TRANSPORTATION

AND

BEFORE THE UNITED STATES SENATE COMMITTEE ON ENERGY AND
NATURAL RESOURCES

PRICE GOUGING DURING PERIODS OF ABNORMAL MARKET DISRUPTIONS

November 9, 2005

Thank you Mr. Chairman and members of the Committees on Commerce, Science & Transportation and Energy and Natural Resources for the opportunity to testify on the issue of price gouging during periods of abnormal market disruptions. My name is Henry McMaster and I am the Attorney General for South Carolina.

South Carolina's most recent experience with allegations of price gouging in the sale of a commodity occurred during the time periods immediately before and after Hurricanes Katrina and Rita struck the Gulf Coast on August 29 and September 24, 2005, respectively. The lessons learned in this period with regard to retail gasoline pricing are also applicable to possible price gouging for any other commodity which may result from abnormal disruptions in the market. For this reason, I will review the complexities of the gasoline pricing situation and then discuss its applicability to other commodities in general.

Like other states, South Carolina does not produce many of the resources necessary to drive its economy. With regard to gasoline, South Carolina does not have any native oil production; no refineries are located in South Carolina. South Carolina's supply of gasoline, as well as other commodities, is dependent on events which occur elsewhere.

My office received more than five hundred and fifty complaints directly from consumers and another 1,000 by referrals about alleged price gouging by gasoline retailers in South Carolina after Hurricanes Katrina and Rita struck the Gulf Coast. Our investigation of these complaints opened our eyes to the complexities of investigating allegations of price gouging, including (1) the difficulty of determining whether complaints are legitimate and credible, (2) the complexity of making determinations of

whether price increases were truly "gouging" or were based on legitimate business decisions or increases in the costs to the retailer, (3) the importance of having the tools necessary to investigate allegations of price gouging immediately while the data are fresh, and (4) the interdependence of all regions of the country with regard to price and supply allocation when a catastrophic event occurs. To conduct our investigation to enable us to understand the factors underlying the run-ups in the retail price of gasoline, we met with representatives of the various companies involved in the flow of gasoline from its origin as crude oil to the pump at retail gasoline stations. Enforcement specialists from my office visited approximately one hundred gasoline retailers in twenty counties in South Carolina (we have 46). We have also met with representatives of Marathon Ashland Petroleum, LLC, BP America, Inc., Shell Oil Products US, and ConocoPhillips. Additionally, we had a conference call with the chief economist and others of the American Petroleum Institute, the trade association for the oil producers. To further understand the retail marketing of petroleum products, we met with representatives of the South Carolina Petroleum Marketers Association. We met with an oil jobber to help us understand the problems associated with supplying gasoline to retailers during a period when less gasoline is physically available for distribution than is needed to continue to supply retailers at the same rate as prior to a market disrupting event.

As demonstrated by our efforts, the investigation of price gouging complaints for any commodity will necessarily be a complex investigation. As the result of the on-site investigations of various retailers, we are doing follow-up investigations of four corporate entities that own seven retail outlets. The complexities of the production and marketing of any commodity, petroleum in particular, makes it difficult to determine whether price

increases are the result of market forces and the workings of free enterprise or the result of short-term profiteering which takes untoward advantage of the market disruption. For example, we received a number of complaints about one multi-station retailer whose prices for regular gasoline went up to \$3.519 per gallon on September 29. However, after reviewing his records, it was determined that his supply costs had risen substantially in line with his retail prices, so that the price increases appeared to be the results of increased costs to the retailer rather than price gouging. The records of another retailer indicate that one of the retailer's employees, without direction from the retailer, made an unauthorized price increase out of panic because the employee thought the station would run out of gasoline; the employee wanted to slow down the sales volume in order to avoid running out of supply. As to the retailers under investigation, it is still too early to determine whether or not they acted improperly. But we have learned how difficult it is to make a determination of the true cause of fluctuations in market price.

Investigative powers which can be implemented immediately are necessary to determine whether rapid and large increases in the retail prices of any necessary commodity are the result of short-term profiteering or fraud instead of the market forces balancing the demand for the commodity with the available supply. South Carolina has those under the Unfair Trade Practice Act, 35-5-10 et seq.

The power to file civil actions concerning these changes in prices also arise under the Unfair Trade Practice Act. Further, during a declared state of emergency (by the Governor of South Carolina or the President of the United States), one specific section of the Act also makes it a crime (1) to rent or sell or offer to rent or sell a commodity (broadly defined, including goods and services) at an unconscionable price within the

area for which the state of emergency is declared during the time period that the state of emergency is declared and (2) to impose unconscionable prices for the rental or lease of a dwelling unit, including a motel or hotel unit or other temporary lodging or self-storage facility. A willful violation constitutes a misdemeanor punishable by a fine of not more than one thousand dollars or imprisonment for not more than thirty days. An "unconscionable price" is a price which either represents a "gross disparity" between the price of the covered commodity and the average price at which the covered commodity was available during the thirty days prior to the declaration of the state of emergency or that "grossly exceeds" the average price that was readily available for the covered commodities and services in the trade area thirty days prior to the declaration of the state of emergency. A price is not considered to be an "unconscionable price" if the increase is attributable to additional costs incurred or regional, national, or international market trends. See South Carolina Statute § 39-5-145, a copy of which is attached as Attachment I.

As mentioned, even without a declared emergency the Attorney General in South Carolina has the power to investigate and punish violations under the other sections of the Unfair Trade Practices Act, all civil in nature, which declares "unfair methods of competition and unfair or deceptive acts or practices in the conduct of any trade or commerce" unlawful. The Attorney General may recover, on behalf of the state, civil penalties not exceeding five thousand dollars per violation for willful violations. See South Carolina Statutes § 39-5-20 and § 39-5-110, copies of which are attached as Attachment II. But other than price gouging during a declared state of emergency, there are no statutes which specifically address "price gouging" in South Carolina. This makes

it difficult to prove price gouging, as the available statutory authority in non-emergency times is only the general prohibition against practices that are "unfair" or "deceptive", but which lacks a precise definition.

Under our competitive economic system, high prices or quick run-ups in prices are not and should not be illegal absent certain compelling circumstances. Taking risks and making a profit - or a loss - is the American way. To effectively fight true price gouging, however, we need authority to pursue price gougers in South Carolina when we are suffering an abnormal disruption of our market as the result of an event elsewhere. To this end, we are proposing an addition to South Carolina's price gouging statute which would apply to a direct and abnormal disruption in the market in South Carolina caused by an event happening outside of South Carolina which results in the governor of the other state, or the President, declaring a state of emergency or disaster. This approach recognizes the regional impacts of events and allows prosecutorial authorities to act quickly when unconscionable prices are being charged, without the necessity of a locally declared state of emergency. I believe such a law would have a salutary deterrent effect. See proposed amendment to South Carolina Statute § 39-5-145, a copy of which is attached as Attachment III. I see no need for additional federal legislation on these points.

Thank you for the opportunity to testify before this Committee on the topic of price gouging. I will be glad to respond to any questions.

ATTACHMENT 1

South Carolina's Price Gouging Statute

SECTION 39-5-145. Price gouging during emergency; definitions; penalty; evidence of knowledge or intent.

(A) As used in this section:

(1) "Commodity" means goods, services, materials, merchandise, supplies, equipment, resources, or other articles of commerce, and includes, without limitation, food, water, ice, chemicals, petroleum products, and lumber essential for consumption or use as a direct result of a declared state of emergency.

(2)(a) "Unconscionable price" means an amount charged, which:

(i) represents a gross disparity between the price of the commodity or rental or lease of a dwelling unit, including a motel or hotel unit or other temporary lodging, or self-storage facility that is the subject of the offer or transaction and the average price at which that commodity or dwelling unit, including a motel or hotel unit or other temporary lodging, or self-storage facility was rented, leased, sold, or offered for rent or sale in the usual course of business during the thirty days immediately before a declaration of a state of emergency, and the increase in the amount charged is not attributable to additional costs incurred in connection with the rental or sale of the commodity or rental or lease of the dwelling unit, including a motel or hotel unit or other temporary lodging, or self-storage facility, or regional, national, or international market trends; or

(ii) grossly exceeds the average price at which the same or similar commodity, dwelling unit, including a motel or hotel unit or other temporary lodging, or self-storage facility was readily obtainable in the trade area during the thirty days immediately before a declaration of a state of emergency, and the increase in the amount charged is not attributable to additional costs incurred in connection with the rental or sale of the commodity or rental or lease of the dwelling unit, including a motel or hotel unit or other temporary lodging, or self-storage facility, or regional, national, or international market trends.

b) It is prima facie evidence that a price is unconscionable if it meets the definition of item (i) or (ii).

(B)(1) Upon a declaration of a state of emergency by the Governor, it is unlawful and a violation of this article for a person or his agent or employee to:

(a) rent or sell or offer to rent or sell a commodity at an unconscionable price within the area for which the state of emergency is declared; or

(b) impose unconscionable prices for the rental or lease of a dwelling unit, including a motel or hotel unit or other temporary lodging, or self-storage facility within the area for which the state of emergency is declared.

(2) This prohibition remains in effect until the declaration expires or is terminated.

(C)(1) Upon a declaration of a state of disaster by the President, in which the disaster area includes all or a portion of the State of South Carolina, it is unlawful and a violation of this article for a person or his agent or employee in this State to:

(a) rent or sell or offer to rent or sell a commodity at an unconscionable price within the area for which the state of disaster is declared; or

(b) impose unconscionable prices for the rental or lease of a dwelling unit, including a motel or hotel unit or other temporary lodging, or self-storage facility within the area for which the state of disaster is declared.

(2) This prohibition remains in effect until the declaration expires or is terminated.

(D) A price increase approved by an appropriate government agency is not a violation of this section.

(E) This section does not apply to sales by growers, producers, or processors of raw or processed food products, except for retail sales of those products to the ultimate consumer within the area of the declared state of emergency or disaster.

(F) This section does not preempt the powers of local government, except that the evidentiary standards contained in this section are the sole evidentiary standards to be adopted by ordinance of a local government to restrict price gouging during a declared state of emergency or disaster. In the event a local government declares a state of emergency or disaster in which the disaster area includes all or a portion of the area under the local government's jurisdiction, and restricts price gouging during that emergency or disaster, the governmental entity must notify the Governor's Office of such declaration. The Governor's Office must notify registered agents simultaneously at the time of the declaration and also at the termination of the state of emergency.

(G) In addition to all other remedies provided in this article, a person who wilfully and knowingly violates this section is guilty of a misdemeanor and, upon conviction, must be punished by a fine of not more than one thousand dollars or imprisoned not more than thirty days.

(H) Any person who is charged with committing an action in violation of this section may present evidence relating to, but not limited to, his knowledge or intent when committing such action in order to rebut any presumption or evidence of violation of this section.

ATTACHMENT II

Selected Provisions of the South Carolina's Unfair Trade Practices Act

SECTION 39-5-20. Unfair methods of competition and unfair or deceptive acts or practices unlawful; application of interpretations of Federal act.

(a) Unfair methods of competition and unfair or deceptive acts or practices in the conduct of any trade or commerce are hereby declared unlawful.

(b) It is the intent of the legislature that in construing paragraph (a) of this section 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 (15 U.S.C. 45(a)(1)), as from time to time amended.

SECTION 39-5-110. Civil penalties for willful violation or violations of injunction.

(a) If a court finds that any person is willfully using or has willfully used a method, act or practice declared unlawful by Section 39-5-20, the Attorney General, upon petition to the court, may recover on behalf of the State a civil penalty of not exceeding five thousand dollars per violation.

(b) Any person who violates the terms of an injunction issued under Section 39-5-50 shall forfeit and pay to the State a civil penalty of not more than fifteen thousand dollars per violation. For the purposes of this section, the court of common pleas issuing an injunction shall retain jurisdiction, and the cause shall be continued and in such cases the Attorney General acting in the name of the State may petition for recovery of civil penalties. Whenever the court determines that an injunction issued pursuant to Section 39-5-50 has been violated, the court shall award reasonable costs to the State.

(c) For the purposes of this section, a willful violation occurs when the party committing the violation knew or should have known that his conduct was a violation of Section 39-5-20.

ATTACHMENT III

Revised Statute Proposed for Adoption in South Carolina Showing Proposed

Textual Changes

A BILL

TO AMEND SECTION 39-5-145, CODE OF LAWS OF SOUTH CAROLINA, 1976, RELATING TO PRICE GOUGING DURING A DECLARED STATE OF EMERGENCY OR DISASTER, SO AS TO PROHIBIT THE ACTS ALSO UPON AN OUT-OF-STATE DECLARATION OF A STATE OF EMERGENCY OR DISASTER RESULTING IN ABNORMAL DISRUPTION OF THE MARKET IN CERTAIN COMMODITIES WHEN THIS STATE IS AFFECTED.

Be it enacted by the General Assembly of the State of South Carolina:

SECTION 1. Section 39-5-145 of the 1976 Code, as added by Act 339 of 2002, is further amended to read:

“Section 39-5-145. (A) As used in this section:

(1) ‘Abnormal disruption of the market’ means a change in the market for a commodity in a part of South Carolina, whether actual or imminently threatened, resulting from stress of weather, forces of nature, failure or shortage of electric power or other source of energy, strike, civil disorder, or other cause that constitutes the basis for an out-of-state declaration.

(2) ‘Commodity’ means goods, services, materials, merchandise, supplies, equipment, resources, or other articles of commerce, and includes, without limitation, food, water, ice, chemicals, petroleum products, and lumber essential for consumption or use as a direct result of a declared state of emergency.

(3) ‘Out-of-state declaration’ means a declaration of a state of emergency, state of disaster, or similar declaration by the President of the United States or a governor of a state of the United States of America, other than the state of South Carolina.

~~(2)~~(4)(a) ‘Unconscionable price means an amount charged, which:

(i) represents a gross disparity between the price of the commodity or rental or lease of a dwelling unit, including a motel or hotel unit or other temporary lodging, or self-storage facility that is the subject of the offer or transaction and the average price at which that commodity or dwelling unit, including a motel or hotel unit or other temporary lodging, or self-storage facility was rented, leased, sold, or offered for rent or sale in the usual course of business during the thirty days immediately before a declaration of a state of emergency, and the increase in the amount charged is not attributable to additional costs incurred in connection with the rental or sale of the commodity or rental or lease of the dwelling unit,

including a motel or hotel unit or other temporary lodging, or self-storage facility, or regional, national, or international market trends; or

(ii) grossly exceeds the average price at which the same or similar commodity, dwelling unit, including a motel or hotel unit or other temporary lodging, or self-storage facility was readily obtainable in the trade area during the thirty days immediately before a declaration of a state of emergency, and the increase in the amount charged is not attributable to additional costs incurred in connection with the rental or sale of the commodity or rental or lease of the dwelling unit, including a motel or hotel unit or other temporary lodging, or self-storage facility, or regional, national, or international market trends.

(b) It is prima facie evidence that a price is unconscionable if it meets the definition of item (i) or (ii).

(B)(1) Upon a declaration of a state of emergency by the Governor, it is unlawful and a violation of this article for a person or his agent or employee to:

(a) rent or sell or offer to rent or sell a commodity at an unconscionable price within the area for which the state of emergency is declared; or

(b) impose unconscionable prices for the rental or lease of a dwelling unit, including a motel or hotel unit or other temporary lodging, or self-storage facility within the area for which the state of emergency is declared.

(2) This prohibition remains in effect until the declaration expires or is terminated.

(C)(1) Upon a declaration of a state of disaster by the President, in which the disaster area includes all or a portion of the State of South Carolina, it is unlawful and a violation of this article for a person or his agent or employee in this State to:

(a) rent or sell or offer to rent or sell a commodity at an unconscionable price within the area for which the state of disaster is declared; or

(b) impose unconscionable prices for the rental or lease of a dwelling unit, including a motel or hotel unit or other temporary lodging, or self-storage facility within the area for which the state of disaster is declared.

(2) This prohibition remains in effect until the declaration expires or is terminated.

(D) When an abnormal disruption of the market occurs, it is unlawful and a violation of this article for a person or his agent or employee to:

(1) rent or sell or offer to rent or sell a commodity at an unconscionable price in any area of this State where there is an abnormal disruption in the market; or

(2) impose unconscionable prices for the rental or lease of a dwelling unit, including a motel or hotel unit or other temporary lodging, or self-storage facility in any area of this State where there is an abnormal disruption in the market.

(E) A price increase approved by an appropriate government agency is not a violation of this section.

~~(E)(F)~~ This section does not apply to sales by growers, producers, or processors of raw or processed food products, except for retail sales of those products to the ultimate consumer within the area of the declared state of emergency or disaster.

~~(F)(G)~~ This section does not preempt the powers of local government, except that the evidentiary standards contained in this section are the sole evidentiary standards to be adopted by ordinance of a local government to restrict price gouging ~~during a declared state of emergency or disaster~~. In the event a local government declares a state of emergency or disaster or experiences an abnormal disruption of the market in which the ~~disaster~~ area includes all or a portion of the area under the local government's jurisdiction, and restricts price gouging during that ~~emergency or disaster~~ time, the governmental entity must notify the Governor's Office of ~~such the~~ declaration. The Governor's Office must notify registered agents simultaneously at the time of the declaration and also at ~~the termination of the state of emergency~~ its expiration or termination.

~~(G)~~(H) In addition to all other remedies provided in this article, a person who wilfully and knowingly violates this section is guilty of a misdemeanor and, upon conviction, must be punished by a fine of not more than one thousand dollars or imprisoned not more than thirty days, or both.

~~(H)~~(I) ~~Any~~ A person who is charged with committing an action in violation of this section may present evidence relating to, but not limited to, his knowledge or intent when committing ~~such~~ the action ~~in order~~ to rebut any presumption or evidence of violation of this section.”

SECTION 2. This act takes effect upon approval by the Governor.
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