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Client Alert Commentary

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New FTC Policy Statement Expands Scope of "Unfair" Methods of Competition

The guidance significantly expands the reach of Section 5 beyond the Sherman and Clayton Acts to encompass unfair methods of competition that constitute "incipient" violations of the antitrust laws or violate "the spirit" of the antitrust laws.

Key Points:

- The guidance significantly expands antitrust enforcement under the FTC Act to potentially capture conduct that is otherwise permissible under the antitrust laws.
- The new policy affords the FTC great leeway through its broad terms and lack of clear guidance for businesses and individuals.

On November 10, 2022, the Federal Trade Commission (FTC or Commission) issued a new policy statement (the Policy Statement) regarding its enforcement of unfair methods of competition under Section 5 of the FTC Act. Commissioner Wilson, the lone Republican on the Commission, issued a lengthy dissent critical of the lack of clarity and guidance in the statement.

The Policy Statement replaces a prior Section 5 statement issued by a bipartisan Commission in 2015. That policy statement limited Section 5 to a similar scope as the other antitrust laws and rooted Section 5 enforcement in the consumer welfare standard. The current leadership of the Commission withdrew the 2015 statement a little over a year ago, on a party-line vote. The new Policy Statement aims to greatly expand the scope of enforcement under Section 5 beyond the limitations of the Sherman and Clayton Acts, the US's other two federal antitrust laws. The majority of the Commission reads the "unfair methods of competition" in Section 5 of the FTC Act broadly to forbid conduct that "tend[s] to negatively affect competition conditions" by "affecting consumers, workers or other market participants." Unlike the long-understood burdens in antitrust laws, the FTC need no longer show actual anticompetitive effects under the Policy Statement, but rather only that the challenged conduct negatively affects competitive conditions.

The FTC's New Approach

The Policy Statement articulates the following general principles that the FTC will apply when determining whether conduct constitutes an unfair method of competition under Section 5:

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1. **The conduct must be a method of competition.** Section 5 will apply only to *conduct* implicating competition, not conditions of the market (like high concentration or barrier to entry). While the conduct must implicate competition, it does not need to do so directly in order to qualify as a method of competition. For example, misuse of the regulatory process that can create or exploit impediments to competition with respect to licensing, patents, or standard setting can constitute a method of competition. On the other hand, violations of generally applicable laws like environmental or tax laws will not likely qualify as a method of competition.

2. **The conduct must be unfair.** The conduct must go beyond competition on the merits. When evaluating the conduct's extent, the FTC will analyze whether the conduct: (A) may be coercive, exploitative, collusive, abusive, deceptive, predatory, etc. (referred to as "indicia of unfairness"); and (B) tends to affect competitive conditions negatively (referred to as "negative impact"). These two factors will be evaluated on a sliding scale — for example, if the indicia of unfairness are clear, the FTC will need less evidence of a negative impact. Nevertheless, even conduct that "is not facially unfair" may violate Section 5 depending on competitive conditions, which include the respondent's power and intent. Further, the conduct does not need to cause *actual* harm in the specific instance to be considered unfair. Instead, the FTC will examine whether the conduct "has a tendency to generate negative consequences," which will include items such as raising prices, limiting choice, impairing other market participants, or reducing the likelihood of potential or nascent competition.

3. **The FTC *may* consider potential cognizable justifications.** The Policy Statement expresses a great deal of skepticism about whether any justifications could overcome a showing of a *prima facie* case by the FTC. Similar to other antitrust actions, the respondent bears the burden to show that the conduct is legally cognizable, non-pretextual, and narrowly tailored. Additionally, the asserted benefits must be in the market where the harm occurs and must outweigh the harm. Because the FTC does not need to prove a relevant market for Section 5 under the Policy Statement, the respondent will likely need to do so in order to prove that asserted benefits exist in the same market.

The Policy Statement contains (or omits) several notable items:

- The Policy Statement identifies that Section 5 does not require a showing of market definition or market power. According to the Policy Statement, Section 5 will not focus on the balancing structure of pro- and anticompetitive effects under the "rule of reason," but will instead focus on unfair methods of competition that tend to negatively affect competitive conditions. The Policy Statement explains that because the goal of Section 5 is distinct from that of the Sherman Act, evidence that conduct tends to negatively affect competitive conditions will eliminate the need to prove a relevant market or market power.

- The Policy Statement extends the FTC Act beyond the consumer welfare standard. According the Policy Statement, protected groups extend beyond consumers to include competitors, employees, and others affected by the conduct.

- The Policy Statement relies very little on recent case law. Instead, it primarily relies on dated decisions and citations to the legislative history to support its positions.

- The Policy Statement seeks to establish a potential defense to future challenge by stating that Congress created the Commission as the expert agency in interpreting the FTC Act, and therefore its interpretation deserves deference.

Examples of Potential Violations

The Policy Statement identifies historical examples of unfair methods of competition that might constitute a violation of Section 5 — including both horizontal and vertical conduct. While this conduct may also violate the Sherman or Clayton Acts, it does not need to in order to be considered a violation of Section 5. For example, otherwise permissible conduct (such as a refusal to deal under *Trinko*) may still violate Section 5 under the Policy Statement. Similarly, exclusive dealing that negatively affects a competitor may now constitute a violation of Section 5. The Policy Statement identifies the following examples of potential violations of Section 5:

- **Conduct deemed to be an incipient violation of the antitrust laws.** This includes conduct by respondents who do not have market power or conduct that has "the tendency to ripen into violations." Examples include:
  - practices deemed to violate Sections 1 and 2 of the Sherman or Clayton Acts;
  - invitations to collude (a long-viewed violation of Section 5);
  - mergers, acquisitions, or joint ventures "that have the tendency to ripen into violations of the antitrust laws";
  - a series of mergers or other transactions that individually may not violate the antitrust laws but rather "tend to bring about the harms that the antitrust laws were designed to prevent" as a group; and
  - loyalty rebates, tying, bundling, and exclusive dealing arrangements that "have the tendency to ripen into violations" through industry conditions or the actor's position within the industry.

- **Conduct that violates "the spirit" of the antitrust laws.** The Commission set out a list of conduct that does not constitute an actual violation, but that it characterized as conduct that "tends to cause potential harm similar to an antitrust violation." Examples include:
  - practices that facilitate tacit collusion;
  - parallel exclusionary conduct that may cause harm;
  - individual conduct when looked at cumulatively (the so-called monopoly broth theory);
  - fraudulent and inequitable practices that undermine the standard-setting process or a process at the PTO;
  - price discrimination that is not otherwise barred by the Robinson-Patman Act;
  - *de facto* tying, bundling, exclusive dealing, or loyalty rebates that use market power in one market to affect negatively the same or a related market;
  - a succession of lawful mergers that may "tend to bring about" harm cumulatively;
  - potential or nascent competitor acquisitions;
  - interlocking directors and officers that do not violate the plain terms of Clayton Act Section 8;
  - commercial bribery and corporate espionage that "tends to create or maintain market power";
  - false or deceptive marketing; and
  - discriminatory refusals to deal that "tend to create or maintain market power."

The Commission will use a "totality of the circumstances" analysis to evaluate such conduct, giving yet additional leeway to enforcers.

Additional Considerations

The Policy Statement's expansive view of Section 5 coupled with a lack of clear definitions means that the FTC may determine that a broader range of conduct violates Section 5. The lack of clear guidance

and reliance on terms such as “tends” and “negatively affects competitive conditions” leaves the Commission significant leeway to condemn any conduct that it wants to under Section 5. The FTC provides no guidance, for example, on how it intends to distinguish unfair “corporate espionage” from legitimate competitive intelligence gathering. As such, companies may only learn that their conduct violated the FTC Act when they are charged with a violation.

Companies should consider how their actions will affect employees and other stakeholders before making a decision and pay careful attention when addressing items such as exclusive agreements, discounting and rebating agreements, and employee non-competes. For one, companies should consider the purpose behind any particular practice and take time to document such rationales. While the Policy Statement indicates that the Commission may reject nearly all defenses to what it considers a violation of Section 5, such efforts are important in the investigatory phase and in any subsequent litigation.

As with the prior policy statement, the new Policy Statement does not come with the force of law, and the Commission can rewrite or revise it. Further, the Commission’s new interpretation of Section 5 has not yet been tested in the courts — which is likely to occur if (and when) the Commission decides to take enforcement actions based on the Policy Statement. The FTC’s interpretation of Section 5 may prove difficult to square with judicial interpretations of state unfair competition laws, for example, where in many jurisdictions the courts have long recognized that business conduct that is not anticompetitive is not unfair.

Latham & Watkins will continue to report on the FTC’s interpretation and application of Section 5, and other developments in this area.

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