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Section 5 in action: reinvigorating the FTC Act and the rule of law

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*Disclaimer: Chair Khan is not speaking for the Commission or any other FTC Commissioner.

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The Federal Trade Commission Act of 1914 didn't just create a new agency. It created new law for that agency to enforce. The heart of that law is Section 5, which provides that 'unfair methods of competition in or affecting commerce' are 'hereby declared unlawful'.[1] In passing this law, Congress also tasked the FTC with identifying the range of methods of competition that qualify as unfair, since lawmakers recognized they could not specify them all prospectively.

This is a straightforward reading of the statute, and yet it is somewhat controversial. There is a school of thought that considers Section 5's prohibition of unfair methods of competition to be almost a dead letter. According to this view, Section 5 should be read merely as extending Sherman Act enforcement authority to the FTC.[2] Even though the statute outlaws a clearly distinct category of conduct, it is argued that 'unfair methods of competition' should be defined by reference to Sherman 'rule of reason' case law.

Through the first half of its existence, the Commission used its Section 5 authority to challenge a host of unlawful business practices not covered by the other antitrust laws. But more recently, the alternate reading of the statute became dominant. From the 1980s until last year, the Commission allowed its Section 5 authority to lay essentially dormant.

The FTC's legitimacy depends on its adherence to the statutes Congress tasked it with enforcing. Antitrust is a quintessentially democratic area of law, concerned as it is with the diffusion and decentralization of private economic power. For enforcers to retain legitimacy, their actions must be rooted in the laws passed by a democratically elected legislature. That's why, last year, the Commission released a policy statement rededicating the agency to faithfully administering Section 5 of the FTC Act. The statement was one of my highest priorities. It makes clear that our interpretation of Section 5 will be firmly rooted in statutory text, history, purpose, and judicial precedent. I hope and expect that reactivating Section 5 will

[1] 15 USC s 45(a)(1).
[2] For the purposes of this statement, I use Section 5 as shorthand for the unfair methods of competition prohibition; I do not address unfair or deceptive acts or practices, which Congress added to Section 5 in 1938.

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promote not only fair competition, but also the rule of law and the democratic legitimacy of our work.

Congress did not intend Section 5 as a Sherman Act clone. Quite the contrary. Congress created the FTC and its new authorities precisely because it was unsatisfied with the Sherman Act. In the *Standard Oil* case, the Supreme Court had announced it would interpret the Sherman Act using the open-ended rule of reason. Lawmakers were alarmed. They worried that the rule of reason generated erratic, contradictory results, prolonged the resolution of cases, and handed unchecked discretion to the judiciary.[3] A landmark 1913 Senate committee report stated that Sherman Act cases had become 'impossible to predict' and called for legislation 'establishing a commission for the better administration of the law'.[4]

This was the backdrop for the establishment of the FTC. As the congressional record makes clear, Congress believed that an expert, independent agency, with flexible investigatory and administrative powers, would be more effective at combatting evolving anticompetitive business schemes than generalist judges armed only with the rule of reason. Crucially, in outlawing 'unfair methods of competition', lawmakers chose language that clearly departed from the Sherman Act and judicial interpretations of it. With this text, Congress distinguished between *fair* and *unfair* methods of competition—a new distinction, foreign to the Sherman Act—and tasked the FTC with policing the boundary. Lawmakers intended Section 5 to prohibit conduct that threatened fair competition even if it fell beyond the scope of the other antitrust laws.[5]

A large body of judicial precedent, including multiple Supreme Court opinions, affirms this interpretation.[6] As the Court put it in one such decision, in 1968, 'In large measure the task of defining 'unfair methods of competition' was left to the Commission.' Citing the legislative history, the Court went on, 'Congress concluded that the best check on unfair competition would be 'an administrative body of practical men . . . who will be able to apply the rule

[3] Statement of Chair Lina M. Khan Joined by Commissioner Rohit Chopra and Commissioner Rebecca Kelly Slaughter on the Withdrawal of the Statement of Enforcement Principles Regarding 'Unfair Methods of Competition' Under Section 5 of the FTC Act, at 3 (1 July 2021) [hereinafter 'Statement on 2015 Statement Withdrawal'] (citing Neil Averitt, 'The Meaning of "Unfair Methods of Competition" in Section 5 of the FTC Act' (1980) 21 BC L REV 227, 229–40) <https://www.ftc.gov/system/files/documents/public_statements/1591498/final_statement_of_chair_khan_joined_by_rc_and_rks_on_section_5_0.pdf> accessed 27 June 2023.

[4] ibid, at 3.

[5] ibid, at 3. As Senator Albert Cummins, one of the FTC Act's chief proponents, put it, 'the only purpose of Section 5' was to 'prevent some things, that cannot [sic] be punished or prevented under the antitrust law'. See 51 Cong. Rec. 12454 (1914) (statement of Sen. Cummins).

[6] See, eg *FTC v Ind. Fed'n of Dentists*, 476 US 447, 454 (1986) (holding that '[t]he standard of "unfairness" under the FTC Act is, by necessity, an elusive one, encompassing not only practices that violate the Sherman Act and the other antitrust laws'); *FTC v Sperry & Hutchinson Co*, 405 US 233, 242 (1972) (holding that 'the Commission has broad powers to declare trade practices unfair'.); *FTC v Brown Shoe*, 384 US 316, 321 (1966) (holding that the FTC 'has broad powers to declare trade practices unfair[,] particularly . . . with regard to trade practices which conflict with the basic policies of the Sherman and Clayton Acts'); *Atl. Refin. Co. v FTC*, 381 US 357, 369 (1965) (holding that all that is necessary is to discover conduct that runs counter to the public policy declared in the Act . . . .' and that 'there are many unfair methods of competition that do not assume the proportions of antitrust violations'); *FTC v Colgate- Palmolive et al.*, 380 US 377, 384–85 (1965) (noting that the proscriptions in section 5 are flexible); *Pan Am. World Airways v United States*, 371 US 296, 306–308 (1963) ('[Section 5] was designed to bolster and strengthen antitrust enforcement[,] and the definitions are not limited to precise practices that can readily be catalogued. They take their meaning from the facts of each case and the impact of particular practices on competition and monopoly'); *FTC v Nat'l Lead Co.*, 352 US 419, 428–29 (1957) (affirming past rulings finding that the commission is clothed with 'wide discretion in . . . [bringing] an end to the unfair practices found to exist[;] . . . . [is] "the expert body to determine what remedy is necessary to eliminate the unfair or deceptive trade practices which have been disclosed[;] . . . has wide latitude for judgment and"[;] . . . [that] "to attain the objectives Congress envisioned, [the FTC] cannot be required to confine its road block to the narrow lane the transgressor has traveled"'); *Am. Airlines, Inc. v N. Am. Airlines, Inc.*, 351 US 79, 85 (1956) (finding that '"[u]nfair or deceptive practices or unfair methods of competition". . . are broader concepts than the common-law idea of unfair competition'); *FTC v Motion Picture Advert. Serv. Co.*, 344 US 392, 394–95 (1953) (noting that 'Congress advisedly left the concept [of unfair methods of competition] flexible . . . [and] designed it to supplement and bolster the Sherman Act and the Clayton Act[,] [so as] to stop . . . acts and practices [in their incipiency] which, when full blown, would violate those Acts[,] . . . as well as to condemn as 'unfair methods of competition' existing violations of them'); *FTC v Cement Inst.*, 333 US 683, 708 (1948) (holding that conduct that falls short of violating the Sherman Act may violate Section 5); *FTC v R.F. Keppel & Bro., Inc.*, 291 US 304, 310 (1934) (finding that unfair methods of competition not limited to those 'which are forbidden at common law or which are likely to grow into violations of the Sherman Act').

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enacted by Congress to particular business situations, so as to eradicate evils with the least risk of interfering with legitimate business operations.'[7]

In keeping with this consensus, through the late 1970s, the FTC frequently brought Section 5 cases against conduct that would not necessarily run afoul of the Sherman Act. We now call these 'standalone' Section 5 cases. They included invitations to collude;[8] price discrimination claims against buyers not covered by the Clayton Act;[9] de facto bundling,[10] tying, and exclusive dealing;[11] and many other practices.[12]

In the 1980s, however, the Commission backed away from bringing standalone Section 5 cases. This is sometimes attributed to the fact that the Commission lost three Section 5 cases in the first half of the decade.[13] There is a grain of truth to this: The losses were a genuine setback, and agency leaders understandably grew more cautious. But the abandonment of Section 5 cannot be explained by those defeats alone. None of the three rulings disputed the Commission's authority or narrowed the reach of Section 5. Rather, in each case, the courts held that the FTC had not met its factual or evidentiary burden.[14] At no point did the judiciary signal that standalone Section 5 cases were inherently suspect. The Commission's turn reflected a philosophical shift, not merely an agency turned gun-shy.

The retreat from standalone Section 5 cases culminated in the Commission's 2015 Statement of Enforcement Principles. In that statement, the Commission announced that the FTC would interpret Section 5 'under a framework similar to the rule of reason'.[15] This made Section 5 essentially coterminous with the Sherman Act, implying that we would only bring cases under the former that closely resemble cases that could be brought under the latter. It is difficult to square this decision with the fact that Congress specifically designed Section 5 to go beyond the confines of the Sherman Act and the rule of reason. The 2015 statement therefore departed from the plain text, purpose, structure, and history of the FTC Act. By declaring that the Commission would ignore a clear set of congressional instructions, it undermined our legitimacy. As enforcers, we of course must exercise discretion in deciding what cases to bring and how to use our limited resources. But we cannot simply ignore the text of our governing statutes and our core congressional mandate.[16] To do so would be to place ourselves above the people's elected representatives as the final arbiters of public policy.

7 *FTC v Texaco, Inc*, 393 US 223, 262 (1968).

8 *FTC v Cement Inst.*, 333 US 683.

9 *Alterman Foods v FTC*, 497 F.2d 993 (5th Cir. 1974); *Colonial Stores v FTC*, 450 F.2d 733 (5th Cir. 1971); *R.H. Macy & Co. v FTC*, 326 F.2d 445 (2d Cir. 1964); *Am. News Co. v FTC*, 300 F.2d 104 (2d Cir. 1962); *Grand Union Co. v FTC*, 300 F.2d 92 (2d Cir. 1962); *In re Foremost-McKesson, Inc.*, 109 FTC 127 (1987).

10 *Atl. Refin. Co. v FTC*, 381 US 357.

11 *FTC v Motion Picture Advert. Service Co.*, 344 US 392.

12 *Atl. Refin. Co. v FTC*, 381 US 357.

13 *Official Airline Guides, Inc. v FTC*, 630 F.2d 920 (2d Cir. 1980); *Boise Cascade Corp. v FTC*, 637 F.2d 573 (1980); *E.I. Du Pont de Nemours & Co. v FTC* 729 F.2d 128 (2d Cir. 1984) ('*Ethyl*').

14 See, eg Concurring Opinion of Commissioner Jon Leibowitz in the Matter of Rambus, Inc., Docket No 9302, at 7 (2 August 2006) <https://www.ftc.gov/sites/default/files/documents/cases/2006/08/060802rambusconcurringopinionofcommissionerleibowitz.pdf> accessed 27 June 2023; ('The decision in each, however, turns primarily on an evidentiary failure to demonstrate that the challenged conduct constituted an effort to acquire market power, tacitly collude, or manipulate price for anticompetitive purposes. *None* of these cases significantly constrains the FTC's authority to apply Section 5 to violations of the policies that underlie the antitrust statutes or that cause actual or incipient antitrust injury.' (emphasis original)).

15 Fed. Trade Comm'n, Statement of Enforcement Principles Regarding 'Unfair Methods of Competition' Under Section 5 of the FTC Act (13 August 2015) <https://www.ftc.gov/system/files/documents/public_statements/735201/150813section5enforcement.pdf> accessed 27 June 2023.

16 See, eg Opening Remarks by Chairman William Kovacic, Workshop on Section 5 of the FTC Act as a Competition Statute, at 4 (17 October 2008) [hereinafter Kovacic Remarks at Section 5 Workshop] (transcript available at <https://www.ftc.gov/sites/default/files/documents/public_events/section-5-ftc-act-competition-statute/transcript.pdf> accessed 27 June 2023) (describing Section 5 as 'a critical assumption upon which the agency itself was founded'.); see also ibid, at 5 ('If you pull Section 5 out of the mix of what the Commission does, I think you begin to ask profound questions about whether the institution ought to exist at all.').

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Accordingly, in 2021, the Commission voted to rescind the 2015 policy statement,[17] and in 2022 issued a new one to replace it. The new statement brings the agency back in line with its statutory obligations. It is based on the text, structure, purpose, and history of the FTC Act, as well as approximately 180 judicial opinions interpreting Section 5—including in cases where the Commission did not prevail. I encourage interested readers to read the policy statement in its entirety. Broadly speaking, it identifies the framework and factors the Commission will consider when determining whether a business practice constitutes an 'unfair method of competition'. It also identifies the types of justifications the Commission will and will not consider, in accordance with the relevant case law.

Critics have faulted the policy statement for not neatly setting out a bounded list of prohibited practices.[18] But this is by design—indeed, it is compelled by the statute itself. Lawmakers opted against a pre-specified list of proscribed tactics because they knew that such a list would quickly become outdated. Congress instead tasked the FTC with concretizing the meaning of 'unfair methods of competition' through litigation and rulemaking, informed by the agency's expertise and ability to do rigorous research into real-world markets and evolving business practices.[19] The purpose of the policy statement is to outline the framework and factors the Commission will use to do so, guided by many decades of agency experience and judicial precedent.[20]

The Commission's recent work on noncompete clauses illustrates this process in action. In January, we settled two cases involving the use of noncompete clauses to restrict workers. One case concerned a security-guard company that barred its workers—security guards earning at or near the minimum wage—from taking a job with another security company within a 100-mile radius for two years.[21] As the complaint alleges, the noncompete provision included a $100,000 liquidated damages clause. A state court had already ruled it unenforceable, but the company continued to include it in contracts anyway—perhaps sensing that its low-wage workers were unlikely to risk litigation and indeed were probably unaware that the clause was unenforceable. Taking these facts together, the Commission alleged that the use of noncompetes was coercive and exploitative toward the relevant workers, who lacked real bargaining power, and that it tended to harm competitive conditions by preventing the free flow of labour.

The second case concerned the use of noncompetes by two of the three largest manufacturers in the highly concentrated glass container industry.[22] As alleged in the complaint,

[17] Statement on 2015 Statement Withdrawal, (n 3).

[18] See, eg Dissenting Statement of Commissioner Christine S Wilson Regarding the 'Policy Statement Regarding the Scope of Unfair Methods of Competition Under Section 5 of the Federal Trade Commission Act' (10 November 2022) <https://www.ftc.gov/system/files/ftc_gov/pdf/P221202Section5PolicyWilsonDissentStmt.pdf> accessed 27 June 2023.

[19] *FTC v Texaco, Inc.*, 393 US at 226 ('While the ultimate responsibility for the construction of this statute rests with the courts, we have held on many occasions that the determinations of the Commission, an expert body charged with the practical application of the statute, are entitled to great weight.').

[20] Judges and scholars have noted that rule of reason poses serious administrability challenges. See, eg *FTC v Actavis, Inc.*, 570 US 136, 173 (2013) (Roberts, CJ, dissenting) ('[T]he majority declares that such questions should henceforth be scrutinized by antitrust law's unruly rule of reason. Good luck to the district courts that must, when faced with a patent settlement, weigh the "likely anticompetitive effects, redeeming virtues, market power, and potentially offsetting legal considerations present in the circumstances"'. (quoting ibid, at 149 (majority opinion))); *Leegin Creative Leather Prods., Inc. v PSKS, Inc.*, 551 US 877, 916 (2007) (Breyer, J, dissenting) ('How easily can courts identify instances in which the benefits are likely to outweigh potential harms? My own answer is, *not very easily*.'); Rebecca Haw Allensworth, 'The Commensurability Myth in Antitrust' (2016) 69 Vand L Rev 1; Maurice E Stucke, 'Does the Rule of Reason Violate the Rule of Law?' (2009) 42 UC Davis L Rev 1375, 1421–73.

[21] Press Release, Fed. Trade Comm'n, FTC Cracks Down on Companies That Impose Harmful Non-compete Restrictions on Thousands of Workers (4 January 2023) <https://www.ftc.gov/news-events/news/press-releases/2023/01/ftc-cracks-down-companies-impose-harmful-noncompete-restrictions-thousands-workers> accessed 27 June 2023.

[22] Press Release, Fed. Trade Comm'n, FTC Approves Final Orders Requiring Two Glass Container Manufacturers to Drop Noncompete Restrictions That They Imposed on Workers (23 February 2023) <https://www.ftc.gov/news-events/news/press-releases/2023/02/ftc-approves-final-orders-requiring-two-glass-container-manufacturers-drop-noncompete-restrictions> accessed 27 June 2023.

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these noncompetes locked up highly specialized workers, potentially depriving would-be entrants of the talent necessary to launch a new competitor. Section 5 is uniquely appropriate for this type of scenario, with a small number of dominant players engaging in the same restrictive practices with a cumulatively anticompetitive effect.

Finally, also in January, the Commission issued its Notice of Proposed Rulemaking to issue a rule generally prohibiting the use of noncompetes.[23] The proposal was based on an extensive review of empirical research and a voluminous record of public comments, from which staff drew several preliminary conclusions: that noncompetes systemically reduce aggregate worker income by an estimated $250–$296 billion; that workers rarely negotiate over noncompete clauses, and many aren't even presented with them until they have already begun their employment; that, rather than safeguarding innovation, the use of non-competes tends to stifle it by locking talent in place and creating barriers to entry for startups; and that more appropriate tools, such as tailored non-disclosure agreements and trade secret law, exist where there are genuine concerns over protecting company information.

This work illustrates how the Commission determines whether a given method of competition is unfair: through rigorous study of concrete, on-the-ground business realities, informed by market participants and guided by precedent. This does not mean there won't be difficult cases, that our judgment is infallible, or that the Commission will always prevail in court. It means simply that we will do the job Congress assigned us, even when that job is hard. Respect for democracy and the rule of law requires nothing less.

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23 Press Release, Fed. Trade Comm'n, FTC Proposes Rule to Ban Noncompete Clauses, Which Hurt Workers and Harm Competition (5 January 2023) <https://www.ftc.gov/news-events/news/press-releases/2023/01/ftc-proposes-rule-ban-noncompete-clauses-which-hurt-workers-harm-competition> accessed 27 June 2023.