

New Federal Initiatives Project

**Expanding FTC's Rulemaking and
Enforcement Authority**

**By
Joshua D. Wright***

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Expanding FTC's Rule making and Enforcement Authority

In December, the House of Representatives passed H.R. 4173, the Wall Street Reform and Consumer Protection Act of 2009 (the "House Bill"). The Senate is currently debating a version of the legislation, S. 3217, the Restoring American Financial Stability Act of 2010 (the "Senate Bill"). Both measures modify and expand Federal Trade Commission ("FTC") power in terms of (1) the agency's rulemaking authority and (2) enforcement capabilities.¹

The House and Senate bills are best known for their establishment of a new financial regulatory body, the Consumer Financial Protection Agency (the "CFPA").² While banks, savings and loans, and federal credit unions are already exempt from FTC regulation, the House and Senate bills similarly exempt "consumer financial products or services" from FTC oversight and shift this responsibility to the new CFPA.³

However, at the same time, the bills effectively eliminate various procedural safeguards against FTC enforcement, collectively known as "Magnuson-Moss" rulemaking. Congress established current Magnuson-Moss standards in 1980 to prevent the sort of economic interventionism for which the FTC became well-known in the 1970s, when the agency sought to be "the second most powerful legislature in Washington."⁴ Magnuson-Moss implemented a specialized FTC standard for regulation: the FTC must show "substantial evidence" for the FTC to regulate "prevalent" unfair and deceptive acts. Magnuson-Moss also expanded upon the backdrop procedures required by the Administrative Procedure Act ("APA"): two notices of proposed notification, prior notification to Congress, opportunity for informal hearings, and possible cross-examination of witnesses. Magnuson-Moss forced the FTC to justify a new rule with "particularity" after obtaining objective evidence based on a relevant market taken as a whole rather than relying on anecdotal accounts from individual consumers. Due to this high standard, it has often taken the FTC years to implement new rules.⁵

The CFPA bill amends the FTC Act and replaces the Magnuson-Moss standards with a more permissive application of rulemaking under the APA. Under the APA, new rules may be issued only after a "notice and comment" procedure. Federal courts have interpreted these "notice and comment" requirements as substantially informal, imposing few to no particular procedural requirements on the form of the relevant notice and duration for public comment. Additionally, the standard for judicial review of new rules under the APA provides greater deference to the FTC than the Magnuson-Moss standard, and would permit the FTC or CFPA to regulate with minimal oversight in a manner similar to that of other, more specialized, federal agencies.

Currently, APA rulemaking standards act as a backdrop for administrative agencies not otherwise subject to specific procedures by statute – such as Magnuson-Moss – and the FTC currently relies on APA procedures for areas not covered by Magnuson-Moss, such as telemarketing. According to former FTC Chairman Timothy J. Muris, APA rulemaking coupled with a more activist regulatory environment could prompt the FTC to regulate wide areas of the economy with which they may have little previous experience.

The current Commission's leadership is eager to acquire this new and expanded rulemaking function. Chairman Jon Leibowitz testified in a recent Senate committee hearing that this expansion would "significantly enhance the agency's ability to stop financial fraud."⁶

Commissioner Kovacic has shown greater hesitation, citing the FTC's "unique . . . range of subject matter [unfair or deceptive acts or practices] and sectors [reaching broadly across the economy, except for specific carve-outs]" and a belief that current procedures surrounding Commission rulemaking strike an appropriate balance between vigor and caution in maximizing consumer welfare.⁷

The CFPB bills augment the FTC's enforcement powers in two distinct ways: (1) the FTC would have the power to impose civil penalties on a company for "unfair or deceptive acts or practices" without referral to the Department of Justice (the "DOJ") and (2) the FTC could impose third-party liability upon companies that "substantially assist" an unlawful act.

The CFPB bills would grant the FTC power to impose broader civil penalties.⁸ Muris testified that enhanced civil penalty authority may have the effect of over-deterrence and additional complication of blurring the distinction between DOJ and FTC authority. Additionally, the statute may be read to impose automatic monetary fines on companies in antitrust actions. Chairman Leibowitz supports independent FTC imposition of civil penalties of up to \$16,000 per violation per day without referral to DOJ.⁹ Chairman Leibowitz criticized the current DOJ referral process as "inefficient" due to the length of time allowed for DOJ deliberation and because of the FTC's relative expertise in enforcing the FTC Act. Chairman Leibowitz accordingly compares the FTC's potential new power of independent enforcement to the Securities and Exchange Commission's existing powers.¹⁰ However, in his Senate testimony, Muris suggested a lack of empirical evidence supporting the claim these additional penalties would produce welfare benefits over and above the chilling effect of the ambiguous new fines.¹¹ Muris testified that current FTC penalties are sufficient to both punish violations and deter future violators.¹²

The bills also expand the FTC's enforcement powers to third party liability. Since the Supreme Court decided *Central Bank of Denver v. First Interstate Bank of Denver*, there has been no implied third party right of action in the FTC Act.¹³ In response, the Senate bill expressly provides a cause of action and extends liability to companies that "substantially assist" an unlawful act, even without direct responsibility for or actual knowledge of the violation. Muris finds third-party liability unnecessary for several reasons. Muris first argued the impropriety of holding advertising agencies liable for the actions of their clients, because these agencies are neither expected to substantiate clients' claims nor are they well-positioned to do so. Second, Muris suggested the FTC already has the authority to address, in "appropriate circumstances", third-party liability under the FTC's power to regulate "unfair" practices. One plausible construction of this language would interpret a third party's decision not to prevent a deceptive practice at relatively low cost as inherently "unfair" within the meaning of the Act. Thus, according to Muris, further legislation is unnecessary.¹⁴

Despite the political momentum in favor of financial regulatory reform, there remains the possibility of significant change to the legislation during consideration of the Senate bill and consolidation of two bills. In the currently proposed legislation, the rulemaking and enforcement powers of the FTC will expand dramatically. The role of the FTC might continue to evolve significantly under new iterations of financial regulatory reform.

* Professor Joshua D. Wright is an Assistant Professor at George Mason University School of Law and Co-Director of the Antitrust Research Center.

¹ See Wall Street Reform and Consumer Protection Act of 2009, H.R. 4173, 111th Cong. § 4901 (2009).

² See generally, *Financial Regulation Reform Bills in Congress*, Wall Street Journal, April 27, 2010 (Business).

³ “Consumer financial products or services” are defined as any product or service that results from or is related to engaging in a financial activity and that is to be used by a consumer “primarily for personal, family or household purposes.”

⁴ *Financial Services and Products: The Role of the Fed. Trade Commission in Protecting Customers: Hearing on S. 3217 Before the Subcomm. on Consumer Protection, Product Safety, and Insurance of the S. Comm. on Commerce, Science, and Transportation*, 111th Cong. 2 (2010) (statement of Timothy J. Muris).

⁵ *Financial Services and Products: The Role of the Fed. Trade Commission in Protecting Customers: Hearing on S. 3217 Before the S. Comm. on Commerce, Science, and Transportation*, 111th Cong. 17 (2010) (statement of the Federal Trade Commission).

⁶ *Id.* at 16-17.

⁷ *Financial Services and Products: The Role of the Fed. Trade Commission in Protecting Customers: Hearing on S. 3217 Before the Subcomm. on Consumer Protection, Product Safety, and Insurance of the S. Comm. on Commerce, Science, and Transportation*, 111th Cong. 3 (2010) (statement of Commissioner William E. Kovacic, FTC).

⁸ Currently, the FTC may only impose civil penalties in fraud cases.

⁹ *Financial Services and Products: The Role of the Fed. Trade Commission in Protecting Customers: Hearing on S. 3217 Before the S. Comm. on Commerce, Science, and Transportation*, 111th Cong. 17-18 (2010) (statement of the Federal Trade Commission).

¹⁰ *Id.* at 18-19.

¹¹ Muris, *supra* note 4, at 31.

¹² *Id.* at 31-32.

¹³ 511 U.S. 164 (1994).

¹⁴ Muris, *supra* note 4, at 46.

Related Materials:

Wall Street Reform and Consumer Protection Act of 2009 “House Bill.”

http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_bills&docid=f:h4173rfs.txt.pdf

Proposed Amendments to House Bill:

<http://www.opencongress.org/bill/111-h4173/amendments>

Restoring American Financial Stability Act of 2010 “Senate Bill”

http://banking.senate.gov/public/_files/ChairmansMark31510AYO10306_xmlFinancialReformLegislationBill.pdf

Senate Hearing: Executive Session to Mark-Up an Original Bill Entitled: Restoring American Financial Stability Act of 2010 (webcast):

http://banking.senate.gov/public/index.cfm?FuseAction=Hearings.Hearing&Hearing_ID=b8c4a3bd-db46-4b8d-a759-5024b72204cd

Comparing the House and Senate Financial Reform Bills: Republicans Soften on Wall Street Reform Bill:

<http://www.nytimes.com/interactive/2010/03/16/business/financialreform-billcompare.html>

“Senate Dips Toes into Financial Reform Pool” by Janet Hook and Jim Puzzangera, *Chicago Tribune*, May 5, 2010:

http://articles.chicagotribune.com/2010-05-05/news/sc-biz-0506-overhaul--20100505_1_large-financial-firm-amendment-wall-street

“To Protect Consumers, Who Will Be Regulated?” by Edward Wyatt and Sewell Chan, *New York Times*, May 1, 2010:

<http://www.nytimes.com/2010/05/01/business/01consume.html>

“Twelve Ways to Fix Wall Street” by James Altucher, *Wall Street Journal*, April 27, 2010:

<http://blogs.wsj.com/financial-adviser/2010/04/27/12-ways-i-would-fix-wall-street/>