

## Interpreting Abusive Practices

William MacLeod<sup>1</sup>

I was director of the Bureau of Consumer Protection at the Federal Trade Commission in the 1980s, a period that one scholar called the era of unfairness at the FTC.<sup>2</sup> The characterization was not a criticism of the Commission's decisions but a commentary on the successful enforcement of its most ambitious, and ambiguous, authority — the prohibition of unfair acts and practices in the FTC Act (FTCA). The Commission brought cases to stop companies from such practices as breaching their contracts with consumers,<sup>3</sup> imposing onerous clauses in contracts,<sup>4</sup> failing to disclose fire hazards in farm equipment,<sup>5</sup> and failing to disclose automobile recalls in rental cars.<sup>6</sup> These and other initiatives marked a resurgence of authority that almost died – and threatened to take the Commission with it – when the decade began.

Some of the Commissions major historical accomplishments came from the unfairness prong of Section 5, which was added to the FTCA in 1938.<sup>7</sup> Unfairness was the legal basis for the first proceedings to require health warnings on cigarettes, which precipitated the legislation that accomplished the same.<sup>8</sup> It was the authority the Commission used to prevent products that could injure kids from being delivered in media that appealed to them. It justified the Commission's ruling that advertising claims not only be truthful, but also substantiated by evidence.

Major accomplishments every now and then were not enough to satisfy the demands for a more forceful Federal Trade Commission. By the late 1960s, consumerism had matured into a potent force. Nader's Raiders issued a scathing critique of the FTC.<sup>9</sup> It was the natural agency to

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<sup>1</sup> Partner, Kelley Drye & Warren LLP.

<sup>2</sup> Stephen Calkins, *FTC Unfairness: An Essay*, 46 WAYNE L. REV. 1935 (2000).

<sup>3</sup> Orkin Exterminating Co., Inc., 1985 F.T.C. LEXIS 61 (1984); *Orkin Exterminating Co. v. FTC*, 849 F.2d 1354, 1355-56 (11th Cir. 1988), *cert. denied*, 488 U.S. 1041 (1989).

<sup>4</sup> J.C. Penney, Inc., 109 F.T.C. 54 (1987).

<sup>5</sup> Int'l Harvester Co., 104 F.T.C. 949 (1980).

<sup>6</sup> Budget Rent a Car Corp., 113 F.T.C. 1109 (1990).

<sup>7</sup> Federal Trade Commission Act Amendments of 1938 (Wheeler-Lea Act), Pub. L. No. 75-447, 52 Stat. 111.

<sup>8</sup> Unfair or Deceptive Advertising and Labeling of Cigarettes in Relation to the Health Hazards of Smoking, Statement of Basis and Purpose, 28 Fed. Reg. 8355 (1964) ("Cigarette Rule").

<sup>9</sup> Edward F. Cox et al., "The Nader Report" on the Federal Trade Commission (1969).

implement a consumer agenda, but it had repeatedly failed to advance it in their view. A task force of the American Bar Association weighed in with similar doubts about its contributions.<sup>10</sup> The Nixon administration responded with appointments of distinguished Chairmen and Commissioners,<sup>11</sup> and the agency embarked on a mission to improve the performance of entire sectors of the economy.

Bolstered by the Supreme Court, which ruled that the agency possessed almost unlimited power to declare practices unfair,<sup>12</sup> the Commission proposed rules to regulate food advertising to kids, to mandate warranties on used cars, to preempt the Uniform Commercial Code in credit transactions, to prescribe advertising for vocational schools, and more. Commission officials hinted at even more creative enforcement. They floated ideas like declaring unfair such practices as hiring undocumented immigrants and failing to diversify corporate boards. The Commission gained the reputation as the second most powerful legislature in the United States.

It didn't last. Large and small businesses complained to Congress.<sup>13</sup> Opinion leaders piled on the agency, including the Washington Post, which called the Commission a "National Nanny."<sup>14</sup> By the end of the decade, protests by constituents prompted Congress to close the Commission (a targeted precursor to the wider shutdowns we have seen recently). Chagrined Commission leaders found themselves in the Oval Office, where the President had to mediate a deal that persuaded the

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<sup>10</sup> Am. Bar Ass'n, Report of the ABA Commission to Study the Federal Trade Commission (1969).

<sup>11</sup> Fed. Trade Comm'n, The FTC During the Administrations of Richard Nixon (1969-74) and Gerald R. Ford (1974-77), <https://www.ftc.gov/reports/ftc100-bibliography/1969-1977>.

<sup>12</sup> *FTC v. Sperry & Hutchinson Co.*, 405 U.S. 233, 245 (1972) (holding "Federal Trade Commission does not arrogate excessive power to itself if, in measuring a practice against the elusive, but congressionally mandated standard of fairness, it, like a court of equity, considers public values beyond simply those enshrined in the letter or encompassed in the spirit of the antitrust laws.").

<sup>13</sup> See, e.g., Michael Pertschuk, REVOLT AGAINST REGULATION: THE RISE AND PAUSE OF THE CONSUMER MOVEMENT (1982).

<sup>14</sup> *The FTC as a National Nanny*, The Washington Post (Mar. 1, 1978), [https://www.washingtonpost.com/archive/politics/1978/03/01/the-ftc-as-national-nanny/69f778f5-8407-4df0-b0e9-7f1f8e826b3b/?noredirect=on&utm\\_term=.e78356768169](https://www.washingtonpost.com/archive/politics/1978/03/01/the-ftc-as-national-nanny/69f778f5-8407-4df0-b0e9-7f1f8e826b3b/?noredirect=on&utm_term=.e78356768169).

Congress to reopen the agency.<sup>15</sup> Congress relented, in exchange for a promise from the Commission to wield its powerful unfairness weapon with more reason and predictability. The Unfairness Policy Statement of 1980<sup>16</sup> was the down payment on that promise. Forty years after unfairness had been added to the FTCA, prosecutors who enforced the law, judges who interpreted it, and companies that had to follow it understood what it meant.

Unfairness was not the only aspect of the Commission's authority that had divided commissioners and confused constituents. The elements of deception and substantiation were likewise unclear. Was an obviously false claim that misled nobody but a fool deceptive? What about a claim that targeted a vulnerable audience? How much evidence did an advertiser need to substantiate a claim? The Commission answered these questions with policy statements on deception and substantiation, which became law when they were adopted in Commission decisions and widely accepted in the courts.<sup>17</sup>

The controversies surrounding the Commission's unfairness authority may sound familiar to those who followed the debates over Dodd-Frank and the addition of abusive practices to the prohibitions in the CFPB's enforcement arsenal. The similarities should come as no surprise. Unfairness was not the first example. Abusive is unlikely to be the last.

When the Sherman Antitrust Act became law in 1890, it literally banned commercial contracts – “[e]very contract...in restraint of trade or commerce ...is declared to be illegal.”<sup>18</sup> Of course, the

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<sup>15</sup> William C. MacLeod & Robert A. Rogowsky, Consumer Protection at the FTC during the Reagan Administration, in REGULATION AND THE REAGAN ERA: POLICY, BUREAUCRACY AND THE PUBLIC INTEREST (Roger E. Meiners & Bruce Yandle eds., 1989).

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<sup>16</sup> FTC Policy Statement on Unfairness (Dec. 17, 1980), Appended to Int'l Harvester Co., 104 F.T.C. 949, 1070 (1984), <https://www.ftc.gov/public-statements/1980/12/ftc-policy-statement-unfairness>.

<sup>17</sup> FTC Policy Statement on Deception (Oct. 14, 1983), Appended to Cliffdale Associates, Inc., 103 F.T.C. 110, 174 (1984), <https://www.ftc.gov/public-statements/1983/10/ftc-policy-statement-deception>; FTC Policy Statement Regarding Advertising Substantiation (Mar. 11, 1983), 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), <https://www.ftc.gov/public-statements/1983/03/ftc-policy-statement-regarding-advertising-substantiation>.

<sup>18</sup> 15 U.S.C. § 1.

purpose of every commercial contract is to restrain trade, whether it is an agreement to repair a car or sell a company. Courts had to do some quick judicial amending to make sense of the Act or preside over paralyzed commerce. Judge Taft (before he was president of the United States and Chief Justice of the Supreme Court) added the Rule of Reason in 1898 in *Addyston Pipe and Steel*.<sup>19</sup> The Supreme Court elaborated on the doctrine, which became known as the Rule of Reason, in 1911 in *Standard Oil v. United States*.<sup>20</sup>

These developments generated their own controversy and resulted in legislation that created the FTC. Concerned that the courts had added too much reason to the Sherman Act, Congress responded with the FTC Act and its unfair methods of competition. To this day, we are debating the contours of the rule of reason and unfair methods of competition. After a century of enforcement, the Commission issued a policy statement on unfair methods, but the Commissioners could not agree on the specifics of what those methods encompassed.<sup>21</sup> The debate will continue to play out in speeches, articles, opinions, and orders.

There is reason for hope that the CFPB can give meaningful substance to abusive practices more quickly than the forty years it took the FTC to come to terms with unfairness, or the century (and counting) it has taken the courts and the FTC to explicate illegal restraints of trade and unfair methods of competition. This comment outlines some challenges, some means to surmount them, and a brief reminder of what is at stake if the definition of abusive practices is not harmonized with standards in comparable statutes regulating commercial activity.

The CFPB has a head start. It has already taken advantage of the FTC's interpretations of unfairness and deception.<sup>22</sup> And to the credit of the Dodd-Frank drafters, abusive practices already incorporates materiality and reasonableness:

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<sup>19</sup> *United States v. Addyston Pipe & Steel Co.*, 85 F. 271, 279-84 (6th Cir. 1898), *aff'd*, 175 U.S. 211 (1899).

<sup>20</sup> *Standard Oil Co. v. United States*, 221 U.S. 1, 61-68 (1911).

<sup>21</sup> Release, FTC Issues Statement of Principles Regarding Enforcement of FTC Act as a Competition Statute (Aug. 13, 2015), <https://www.ftc.gov/news-events/press-releases/2015/08/ftc-issues-statement-principles-regarding-enforcement-ftc-act>.

<sup>22</sup> See, e.g., CFPB Bulletin 2013-07 (July 10, 2013), [https://files.consumerfinance.gov/f/201307\\_cfpb\\_bulletin\\_unfair-deceptive-abusive-practices.pdf](https://files.consumerfinance.gov/f/201307_cfpb_bulletin_unfair-deceptive-abusive-practices.pdf).

An act or practice is abusive when it:

- (1) Materially interferes with the ability of a consumer to understand a term or condition of a consumer financial product or service; or
- (2) Takes unreasonable advantage of –
  - (A) a consumer’s lack of understanding of the material risks, costs, or conditions of the product or service;
  - (B) a consumer’s inability to protect his or her interests in selecting or using a consumer financial product or service; or
  - (C) a consumer’s reasonable reliance on a covered person to act in his or her interests.<sup>23</sup>

Thus there is reason for optimism that the CFPB and the courts can avoid setting sail on the sea of doubt that bedeviled antitrust enforcement in its early days.<sup>24</sup> Instead, one hopes that sessions like today’s Symposium can give the Bureau some lodestars to chart a course that allows the prohibition against abusive practices to reign in conduct that is harmful to consumers without stifling competition or depriving consumers of services that they value.

At stake in the interpretation of abusive practices is more than the setback the FTC faced when its daring deployment of unfairness backfired in the 1970s. When an authority prohibits practices without assessing their costs and benefits, it runs the risk of doing net harm to the economy, and to consumers who expect protection, not harm, from consumer protection laws.

The risks are real. The Bureau’s Brian Johnson eloquently recounted the potential consequences of overreach in the regulation of markets for financial goods and services.<sup>25</sup> A trenchant dissent by a D.C. Circuit judge did the same.<sup>26</sup> This comment will not recount those observations. What has not been documented to our knowledge is what lawyers in the space are seeing from the

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<sup>23</sup> Dodd-Frank Act § 1031(d), 12 U.S.C. 5531(d).

<sup>24</sup> See *Addyston Pipe* at 283-84 (“courts, mistaking . . . the proper limits of the relaxation of the rules for determining the unreasonableness of restraints of trade, have set sail on a sea of doubt. . . .”)

<sup>25</sup> Brian Johnson, Toward a 21st century approach to consumer protection, Remarks to Consumer Action (as prepared for delivery) (Nov. 15, 2018), <https://www.consumerfinance.gov/about-us/newsroom/toward-21st-century-approach-consumer-protection/>.

<sup>26</sup> See *Am. Fin. Servs. Ass’n v. FTC*, 767 F.2d 957 (D.C. Cir. 1985) (Tamm, J., dissenting).

counseling we do every day. Marketers are thinking twice about extending credit to consumers of limited means. Extending credit is risky enough with customers whose financial resources don't match those of affluent consumers. When the risks are compounded by onerous regulation or the prospect of prosecution when borrowers cannot meet their obligations, lenders and marketers have extra incentives to shy away.

Competition can suffer as well. It was no surprise to financial firms when the CFPB observed that the Mandatory Underwriting Provisions in the 2017 Final Rule governing Payday, Vehicle Title, and Certain High-Cost Installment Loans "would have the effect of restricting access to credit and reducing competition for these products."<sup>27</sup> Companies fearing disapproval of the CFPB have questioned their relations with financial service providers that offer alternatives to traditional providers. This is a recipe for barriers to entry. In short, reductions in competition can undermine consumer protection.

The legislative history to Dodd-Frank and the Consumer Financial Protection Act (CFPA) bears striking similarities to the history of competition and consumer protection laws. Supporters of the legislation claimed that more authority was needed after the financial crisis to address the "failure of federal regulators to stop abusive lending, particularly unsustainable home mortgage lending."<sup>28</sup> As one court put it, "[t]he legislative history of the CFPA suggests that the term [abusive] was added, in part, to enable the Bureau to reach forms of misconduct not embraced by the more rigid, cost-benefit standard that had grown up around the terms 'unfair' and 'deceptive.'"<sup>29</sup> This is an *S&H*<sup>30</sup> invitation to the CFPB.

Missing from the debate was a reasonable basis for the proposition that authority was needed to untether abuse from a cost-benefit analysis. Plentiful in the debate were misunderstandings as to what unfairness required - dollar damages, economic harm, unnecessary analysis. Also plentiful

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<sup>27</sup> Notice of proposed rulemaking, Payday, Vehicle Title, and Certain High-Cost Installment Loans, Docket No. CFPB-2019-0006, available at [https://files.consumerfinance.gov/f/documents/cfpb\\_payday\\_nprm-2019-reconsideration.pdf](https://files.consumerfinance.gov/f/documents/cfpb_payday_nprm-2019-reconsideration.pdf).

<sup>28</sup> S. Rep. No. 111-176 (2010), <https://www.congress.gov/congressional-report/111th-congress/senate-report/176>.

<sup>29</sup> *Consumer Fin. Prot. Bureau v. ITT Educ. Servs., Inc.*, 219 F.Supp. 3d 878, 904 (S.D. Ind. 2015).

<sup>30</sup> *FTC v. Sperry & Hutchinson Co.*, 405 U.S. 233, 245 (1972).

were assertions that consumers would be better off if businesses or regulators took consumer choice into their own hands. None of these arguments or assertions makes sense without cost-benefit analysis. What does it mean to “materially interfere with the ability of a consumer to understand a term or condition of a consumer financial product or service,” or to “take unreasonable advantage of a lack of understanding on the part of the consumer of the material risks, costs, or conditions of the product or service”?<sup>31</sup> Virtually all examples that have survived review are those that failed the cost benefit test. Tellingly, the CFPB’s October 2012 Examination Procedures on its UDAAP Authority provide examples of deception and unfairness – adding to the plethora of examples from FTC enforcement – yet the Examination Procedures provide no examples of “abusive” acts and practices.

A review of how the CFPB has used its abusive authority to date is not particularly helpful in providing meaningful guidance to industry. One simple truth I have learned over the course of my legal career is that lawyers want to win – both on the affirmative and the defensive side. Litigation tactics can take a case down detours agency never anticipated when the action began. Complaint counsel are reluctant to concede limits on an agency’s authority.<sup>32</sup> Defense counsel are eager to argue for limits that Congress never intended.<sup>33</sup> Not surprisingly, regulators typically bring enforcement actions they can win and frame allegations in a manner that is not easily challenged – often resulting in outcomes that don’t provide others with clear guidance.

In the context of CFPB enforcement, this has often translated into complaints that include factual assertions and then summary allegations that conduct is unfair, deceptive, and/or abusive – without a thorough analysis of how each prong of each standard is met. For example, in its 2015 complaint against NDG Financial Corp, the Bureau alleged that defendant violated the CFPA by originating, servicing, and collecting on payday loans that were void in whole or in part under certain state laws.<sup>34</sup> The complaint alleged different counts for deception, unfairness, and abusiveness relating to “the collection of loan payments that consumers did not owe” – each of which effectively

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<sup>31</sup> Dodd-Frank Act §1036(a)(1)(B), 12 U.S.C. § 5536(a)(1)(B).

<sup>32</sup> See, e.g., *FTC v. Shire Viropharma Inc.*, 917 F.3d 147 (3d Cir. 2019).

<sup>33</sup> See, e.g., *FTC v. Wyndham Worldwide Corp.*, 799 F.3d 236 (3d Cir. 2015).

<sup>34</sup> *Consumer Fin. Prot. Bureau v. NDG Fin. Corp.*, Case No. 15-cv-05211 (S.D.N.Y. Dec. 11, 2015).

restated the applicable statutory standard, and which presumably satisfied the respective definitions of deception and unfairness.

The CFPB has brought actions limited to its “abusive” authority in only a few circumstances – and in each of these cases it’s not clear that the Bureau could not have instead brought an unfairness count by also including allegations related to a cost-benefit analysis. For example, in an action against Aequitas Capital Management, the Bureau alleged that the company funded a private student loan program offered to Corinthian Colleges, Inc. students as part of a scheme to allow Corinthian to present a facade of compliance with federal laws requiring that a certain portion of a for-profit school's revenue come from sources other than federal student aid.<sup>35</sup> In its action against Zero Parallel, the CFPB alleged that the company engaged in abusive acts by providing leads for loans that it knew would be partially or wholly void under state law – an action that sounds a lot like the case against NDG Financial that included deception and unfairness counts as well.<sup>36</sup>

The point here is that it is not clear that this conception of abusiveness untethered to any cost-benefit analysis is even being used. Yet clients continue to tell us that the ambiguity surrounding the authority contributes to regulatory uncertainty that results in certain products and services being curtailed or not offered to certain populations altogether.

Simply adding some certainty and predictability to the abusiveness standard could yield significant benefits. There should be no need to cite authority for the proposition that uncertainty is an impediment to investment and innovation. When uncertainty applies to the legality of a business practice, the reaction in markets is predictable. Legitimate businesses shy away. If there is a demand for the suppressed service, shady characters, con artists, thugs, and crooks fill the void. That is when consumer protection puts consumers in peril.

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<sup>35</sup> *Consumer Fin. Prot. Bureau v. Aequitas Capital Mgmt., Inc.*, No. 3:17-cv-01278-MO (D. Or. Aug. 17, 2017).

<sup>36</sup> Zero Parallel, LLC, 2017 CFPB 0017 1 (Sept. 9, 2017).