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On Notice: Procedural Overview of the FTC's Section 5 Penalty Offense Authority

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As discussed in our earlier post, on October 13, 2021, the FTC issued "Notice of Penalty Offenses" letters to more than 700 companies, placing them on notice of civil penalties up to $43,792 per violation if they use endorsements or testimonials in an unfair or deceptive manner. These letters are the first step for the FTC to obtain civil penalties in administrative adjudication proceedings under Section 5 of the FTC Act. In this post, we explain the process for the FTC to obtain such penalties under Section 5. Future posts in our "On Notice" series will cover the substantive aspects of the Notice of Penalty Offenses concerning endorsements and testimonials, and will offer tips to comply with the FTC's precedent and guidelines.

The FTC may enforce the FTC Act's prohibition on unfair or deceptive acts or practices either by commencing administrative adjudication proceedings under Section 5 of the Act or by suing a party in court under Section 13(b). As noted in our previous post, the Supreme Court's decision this past April in *AMG Capital Mgmt., LLC v. FTC* has significantly curtailed the FTC's ability to pursue civil penalties under Section 13(b). Thus, the FTC seems to be looking to increase its utilization of Section 5, which explicitly allows for civil penalties.

Under Section 5 of the FTC Act, the Commission can obtain civil penalties against a company that acted unfairly or deceptively through the Penalty Offense Authority. The FTC can seek civil penalties if it proves that (1) the company knew the conduct was unfair or deceptive in violation of the FTC Act and (2) the FTC had already issued a written decision that such conduct is unfair or deceptive. 15 U.S.C. § 45(m)(1)(B). The Notice of Penalty Offenses letters provide a non-exhaustive list of conduct relating to endorsements and testimonials that the FTC has determined to be unfair or deceptive, including:

- Falsely claiming an endorsement by a third party;

- Misrepresenting whether an endorser is an actual, current, or recent user;
- Using an endorsement to make deceptive performance claims;
- Failing to disclose an unexpected material connection with an endorser;
- Misrepresenting that an endorsement represents the experience, views, or opinions of users or purported users;
- Misrepresenting that the experience of endorsers represents consumers' typical or ordinary experience; and
- Continuing to use an endorsement without good reason to believe that the endorser continues to subscribe to the views presented.

Future posts in our "On Notice" series will explore these types of conduct in further detail.

The letters make clear they are not an indication the recipients have engaged in any unfair or deceptive practices. However, the letters put the recipients on notice of the prohibited conduct and may enable the FTC to seek civil penalties if a company is found to be engaged in such activity.

To begin an administrative adjudication under Section 5, the FTC issues a complaint setting forth its charges if they have "reason to believe" that a violation has occurred. § 45(b). Respondents may elect to settle with the FTC, sign a consent agreement, consent to entry of a final order, or contest the charges. If the FTC accepts a proposed settlement agreement, the corresponding order is made available for public comment for 30 days before the FTC determines whether to make the order final.

If a respondent contests the charges, the complaint is adjudicated in a trial-type proceeding governed by the FTC's rules of practice before an administrative law judge ("ALJ"). The FTC is represented in the proceeding by an FTC "complaint counsel." After the ALJ issues a decision setting forth findings of fact and law, and recommending a remedy or dismissal, either party may appeal the decision to the full Commission. After the Commission's final decision, a losing respondent may file a petition for review with a US Court of Appeals. After all judicial review of the FTC's order is completed, the FTC may seek consumer redress in federal district court for the conduct at issue in the administrative proceeding. If the district court determines that a reasonable person would have known under the circumstances that the conduct was dishonest or fraudulent, the respondent will be liable for consumer harm and subject to civil penalties. As noted, the civil penalty amount is currently $43,792 per violation. It is adjusted for inflation annually.

Watch this space for best practices on using endorsements and testimonials in advertising. We will also be on the lookout for instances of the FTC bringing an enforcement action relating to this subject matter.

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Related Professionals

- **Jennifer Yang**
  Senior Counsel
- **Timothy E. Burroughs**
  Associate