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FTC Policy Statement Broadens the Scope of its Authority under Section 5 of the FTC Act

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On November 10, 2022, the Federal Trade Commission (FTC) released a Policy Statement (Policy Statement) regarding the scope of Section 5 of the Federal Trade Commission Act (FTC Act). Section 5 prohibits "unfair methods of competition" and instructs the FTC to enforce this prohibition. The Policy Statement "supersedes all previous FTC policy statements and guidance" on the scope of Section 5, including a 2015 FTC policy statement, later withdrawn in 2021, that limited its application to the bounds of the Sherman Act and Clayton Act (the antitrust laws). The new Policy Statement departs from this narrower interpretation, emphasizing that Section 5 reaches beyond antitrust statutes to include numerous categories of unfair conduct with a tendency to negatively affect competitive conditions. Ultimately, the Policy Statement sets out the key general principles it will use to "police the boundary between fair and unfair competition through both enforcement and rulemaking."

Background

The FTC's previous 2015 policy statement limited the application of Section 5 to the Sherman Act "rule of reason" test—which asks whether a given restraint of trade is economically "reasonable"—making it harder for the agency to challenge the wide array of anticompetitive behavior in the market. The new Policy Statement broadens the scope of Section 5 and cites to the Section's text, legislative history and caselaw in justifying the departure from its former interpretation.

Similar to the FTC's July 2021 withdrawal of the 2015 policy statement, the new Policy Statement references the text and legislative history of Section 5 in establishing that it reaches beyond the other antitrust statutes: In enacting Section 5, Congress's aim was to create a new prohibition broader than, and different from, the Sherman and Clayton Acts and to give the FTC the unique authority to identify and protect against unfair forms of competition. Moreover, the Policy Statement explains that Congress evinced a clear aim that "unfair methods of competition" need not require a showing of current anticompetitive harm or anticompetitive intent in every case, as would be required under the Sherman Act and Clayton Act.

The Policy Statement notes that the both the Supreme Court and several federal circuit courts have adopted the view that the scope of Section 5 reaches conduct which, although not a violation of the plain text of the antitrust laws, is close to a violation or is contrary to their spirit. The courts have also recognized the importance of deference to the FTC where it acts against conduct that is unfair. After establishing that the broadened scope of Section 5 is rooted in its legislative history and caselaw, the Policy Statement defines the elements for unfair methods of competition in violation of

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Section 5, generally describe the justifications which may act as a defense to a Section 5 allegation, and gives historical examples of violative conduct, each of which are summarized in the paragraphs that follow.

Unfair Methods of Competition

In order to violate Section 5, the conduct must be (1) a method of competition (2) that is unfair.

First, a method of competition is conduct taken by an actor in the marketplace that implicates competition. In contrast, violations of general applicable laws by themselves (i.e., environmental or tax laws) that only give an actor a cost advantage would not be considered a method of competition. An example of what would constitute a method of competition would be the misuse of regulatory processes that can generate or exploit barriers to competition.

Second, the method of competition must be unfair, meaning that the conduct goes beyond competition on the merits. There are two main criteria to consider when evaluating whether conduct goes beyond competition on the merits. First, the conduct itself may be coercive, exploitative, collusive, abusive, deceptive, predatory, or involve the use of economic power of a similar nature. Second, the conduct must tend to negatively affect competitive conditions, such as conduct that tends to exclude or hinder the opportunities of market participants, reduce competition between rivals, limit choice, or otherwise harm consumers. These two principles are weighed according to a sliding scale.

The Policy Statement warns that even when conduct is not facially unfair, it may violate Section 5. In these circumstances, more information about the nature of the commercial setting may be necessary to determine whether there is a tendency to negatively affect competitive conditions. The size, power, and purpose of the respondent may be relevant, as are the current and potential future effects of the conduct. Otherwise, Section 5 does not require a separate showing of market power or market definition when the evidence indicates that such conduct tends to negatively affect competitive conditions. Given the distinctive goals of Section 5, the inquiry will focus on stopping unfair methods of competition in their incipiency based on their tendency to harm competitive conditions.

Justifications

The Policy Statement limits the cognizable justifications that may act as a defense in Section 5 cases noting that "it would be contrary to the text, meaning, and case law of Section 5 to justify facially unfair conduct on the grounds that the conduct provides the respondent with some pecuniary benefits." Unlike in a rule of reason analysis, no net efficiencies test or numerical cost-benefit analysis are applicable in a Section 5 case, due to the "variety of non-quantifiable harms" contemplated by the Section 5 framework. This guidance, in combination with the limited body of caselaw on standalone Section 5 claims, makes uncertain what justifications could defend against a Section 5 allegation or how these justifications would be tested against the alleged harms.

However, the Policy Statement does make clear that the burden of proof in raising a cognizable justification defense remains with the respondent: "It is the party's burden to show that the asserted justification for the conduct is legally cognizable, non-pretextual, and that any restriction used to bring about the benefit is narrowly tailored to limit any adverse impact on competitive conditions. In addition, the asserted benefits must not be outside the market where the harm occurs."

Examples

The Policy Statement offers guidance on the application of Section 5 in the form of a non-exhaustive list of historical examples of unfair methods of competition. Included in this list are:

- **Practices that violate the Clayton Act or Sections 1 and 2 of the Sherman Act.** While the Policy Statement interprets Section 5 as broader than the antitrust laws, violations of these laws still constitute Section 5 violations.
- **"Conduct deemed to be an incipient violation of the antitrust laws."** This includes conduct by firms who have not gained full-fledged monopoly or market power or that leads to violations of the antitrust laws such as invitations to collude or "mergers, acquisitions, or joint ventures that have the tendency to ripen into violations of the antitrust laws."
- **"Conduct that violates the spirit of the antitrust laws."** The Policy Statement explains that this includes conduct that causes potential harm similar to an antitrust violation, but that may not be covered by the literal language of the antitrust laws or falls into a "gap" in those laws. "As such, the analysis may depart from prior precedent based on the provisions of the Sherman and Clayton Acts." Some examples given for such conduct include:
    - practices that facilitate tacit coordination,
    - conduct by a respondent that is undertaken with other acts and practices that cumulatively may tend to undermine competitive conditions in the market,
    - price discrimination claims not covered by Clayton Act,
    - a series of mergers or acquisitions that tend to bring about the harms that the antitrust laws were designed to prevent, but individually may not have violated the antitrust laws,
    - using market power in one market to gain a competitive advantage in an adjacent market by, for example, utilizing technological incompatibilities to negatively impact competition in adjacent markets,
    - conduct resulting in direct evidence of harm, or likely harm to competition, that does not rely upon market definition,
    - interlocking directors and officers of competing firms not covered by the literal language of the Clayton Act,
    - false or deceptive advertising or marketing which tends to create or maintain market power,
    - discriminatory refusals to deal which tend to create or maintain market power.

Key Takeaways

- **Even conduct that does not violate the Sherman Act or Clayton Act may violate Section 5 of the FTC Act.** Conduct that "has the tendency to ripen into violations of the antitrust laws" or that "violates the spirit of the antitrust laws" may warrant liability under Section 5. Although these terms are vague, companies can look to the full list of examples given in the Policy Statement to better ensure compliance with Section 5.
- **Conduct that violates the Sherman Act or Clayton Act also violates Section 5 of the FTC Act.** The FTC may enforce the prohibition of "unfair methods of competition" on a

standalone basis or in conjunction with other antitrust enforcement. Companies should, as always, maintain systems for antitrust compliance in their business activities and transactions to minimize risk of antitrust liability under these laws or Section 5 of the FTC Act.

- **Procompetitive justifications may not effectively defend against Section 5 liability.** The Policy Statement describes the limited nature of available defenses to Section 5 claims and rejects the applicability of justifications to *prima facie* unfair methods of competition. Caselaw recognizing cognizable justifications for otherwise violative conduct is also limited. Our team will continue to monitor this space and provide updates as necessary.