



**DECEPTION, MATERIALITY, AND THE
ECONOMICS OF CONSUMER PROTECTION
COMMENT OF THE GLOBAL ANTITRUST INSTITUTE,
ANTONIN SCALIA LAW SCHOOL, GEORGE MASON UNIVERSITY**

Tad Lipsky

**Antonin Scalia Law School,
George Mason University**

Joshua D. Wright

**Antonin Scalia Law School,
George Mason University**

Douglas H. Ginsburg

**U.S. Court of Appeals for the D.C. Circuit;
Antonin Scalia Law School, George Mason University**

John M. Yun

**Antonin Scalia Law School,
George Mason University**

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Deception, Materiality, and the Economics of Consumer Protection
Comment of the Global Antitrust Institute,
Antonin Scalia Law School, George Mason University

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This comment is submitted in response to the United States Federal Trade Commission (“FTC”) hearing on Consumer Privacy as part of the Hearings on Competition and Consumer Protection in the 21st Century. We submit this Comment based upon our extensive experience and expertise in consumer protection, antitrust law, and economics.¹

Deception is one of the pillars of the FTC’s consumer protection authority under Section 5 of the FTC Act. Since the FTC’s landmark Policy Statement on Deception (“Deception Statement”) was issued in 1983, materiality has been established as one of the three key elements of a deception case. In this comment, we discuss the role of deception and materiality in consumer protection and consider how economic analysis

¹ The Global Antitrust Institute (GAI), a division of the Antonin Scalia Law School at George Mason University (Scalia Law), is a leading international platform for economic education and research that focuses upon the legal and economic analysis of key antitrust issues confronting competition agencies and courts around the world. University Professor Joshua D. Wright, Ph.D. (economics), is the Executive Director of the GAI and a former U.S. Federal Trade Commissioner. John M. Yun, Ph.D. (economics), is the Director of Economic Education, Associate Professor of Law at Scalia Law, and former Acting Deputy Assistant Director in the Bureau of Economics, Antitrust Division, at the U.S. Federal Trade Commission. Professor of Law Douglas H. Ginsburg is a Senior Judge, United States Court of Appeals for the District of Columbia Circuit, Chairman of the GAI’s International Board of Advisors, and a former Assistant Attorney General in charge of the Antitrust Division of the U.S. Department of Justice. Tad Lipsky is the Director of GAI’s Competition Advocacy Program, Adjunct Professor at Scalia Law, a former Deputy Assistant Attorney General for Antitrust and a former Acting Director, Bureau of Competition, U.S. Federal Trade Commission. The GAI gratefully acknowledges substantial assistance in the preparation of this Comment provided by Scalia Law students Jay Kaplan and Nicole Booth.

can sharpen consumer protection enforcement efforts. Ultimately, we find that strong adherence to the materiality standard is a critical component of an enforcement regime that promotes consumer welfare. Deception enforcement untethered from materiality runs the risk of making consumers worse off by chilling pro-consumer behavior.

Deception and Materiality

Section 5 of the FTC Act states that “unfair or deceptive acts or practices in or affecting commerce, are hereby declared unlawful.”² The Deception Statement emphasizes that “[c]ertain elements undergird all deception cases.” In particular, the Deception Statement lays out the following criteria for actionable deception cases under Section 5: “First, there must be a representation, omission or practice that is likely to mislead the consumer . . . Second, [FTC Staff will] examine the practice from the perspective of a consumer acting reasonably in the circumstances . . . [and] Third, the representation, omission, or practice must be a ‘material’ one.”³

A material “act or practice is likely to affect the consumer’s conduct or decision with regard to a product or service.”⁴ In other words, a false or misleading claim is one

² 15 U.S.C. § 45(a) (2006).

³ Fed. Trade Comm’n, Policy Statement on Deception (1983), *appended to Cliffdale Assocs., Inc.*, 103 F.T.C. 110, 170-71 (1984), https://www.ftc.gov/system/files/documents/public_statements/410531/831014deceptionstmt.pdf [hereinafter FTC Policy Statement on Deception] (emphasis omitted). The Deception Statement notes that deceptive practices “include false oral or written representations, misleading price claims, sales of hazardous or systematically defective products or services without adequate disclosures, failure to disclose information regarding pyramid sales, use of bait and switch techniques, failure to perform promised services, and failure to meet warranty obligations.”

⁴ *Id.* at 171.

that causes consumers to choose one product over another to their detriment. A materially false statement is likely to result in consumer injury because, in the absence of a deception, the consumer would have chosen a more preferred option.⁵ Materiality is crucial in differentiating a deceptive representation from a salesman's puffery or embellishment because the consumer would "have chosen differently but for the deception," while a salesman's puffery merely accentuates the features of a particular product in a way that no reasonable person would take literally.⁶

There are some types of representations that the Commission considers presumptively material and thus unlawful. For example, claims that "significantly involve health, safety, or other areas with which the reasonable consumer would be concerned" are presumptively material.⁷ A presumption of materiality also applies to express claims for which the seller knew (or should have known) that an ordinary consumer would need omitted information to adequately evaluate the product or service, and that the omission would mislead a consumer.⁸ Similarly, under certain conditions the Commission can infer materiality from implied claims.⁹ Rebuttable

⁵ *Id.* at 171, 188 n.46 ("In evaluating materiality, the Commission takes consumer preferences as given. Thus, if consumers prefer one product to another, the Commission need not determine whether that preference is objectively justified. Similarly, objective differences among products are not material if the difference is not likely to affect consumer choices.").

⁶ *Id.* at 171.

⁷ *Id.* at 190 (The Commission has found materiality when the representation "concerns the purpose, safety, efficacy, or cost" of these products and services of public concern. (citations omitted)).

⁸ *Id.* at 189.

⁹ FTC Policy Statement on Deception, *supra* note 3, at 191. *See, e.g.*, *Removatron Int'l Corp.*, 111 F.T.C. 206, 306-07 (1988), *aff'd*, 884 F.2d 1489 (1st Cir. 1989); *Am. Home Prods. Corp.*, 98 F.T.C. 136, 368 (1981), *aff'd*,

presumptions of materiality make economic sense when the context of the statement makes apparent that exposure to the statement would affect consumer decision-making with a high degree of probability.

Where the Commission cannot find or infer materiality based on either an express or an implied claim, “the Commission may require evidence that the claim or omission is likely to be considered important by consumers.”¹⁰ This can be evidence “that the product or service with the feature represented costs more than an otherwise comparable product without the feature, a reliable survey of consumers, or credible testimony.”¹¹ The Commission also occasionally relies on economic evidence to identify materiality, and therefore deception.¹²

A finding of materiality is a finding that a representation changed, or would likely change, a consumer’s choice of which product to buy. The Deception Statement recognizes the fundamental economic link between materiality and consumer injury, “A finding of materiality is also a finding that injury is likely to exist . . . Thus, injury

695 F.2d 681 (3d. Cir. 1982). In this case, “[t]he very fact that AHP sought to distinguish its products from aspirin strongly implies that knowledge of the true ingredients of those products would be material to purchasers.”

¹⁰ FTC Policy Statement on Deception, *supra* note 3, at 191.

¹¹ *Id.*

¹² *Id.* at 191 n.57 citing to *Am. Home Prods. Corp.*, 98 F.T.C. at 369 (“If the record contained evidence of a significant disparity between the prices of Anacin and plain aspirin, it would form a further basis for a finding of materiality. That is, there is a reason to believe consumers are willing to pay a premium for a product believed to contain a special analgesic ingredient but not for a product whose analgesic is ordinary aspirin.”). See also Michael R. Baye & Joshua D. Wright, *How to Economize Consumer Protection*, ANTITRUST SOURCE, at 5-6 (Feb. 2018), https://www.americanbar.org/content/dam/aba/publishing/antitrust_source/feb18_baye_2_15f.pdf.

and materiality are different names for the same concept.”¹³ The Deception Statement makes clear that there can be no finding of deception without a finding of materiality.¹⁴

The Importance of Materiality in Consumer Protection Cases: A Case Study

The FTC has, at times, failed to adhere rigorously to the Deception Statement guidance that deception requires materiality. For example, in *Nomi Technologies, Inc.*, the Commission brought suit against a company providing an analytics service, called “Listen,” using data collected from mobile device tracking in brick-and-mortar stores.¹⁵ The Commission’s complaint focused upon a single statement in Nomi’s privacy policy: “Nomi pledges to . . . Always allow consumers to opt out of Nomi’s service on its website as well as at any retailer using Nomi’s technology.”¹⁶ Nomi failed to live up to this pledge because, while consumers could opt out on the website, there was not always a store-level opt-out option.¹⁷

The Commission voted 3-2 to pursue a deception claim against Nomi on the basis of this misrepresentation.¹⁸ The Commission assumed the opt-out pledge was an

¹³ FTC Policy Statement on Deception, *supra* note 3, at 191-92, n.58. Section 5 deception applies to protect competitors as well as consumers.

¹⁴ The materiality inquiry is critical because the Commission's construct of “deception” uses materiality as an evidentiary proxy for consumer injury.

¹⁵ Complaint, In re Nomi Techs., Inc., FTC File No. 132-3251, ¶ 3 (Apr. 23, 2015).

¹⁶ *Id.* ¶ 12.

¹⁷ Dissenting Statement of Commissioner Joshua D. Wright, In re Nomi Techs., Inc., FTC File No. 132-3251, at 2 (Apr. 23, 2015),

https://www.ftc.gov/system/files/documents/public_statements/638371/150423nomiwrightstatement.pdf [hereinafter Wright Dissenting Statement].

¹⁸ FTC Chairwoman Edith Ramirez and Commissioners Julie Brill and Terrell McSweeney voted in favor of the complaint and consent order. Commissioners Maureen Ohlhausen and Joshua D. Wright both dissented.

express claim and thus presumptively material because the pledge contained “information pertaining to the central characteristics of the product or service.”¹⁹ But the Commission did not undertake any further analysis of materiality.

The evidence in the complaint did not support the allegation that Nomi’s representation was material to consumers “in light of the immediate and easily accessible opt out available on the webpage itself.”²⁰ Nor was there evidence that the statement caused consumers to change their product choice.

A presumption of materiality can make economic sense as applied to a statement that, in context, suggests a high probability of changing a consumer’s decision to his or her detriment. That condition was absent in Nomi. Then-Commissioner Wright highlighted in his dissent that the materiality presumption for express claims “was never intended to substitute for common sense, evidence, or analysis.”²¹ He noted that the Deception Statement promises that the “Commission will always consider relevant and competent evidence offered to rebut presumptions of materiality.”²² During the relevant time period, Nomi’s website received 3,840 visitors and 146 opt-outs, an opt-out rate of 3.8 percent, which is several times higher than the 1 percent average opt-out

¹⁹ Statement of Chairwoman Ramirez, Commissioner Brill, and Commissioner McSweeney, In re Nomi Techs., Inc., FTC File No. 132-3251, at 1-2 (Apr. 23, 2015), https://www.ftc.gov/system/files/documents/public_statements/638351/150423nomicommissionstatement.pdf [hereinafter Commission Majority Statement] citing to FTC Policy Statement on Deception, *supra* note 3, at 191.

²⁰ Wright Dissenting Statement, *supra* note 17, at 2.

²¹ *Id.* at 3.

²² *Id.* citing to FTC Policy Statement on Deception, *supra* note 3, at 188 n.47.

rate for online advertising.²³ This high opt-out rate suggests the relative ease of the online opt-out mechanism “that was immediately and quickly available to consumers at the time they may have been reading the privacy policy,” suggesting that the store-level opt-out pledge was not material.²⁴

Untethering materiality from the deception analysis is not a harmless error.

Indeed, deception enforcement aimed at non-material statements not only wastes scarce agency resources, but also makes consumers worse off as it weakens firms’ incentives to offer comprehensive privacy policies.²⁵ As Commissioner Ohlhausen notes, Nomi itself had no legal duty to post a privacy policy, to make the specific promise to offer multiple opt-out methods, or to describe its practices to consumers.²⁶ The FTC’s prosecution of

²³ *Id.* at 3-4; Commission Majority Statement, *supra* note 19, at 1-2.

²⁴ Wright Dissenting Statement, *supra* note 17, at 3. *See also* Dissenting Statement of Commissioner Maureen K. Ohlhausen, In re Nomi Techs., Inc., FTC File No. 132-3251, at 1 (Apr. 23, 2015), https://www.ftc.gov/system/files/documents/public_statements/638361/150423nomiohlhausenstatement.pdf [hereinafter Ohlhausen Dissenting Statement] (citing to the Wright Dissenting Statement “the evidence we have suggests that the privacy policy’s partially inaccurate statement harmed no consumers.”); *see also* Geoffrey A. Manne, R. Ben Sperry & Berin Szoka, In the Matter of Nomi Technologies, Inc.: *The Dark Side of the FTC’s Latest Feel-Good Case*, Int’l Ctr. for L. & Econ. White Paper 2015-1, at 2-3, 7-10, http://laweconcenter.org/images/articles/icle-nomi_white_paper.pdf (“It is of course a valid question whether, even in context, the inaccurate statement amounted to a material deception, and whether the evidence offered by Commissioner Wright was sufficient to rebut the presumption of materiality. Nevertheless, the majority’s *approach* to answering those questions (*i.e.*, dismissing or ignoring them) and weighing the evidence (*i.e.*, failing to) betrays the majority’s implicit rejection of the [Deception Statement’s] admonishment that context and contrary evidence are essential..”).

²⁵ Wright Dissenting Statement, *supra* note 17, at 4 (“aggressive prosecution of this sort will inevitably deter industry participants like Nomi from engaging in voluntary practices that promote consumer choice and transparency – the very principles that lie at the heart of the Commission’s consumer protection mission.”).

²⁶ Ohlhausen Dissenting Statement, *supra* note 24, at 1.

Nomi's immaterial statements sent "a dangerous message to firms weighing the costs and benefits of voluntarily providing information and choice to consumers."²⁷

Today, the legacy of the Nomi consent order is a reminder that consumer protection enforcement best serves consumers when it acknowledges the basic idea that deception cases involve tradeoffs – and that economic analysis is vital to identifying those tradeoffs, calculating the harms and benefits, and analyzing whether a particular remedy will increase consumer welfare.²⁸ Privacy policies often involve unilateral representations by the merchant that have little effect on the actual transaction. Presuming every one of these representations to be an express claim erodes the materiality standard by incentivizing firms to create vague and narrowly tailored privacy policies rather than all-encompassing policies designed to protect and inform consumers. These incentives also run the risk of damaging the entire body of deception law.

The Role of Economic Analysis in Evaluating Materiality and Deception

The Commission often uses survey methods to investigate potentially deceptive practices to determine whether, but for the deceptive practice, consumers' purchase

²⁷ Wright Dissenting Statement, *supra* note 17, at 4. *See also* Ohlhausen Dissenting Statement, *supra* note 24, at 1 ("I fear that the majority's decision in this case encourages companies to do only the bare minimum on privacy, ultimately leaving consumers worse off."); Tim Sparapani, *Privacy and Security Innovation: The Cautionary Tale of Nomi Technologies And The FTC*, FORBES (May 26, 2015), <https://www.forbes.com/sites/timsparapani/2015/05/26/privacy-and-security-innovation-the-cautionary-tale-of-nomi-technologies-and-the-ftc>.

²⁸ Baye & Wright, *supra* note 12, at 12.

decisions would have been different. But surveys are often flawed due to leading or misleading questions, implicit bias, sample choice, or the lack of a control group.²⁹

Economic analysis can add rigor to the analytical framework used to analyze materiality in deception cases. The FTC's practice has been generally – though with some exceptions – to refrain from relying primarily upon economic evidence to prove that a firm has made a deceptive claim. Rather, economic evidence is often left to respondents seeking to prove an alleged statement was not material or did not actually harm consumers.³⁰

When used properly, economics is about counterfactuals – the process of studying a world with a certain variable and comparing it to that same world without the variable.³¹ This is the same process underlying a materiality inquiry. In order to examine the effect of an allegedly deceptive statement, materiality seeks to compare the world with that statement to the hypothetical world without it.³²

Economic analysis can help answer several questions that are vital to materiality, and hence to identifying deception: (1) how would consumers' behavior change, if at all, but for the representation; (2) were consumers harmed and, if so, to what extent; and (3) are consumers going to be made better off by allocating agency resources to

²⁹ *Id.* at 7.

³⁰ *See id.* at 4 citing *Kraft Inc. v. FTC*, 970 F.2d 311, 319-324 (7th Cir. 1992); *see also* James C. Cooper & Joshua D. Wright, *The Missing Role of Economics in FTC Privacy Policy*, in *CAMBRIDGE HANDBOOK OF CONSUMER PRIVACY* (Evan Selinger, Jules Polonetsky, & Omer Tene eds.) (2018).

³¹ Baye & Wright, *supra* note 12, at 6.

³² *Id.*

obtaining a specific remedy in this consumer protection case?³³ Economists use a variety of methods to answer these questions, such as time series data, models, experiments with control groups, and hybrids of multiple methods.³⁴ The Commission's economists have the skills and resources to undertake these types of analyses; indeed, they already use these same economic methods to evaluate the merits of competition cases and to calculate damages.³⁵

Conclusion

The FTC's deception authority is a pillar of its consumer protection enforcement mission. Deterring deception is important to a well-functioning economy. The Deception Statement correctly identifies materiality as the lodestar of deception analysis precisely because it is the concept that links misrepresentations to consumer injury. Economic analysis can help the FTC to better identify misrepresentations and omissions that are material and therefore likely to injure consumers. Economics can play an especially useful role in privacy cases, such as Nomi, where a presumption of materiality is unlikely to make sense. In these cases, economic tools can be deployed to identify whether the agency is spending resources wisely, and whether a remedy might create incentives that would make consumers worse off. In those cases, and throughout the FTC's consumer protection enforcement efforts, "[d]eeper integration of economic

³³ *Id.* at 4.

³⁴ *See id.* at 7-12.

³⁵ *Id.* at 6.

thinking and economic analysis... offers value to all stakeholders—agencies, private plaintiffs, state attorneys general, and defendants—from case development to litigation and settlement.”³⁶

³⁶ *Id.* at 14-15.