

# Client Alert

Latham & Watkins  
Advertising and Marketing Regulation Group

## Federal Trade Commission Reviews Guidelines for Environmental Marketing Claims

The US Federal Trade Commission (FTC) is reviewing its guidelines regarding environmental marketing claims (the Green Guides), 16 CFR Part 260. These guides, originally issued in 1996, have become more significant recently as the number of these types of claims increase. Environmental marketing claims can be very effective. The FTC has noted market research showing that more than 75 percent of the public will switch to a brand associated with the protection of the environment when price and quality are equal. Surveys show that nearly 60 percent of the public favors organizations that support the environment. These facts about consumer behavior suggest that environmental claims are likely to continue to play a major role in the marketplace. This *Client Alert* discusses the FTC's approach to claims relating to greenhouse gas emissions, "carbon offsets" and Renewable Energy Certificates (RECs).

### Background: the Green Guides

The Green Guides indicate how the FTC applies general advertising regulation principles to environmental marketing claims. Like any deceptive claim, an environmental marketing

claim violates Section 5 of the FTC Act if it misleads reasonable consumers about a material fact. The claim may be deceptive because it expressly misstates a fact or because it fails to disclose a material fact.<sup>1</sup> In addition, a claim that is sufficiently specific must be substantiated when the claim is made. According to the Green Guides, "[A]ny party making an express or implied claim that presents an objective assertion about the environmental attribute of a product, packaging or service must, at the time the claim is made, possess and rely upon a reasonable basis substantiating the claim."<sup>2</sup>

Environmental claims often use phrases that do not have a precise meaning. For example, ads may include the terms "recyclable," "environmentally safe" and "biodegradable." Each of these terms can make a product more appealing to consumers. Yet, each of the terms may be used deceptively if the actual attributes of the product do not correspond to how most consumers interpret these terms. The Green Guides contain many examples illustrating how the FTC assumes reasonable consumers interpret a claim. An advertiser must have substantiation that is consistent with such interpretations. For example, the Green Guides state that an unqualified claim that a product

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is “biodegradable” means that the advertiser must have “competent and reliable scientific evidence that the entire product or package will completely break down and return to nature...within a reasonably short time after customary disposal.”<sup>3</sup> Unless products meet this demanding test, advertisers should qualify the claim.

## **Carbon Neutral, Carbon Offset and REC Claims**

One category of claims of particular interest to the FTC are claims about the seller’s impact on greenhouse gas emissions. These can take a variety of forms, ranging from a claim that a seller is “carbon neutral” to a claim that a seller’s products are made with “green” energy. In these cases, the seller wants to make its product more attractive by suggesting that it does not have a harmful effect on the environment.

Two devices are often used to justify claims relating to greenhouse gas emissions—“carbon offsets” and renewable energy certificates or “RECs.” A claim based on a carbon offset means that a company is claiming to have reduced overall carbon emissions, indirectly rather than directly, by engaging in, or arranging, for activities that reduce carbon emissions. For example, a company may pay for landfill methane collection activities or tree planting that offsets some or all of the emissions it generates in its production process.

RECs generally refer to certificates that designate power as having come from a renewable source. Consumers may purchase the equivalent of RECs in order to feel that they are “carbon neutral.” For example, the Pacific Gas & Electric Company’s “ClimateSmart”™ program allows consumers to pay a separate amount on their utility bills to mitigate the carbon dioxide emissions equivalent associated with their energy use.

The public’s concern about global warming means that these types of claims can be quite effective in encouraging consumers to buy a product or service from the advertiser. On the other hand, the complexity of these transactions and the potential ambiguous meaning of certain terms mean that the claims can be misleading or deceptive. For example, one particular type of carbon offset claim is a “renewable energy” claim. Claims about relying on “renewable energy” can be important to businesses that want to convey to consumers that their energy use is not contributing to an increase in fossil fuel emission. In general, “renewable electricity” refers to power generated from non-fossil fuel sources, such as wind and solar power.

In some cases, business can purchase “renewable electricity” directly from these sources. If they do, they would be entitled to make an advertising claim that their operations are based on “renewable power” or “renewable electricity.” As a practical matter, however, most businesses buy power from their local utility and the power comes from the local power grid. If the utility obtains a certain portion of its power from renewable sources, the utility can attribute the purchase of this power to a customer willing to pay a premium. If the customer has arranged for a sufficient amount of renewable power to be allocated to it, it can make a claim that it operates with renewable electricity.

A more complex variation of this arrangement occurs when electricity generators obtain some of their power from renewable sources but sell all of their power in the home market at the same price. In this case, they may sell RECs to electricity users in other market that want to claim that they are using renewable energy.

### **Deceptive Claims**

The complexity of these transactions and the potential ambiguity of advertising claims in this area mean that there is significant potential for advertisers to make claims that are misleading or unsubstantiated. These advertisers include both companies that market products to consumers and power generators that “market” their use of renewable energy to retail users of power. We discuss below two particular problems in the following text.

### **Failure to Substantiate a Claim**

Any advertising claim that is sufficiently specific creates an expectation on the part of consumers that the advertiser has a reasonable basis for the claim.<sup>4</sup> Typically, a consumer cannot find out about a seller’s use of fossil fuels. For example, if a consumer purchases products from a seller that claims that its operations are “carbon neutral,” the consumer has no way of knowing whether that claim is true. The product itself indicates little or nothing about the use of fossil fuels in making it. If a seller’s claim is based on the seller’s purchase of an REC, the problem of verification is even more complicated. The consumer probably does not know that the seller purchased an REC and, even if he or she is aware of the REC purchase, the consumer has no way of knowing if the third party that was supposed to engage in carbon-reducing activities ever did so. The inability of consumers to monitor the truthfulness of these kinds of claims means that the FTC places particular emphasis on advertisers taking steps to substantiate their claims. Misleading or unsubstantiated claims can lead to enforcement actions by the FTC or State Attorneys General.

### **Potentially Misleading Terms**

A second problem concerns the reasonable interpretation of a carbon offset or carbon reduction claim. The complexity of the transactions involved

in sales of RECs and the difficulty consumers have in interpreting claims can create a significant risk that they are being misled by environmental marketing claims. The Green Guides already provide a number of examples of terms used in environmental marketing claims and suggest how consumers are likely to interpret them. It is possible that the FTC will revise the Green Guides to add additional examples to take account for claims relating to greenhouse gas emissions.

One potential source of confusion concerns the ultimate effect of a carbon offset. In general, “additionality” means that a seller’s carbon offset activities have reduced carbon omissions beyond reductions already required by law. For example, a seller might sell RECs or their equivalent to consumers or other businesses in response to the consumer’s desire that their purchase of a product is carbon neutral. The seller might base the REC on its own efforts to capture methane from a landfill. However, the seller would fail the “additionality” test if the seller was already required by environmental regulations to capture the methane. The underlying assumption is that consumers would not pay a premium for carbon offset activities that were already going to take place. A similar analysis applies to advertising claims that imply that a seller is reducing carbon emissions above and beyond reductions already required by law.

### **Implications for Advertisers**

The FTC may provide further guidance about the use of environmental marketing claims by amending and expanding the text of its Green Guides. In the meantime, however, it is important for companies that make environmental marketing claims about greenhouse gas emissions to consider the following guidelines:

- 1) Advertisers must have substantiation for claims that: a) they have reduced their own carbon emissions;

- b) they have engaged in carbon-offset activities that reduce overall emissions; or c) RECs reflect activities that reduce carbon emissions. The substantiation that will be required in a particular case will vary depending on the circumstances, but an advertiser will be expected to collect reliable data on its own carbon-reducing activities and take reasonable steps to monitor the effects of third-party activities.
- 2) If consumers would reasonably expect that sellers have taken steps to reduce greenhouse gas emissions beyond reductions already required by law, companies should ensure that their carbon offset activities meet the "additionality" test. For example, an electric utility that sells consumers the right to be "carbon neutral" in their use of electricity should reduce carbon emissions over and above reductions already required by environmental regulations.
- 3) Terms in advertising should be used in a way that reflects the ordinary understanding of reasonable consumers. For example, a claim that energy is "renewable" should mean that the source of the electric power does not require use of fossil fuels or that the seller has taken steps to offset any fossil fuel emissions resulting from the generation of electrical power from the burning of fossil fuels.

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### Endnotes

- <sup>1</sup> See FTC Policy Statement on Deception, 103 F.T.C. 110, 174 (1984); [www.ftc.gov/bcp/policystmt/ad-decept.htm](http://www.ftc.gov/bcp/policystmt/ad-decept.htm).
- <sup>2</sup> 16 CFR § 260.5.
- <sup>3</sup> *Id.* at § 260.7(b).
- <sup>4</sup> FTC Policy Statement Regarding Advertising Substantiation, <http://www.ftc.gov/bcp/guides/ad3subst.htm>.

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