Written Testimony of

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Before the

Senate Committee on Commerce, Science, and Transportation
Subcommittee on Consumer Protection, Product Safety, Insurance, and Data Security

Hearing on

"FTC Stakeholder Perspectives:
Reform Proposals to Improve Fairness, Innovation, and Consumer Welfare"

Washington, D.C.
September 26, 2017

INTRODUCTION

Mr. Chairman and Members of the Subcommittee: thank you for the opportunity to present testimony on FTC reform proposals. My name is Lydia Parnes and I am currently a Partner at Wilson Sonsini Goodrich & Rosati. Prior to that, I was the Director of the Bureau of Consumer Protection (BCP) at the Federal Trade Commission (FTC or Commission).

Earlier this year, the Section of Antitrust Law of the American Bar Association (the Section) submitted its Presidential Transition Report.[1] I am attaching a copy of this report along with my written testimony.[2] The Section's Presidential Transition Task Force was responsible for compiling this report and was comprised of a bi-partisan group of lawyers, professors, economists, and a federal appellate court judge with deep knowledge of, and extensive work with, the relevant issues and agencies. In fact, over half of the task force members have served in a senior leadership position with either the Commission or the Antitrust Division of the Department of Justice. As a member of this task force, I saw firsthand just how significantly the team's diverse backgrounds and experiences contributed to the crafting of this report.

This report presents the Section's views on the current state of federal consumer protection enforcement, as well as its recommendations regarding how the new administration could enhance that enforcement. As the Section recognizes, the FTC is a highly respected agency and, over the last several decades, its vigorous efforts in the area of consumer protection have been effective in

[1] American Bar Association, Section of Antitrust Law, Presidential Transition Report: The State of Antitrust Enforcement (January 2017), https://www.americanbar.org/content/dam/aba/publications/antitrust_law/state_of_antitrust_enforcement.authcheckdam.pdf [hereinafter Section Presidential Transition Report].

[2] As stated in the report, the views of the task force members were provided in their individual capacities and should not be attributed, in any way, to their law firms, clients or academic institutions, as applicable. *See* Section Presidential Transition Report, *supra* note 1, at 1 n.1. This written testimony sets out the Task Force recommendations as well as my own personal views.

protecting consumers and in halting unfair or deceptive acts or practices. The Section's thoughtful recommendations would build upon the FTC's excellent work to further refine the FTC's practices and processes. These recommendations are based on the task force's comprehensive experience with the agencies—and with subjects of FTC investigations—to pinpoint areas of concern and to identify practical means for improving results. These are important recommendations that deserve serious consideration.

Today I will highlight four specific areas where the task force made recommendations: (1) case selection; (2) civil investigative demands (CIDs); (3) information sharing in investigations; and (4) order provisions.

I. Case Selection

The FTC has broad prosecutorial discretion to select subjects for its enforcement actions—including which subjects to initially investigate and, subsequently, whether to bring a case or to close that investigation. As the Section notes, the FTC also has limited resources to conduct such investigations and litigations. Accordingly, the Section recommends the FTC focus its efforts on cases where significant consumer harm exists. While the Commission does bring many important cases involving serious consumer harm, the Section notes that, at times, the agency has also prosecuted small companies for technical violations where consumer harm was not apparent.[3] Such cases appear to underutilize the FTC's valuable assets, given the lack of meaningful consumer harm. They can also have extreme negative effects on small businesses that have more limited resources with which to respond to and defend such enforcement actions and may, as a result of such actions,

[3] The report mentions *In the matter of Nomi Techs., Inc*., Docket No. C-4538, 2015 WL 5304114 (F.T.C. Aug. 28, 2015), where dissenting Commissioners Ohlhausen and Wright criticized the majority's decision to bring the case given the technical nature of the violations and the absence of evidence of actual consumer harm. *See id.* at *5, *8.

lose the financing, customers, and business relationships they depend upon for their continued viability.

II. Civil Investigative Demands (CIDs)

A typical FTC investigation begins with the issuance of a civil investigative demand (CID), which compels the subject to submit written responses, documents, and other information and materials to the Commission. CIDs are an important component of the FTC's investigative process. Responding to a CID, however, can be exceptionally costly and burdensome to a company under investigation. The Section thus recommends the Commission act more judiciously in crafting and issuing CIDs to companies and individuals to avoid imposing unnecessary costs. Specifically, the Section suggests the Commission issue more narrowly focused initial CIDs, leaving open the option to issue follow up CIDs if needed.

These recommendations are largely a response to the Commission's tendency to issue overly-broad CIDs, which are not tailored to the company or conduct under investigation. While the Commission needs some leeway in composing CIDs to ensure the necessary information and materials are covered—particularly when the Commission is unfamiliar with how the company creates and stores its records—the Commission has tended to issue CIDs that go beyond merely affording the Commission this leeway and leave the subject both confused as to the potential theories being investigated and facing a substantial burden in terms of its response.[4] In fact, the legal fees alone, which subjects incur to negotiate scope with the Commission and then to make the productions, can be prohibitive. These costs are compounded by strict production requirements the FTC often imposes. These requirements may vary significantly depending on how a subject stores

[4] As the Section explained, some CIDs demand all information that could potentially relate to violations of essentially every consumer protection law that could possibly apply. Section Presidential Transition Report, *supra* note 1, at 29 n.91.

its records in the ordinary course, and thus require the subject to retain an expensive vendor to make the required production.

The trend toward broader CIDs is also problematic because respondents have limited means to narrow the scope. If the Commission does not willingly agree to modifications, the respondent can file a petition to quash or limit a CID. But these petitions are made public, which imposes considerable reputational costs on the investigative targets. For smaller businesses, in particular, these reputational costs can be significant and even life-threatening.

Acting Chairman Maureen K. Ohlhausen recently acknowledged these (and other) procedural issues, and established new internal Working Groups on Agency Reform and Efficiency to investigate the causes of such issues and to identify potential solutions. This summer, the Commission announced process reforms concerning consumer protection CIDs, some of which seem directly to respond to the Section's recommendations.[5] For instance, the reforms include "[a]dding more detailed descriptions of the scope and purpose of investigations to give companies a better understanding of the information the agency seeks," and "[w]here appropriate, significantly reducing the length and complexity of CID instructions for providing electronically stored data." Such procedural changes have the potential to significantly reduce the burden of responding to CIDs without negatively impacting the FTC's ability to obtain the necessary information. I would urge the Subcommittee and the Commission to consider steps to make these reforms permanent and to address other issues raised in the report, such as by permitting companies to file confidential petitions to challenge overly broad CIDs.

[5] Press Release, U.S. Fed. Trade Comm'n, Acting FTC Chairman Ohlhausen Announces Internal Process Reforms: Reducing Burdens and Improving Transparency in Agency Investigations (July 17, 2017), https://www.ftc.gov/news-events/press-releases/2017/07/acting-ftc-chairman-ohlhausen-announces-internal-process-reforms.

III. Information Sharing in Investigations

Information sharing is critical in Commission investigations. The information shared by a company being investigated helps the FTC to discern whether a violation has occurred. At the same time, if the FTC shares its concerns, the company can better understand what is being investigated and what information and defenses are relevant. The extent to which the FTC staff actually reveals its theories and concerns, however, varies significantly from case to case.

In cases where the staff engage in open discussions early on regarding what it is investigating, there is more opportunity for both sides to explore the issues and test their theories. Open communication leads to sounder outcomes, as both sides have real opportunities to present evidence and see how that evidence does—or does not—align with the Commission's theories of harm. On the flip side, in cases where the staff does not disclose its theories to the respondent or inform the respondent of what evidence allegedly supports its theories, the respondent is left at a serious disadvantage in defending its conduct. Moreover, this lack of information sharing can undermine the investigative process itself. If the respondent does not know what the Commission's legal theory is, it cannot subject this theory to its best defenses. Thus, while the goal of the investigative process is to analyze the facts to understand whether a violation has occurred, not sharing the underlying theory and the evidence allegedly supporting it effectively short-circuits a thorough factual and legal analysis.

Creating open lines of communication begins with the CID's issuance, as noted. The clearer the CID is regarding the Commission's intent, the more responsive the subject can be from the outset. To this end, the Commission's recent process reforms are likely to enhance information sharing efforts. But information sharing should not stop here. The FTC's theories and concerns are likely to

evolve as they receive more information. Keeping respondents informed of these changes is key to reaching thoughtful outcomes supported by the full set of evidence.

To improve communication between the Commission and parties in a consistent fashion, the Section recommends that the FTC adopt internal guidelines for staff to follow in communicating with respondents. The Section suggests that, beginning as early as possible, the staff should be as transparent as possible and encourage open dialogue regarding their substantive concerns (absent compelling circumstances suggesting otherwise, such as clear bad faith by the respondent). These recommendations would both improve the fairness of the process and help the Commission reach better supported decisions.

IV. Order Provisions

The terms the Commission includes in its consent orders are of critical importance. Realistically, a company may not have the resources or capacity to litigate, and—to a large extent—the Commission relies on consent orders to resolve investigations. Consent order terms that are unduly restrictive may do more harm than good and, compounding this problem, may gain the mantle of precedent over time, making appropriate modifications increasingly unlikely. As such, consent orders should be carefully crafted. The Section offers some specific proposals to assist in this effort.

First, the Section recommends reducing the burden of "boilerplate" provisions. The Commission has established a number of administrative provisions that it reuses in the same or substantially similar terms in each consent order. While this practice can expedite the negotiation process, inappropriately broad terms can impose unnecessary costs. For instance, since 1996 the Commission has required companies entering consent decrees to agree to administrative orders

lasting 20 years and federal court orders lasting in perpetuity.[6] This practice does not account for the nature of the underlying market, nor for how quickly that market might be changing. Accordingly, it may unnecessarily constrain the company's ability to react to competitive changes or consumer demands, particularly when coupled with the "fencing in" provisions and other burdensome affirmative obligations that the Commission routinely includes in consent orders.[7] The Section therefore recommends the FTC adopt a sunset period of around 5 years for both administrative and district court orders, allowing upward deviation for extenuating circumstances such as fraud or recidivism.

Relatedly, the Section recommends the FTC reconsider its standard implementation of "Scofflaw" provisions, to alleviate their burdensome requirements for respondents operating legitimate businesses. Scofflaw provisions include requirements such as distributing the order to various individuals, keeping records, reporting changes (like asset sales, mergers, or bankruptcy), and filing compliance reports, that typically last between 3 and 20 years. Federal court boilerplate Scofflaw provisions often go beyond the Commission's standard ones, including by providing the FTC the right to gather information from the respondent in various ways that can be very burdensome. Federal court orders, for instance, often allow the Commission to contact the

[6] *See* Press Release, U.S. Fed. Trade Comm'n, FTC Rule Incorporating Sunset Policy for Existing Administrative Orders in Consumer Protection and Antitrust Cases (Nov. 20, 1995), https://www.ftc.gov/news-events/press-releases/1995/11/ftc-rule-incorporating-sunset-policy-existing-administrative. The Commission justified keeping federal court orders unlimited because "many of these orders are against defendants involved in hard-core fraud." *Id.*

[7] The FTC typically includes "fencing-in" relief in its consumer protection orders, which is relief that stretches beyond violations identified in the Commission's complaint to reach allegedly related practices. For instance, in matters involving unsubstantiated claims regarding health benefits, the Commission typically imposes a term requiring scientific substantiation for any claim about the health benefits, efficacy, or performance of any food, drug, or dietary supplement. *See e.g.*, POM Wonderful v. FTC, 777 F.3d 478, 505 (D.C. Cir. 2015). This often leaves the respondent with much confusion and uncertainty regarding which implied claims the Commission might find in future advertising or what substantiation it would find sufficient. Other burdensome affirmative obligations the FTC requires include, for data security matters, expensive biennial security audits. *See e.g.*, *In the Matter of* Snapchat, Inc., Docket No. C-4501, 2014 WL 1993567, at *14 (F.T.C. May 8, 2014).

respondent directly—not through counsel—regarding order-related matters, which contradicts longstanding ethical rules prohibiting such conduct.[8] While such terms were originally intended to permit proper oversight when defendants behaved fraudulently, the FTC has increasingly filed cases in federal court in non-fraud cases, but continued to incorporate these onerous terms. This practice imposes unnecessary costs on respondents and should be reconsidered.

Second, the Section recommends tying monetary relief more closely to critical issues including the nature of the violation, the extent of consumer injury, and the culpability of the respondent. In recent years, the Commission has increasingly sought significant monetary relief, including civil penalties, restitution, and/or disgorgement, in Section 5 cases that do not involve fraud or tangible consumer injury. This marks a departure from the Commission's prior practices, in which it sought restitution or disgorgement tethered to injury or unjust enrichment that was traceable to the violation(s). More recently, the staff has sought monetary relief even when violations are marginal, technical, or unintentional and the injury is minimal or nonexistent—and it often seeks the maximum possible amount regardless of the underlying facts or litigation risks.

These changes to FTC practice inappropriately penalize respondents beyond what is necessary to deter the same or similar conduct. They also create unnecessary uncertainty, as the respondents cannot rely on *ex ante* calculations as to the costs of the conduct at issue to estimate likely fines. Consider, for instance, that the public perceives larger fines as indicative of more egregious conduct, and reasonably judges the respondent according to this perceived level of misconduct. By detaching fines from actual wrongdoing, the Commission creates a situation in

[8] *See* AM. BAR ASS'N, MODEL RULES OF PROF'L CONDUCT, R. 4.2 (2014) ("In representing a client, a lawyer shall not communicate about the subject of the representation with a person the lawyer knows to be represented by another lawyer in the matter, unless the lawyer has the consent of the other lawyer or is authorized to do so by law or a court order.").

which the public is judging a respondent more harshly—potentially significantly so—than is warranted. The Section's recommendations would help realign the costs, both monetary and reputational, to the misconduct and harm identified. These recommendations, moreover, mirror the FTC's prior statement on monetary relief, including disgorgement and restitution, in competition cases, which was unanimously adopted but is not in effect today.[9]

CONCLUSION

The Section's Presidential Transition Report offers numerous recommendations for enhancing the FTC's consumer protection enforcement processes and outcomes. These recommendations would alleviate unnecessary burdens on businesses while facilitating better FTC decisions and outcomes.

Thank you for your time. I would be happy to answer any questions.

[9] U.S. Fed. Trade Comm'n, Policy Statement on Monetary Equitable Remedies – Including in Particular Disgorgement and Restitution – in Federal Trade Commission Competition Cases Addressing Violations of the FTC Act, the Clayton Act, or the Hart-Scott-Rodino Act (July 31, 2003), https://www.ftc.gov/public-statements/2003/07/policy-statement-monetary-equitable-remedies-including-particular. This statement established, for instance, that the FTC would seek disgorgement only where (1) the underlying violation was clear, and (2) there was a reasonable basis for calculating the payment amount, and (3) it would take into account the other remedies available, including private actions and criminal proceedings. The FTC withdrew this statement less than 10 years after unanimously adopting it, finding it "overly restrictive." Press Release, U.S. Fed. Trade Comm'n, FTC Withdraws Agency's Policy Statement on Monetary Remedies in Competition Cases; Will Rely on Existing Law (July 31, 2012), https://www.ftc.gov/news-events/press-releases/2012/07/ftc-withdraws-agencys-policy-statement-monetary-remedies.