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Legal Sidebar

UPDATE: Will the FTC Need to Rethink its Enforcement Playbook? Third Circuit Considers FTC's Ability to Sue Based on Past Conduct

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UPDATE: On February 25, 2019, the U.S. Court of Appeals for the Third Circuit (Third Circuit) affirmed the district court's judgment in the case FTC v. Shire ViroPharma, Inc. *The Third Circuit explained that, as a threshold to suing in federal court under Section 13(b) of the Federal Trade Commission Act, the Federal Trade Commission (FTC) must show that the defendant "is violating, or is about to violate" law. The court further construed the "is violating, or is about to violate" language as covering "existing or impending conduct." While it left defining the "exact confines" of the language "for another day," it rejected the FTC's interpretation that the standard could be met by merely showing a "past violation and a likelihood of recurrence." The court further rejected the FTC's "parade of horribles" argument, in which the FTC claimed that the court's interpretation would allow wrongdoers to evade enforcement by ceasing their illegal conduct. The court noted that, while the FTC's "understandable [enforcement] preference" is to litigate under Section 13(b), it can still enforce past violations by seeking cease-and-desist orders through administrative proceedings. After elucidating the "is violating, or is about to violate" standard, the court noted that Shire ViroPharma ceased its allegedly illegal conduct (sham petitioning to delay generic equivalents to its drug Vancocin) five years before the FTC brought suit. Furthermore, the FTC's complaint "lack[ed] specific allegations that Shire is 'about to violate' the law" by engaging in future sham petitioning. Consequently, the court concluded that the FTC failed to plead that Shire ViroPharma "is violating, or is about to violate" the law.*

The original post from December 18, 2018, is below.

On December 11, 2018, the U.S. Court of Appeals for the Third Circuit (Third Circuit) heard oral arguments in *FTC v. Shire ViroPharma, Inc.*, a case with potentially significant implications for the Federal Trade Commission's (FTC) enforcement authority. *Shire ViroPharma* deals with the scope of Section 13(b) of the Federal Trade Commission Act (FTC Act). As interpreted by numerous courts, Section 13(b) allows the FTC to sue companies in federal district court for a wide range of equitable

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relief. The FTC routinely uses Section 13(b) as its primary enforcement mechanism. However, the lower court's decision in *Shire ViroPharma* would, if upheld by the Third Circuit, likely make it more difficult for the FTC to bring Section 13(b) suits based on a defendant's past conduct. The district court held that the FTC must demonstrate in Section 13(b) suits that it has a "reason to believe" the defendant "is violating, or is about to violate" a law enforced by the FTC. This standard, according to the court, requires something more than simply showing that a future violation is "likely to recur."

This Sidebar begins by providing background on the FTC's competition and consumer protection authority and the evolution of enforcement under Section 13(b). The Sidebar then reviews the district court's decision in *Shire ViroPharma, Inc.*, discusses how the Third Circuit's decision may impact Section 13(b) enforcement, and raises potential considerations for Congress.

FTC's competition and consumer protection authority

Congress established the FTC in 1914 through the FTC Act, with the dual mission to protect consumers and promote competition in the marketplace. The FTC's competition and consumer protection authority primarily comes from Section 5 of the FTC Act. Section 5, since the time of its enactment, has granted the FTC authority over "unfair methods of competition." As the Supreme Court has recognized, "unfair methods of competition" encompasses both conduct that violates other antitrust statutes, such as the Sherman and Clayton Acts, as well as conduct in its "incipiency" that when "full blown" would violate these Acts.

In addition to "unfair methods of competition," Section 5, as amended by the Wheeler-Lea Act in 1938, prohibits "unfair or deceptive acts or practices in or affecting commerce" (UDAPs). Section 5's UDAP prohibition has formed the foundation of the FTC's consumer protection authority, and, given its importance, Congress and the FTC have clarified the types of acts or practices that are "unfair" or "deceptive." In 1994, Congress amended the FTC Act to codify prior FTC guidance on the unfairness standard. Under that provision, an act or practice is only "unfair" if it causes an injury to consumers that is: (1) substantial, (2) not reasonably avoidable by consumers, and (3) not outweighed by countervailing benefits to consumers or competition. While there is no statutory definition of "deceptive," the FTC has explained in guidance that an act or practice is deceptive if it involves a material "representation, omission, or practice that is likely to mislead [a] consumer" who is "acting reasonably in the circumstances."

Along with its UDAP authority, the FTC has enforcement authority over a number of other specific consumer protection statutes, such as the Children's Online Privacy Protection Act, Equal Credit Opportunity Act, and Telemarketing and Consumer Fraud and Abuse Prevention Act. The FTC has actively used its authority under Section 5 and other consumer protection statutes to bring enforcement actions against entities under its jurisdiction, which include almost all companies other than banks and common carriers. The FTC has brought enforcement actions based on a broad range of conduct, including advertising practices, debt collection and lending practices, and data privacy and security practices.

Evolution of FTC Enforcement under Section 13(b)

The FTC has stated that when it believes a particular person has violated any competition or consumer protection law over which it has enforcement authority, its preferred method of enforcement is to bring an action in federal court under Section 13(b) of the FTC Act. Section 13(b), which Congress added to the FTC Act in 1973 as part of the Trans-Alaska Pipeline Authorization Act, provides:

> "Whenever the Commission has reason to believe—

> (1) that any person, partnership, or corporation is violating, or is about to violate any provision of law enforced by the Federal Trade Commission, and
>
> (2) that the enjoining thereof pending the issuance of a complaint by the Commission and until such complaint is dismissed by the Commission or set aside by the court on review . . . would be in the interest of the public—
>
> The Commission . . . may bring suit in a district court of the United States to enjoin any such act or practice. Upon a proper showing that, weighing the equities and considering the Commission's likelihood of ultimate success, such action would be in the public interest . . . a temporary restraining order or a preliminary injunction may be granted without bond . . . *Provided further*, That in proper cases the Commission may seek, and after proper proof, the court may issue, a permanent injunction.

Courts often refer to Section 13(b) as being divided into two provisos. The first proviso—the text from the beginning of the provision to the phrase "*Provided further*"—authorizes the FTC to seek preliminary relief from a court while it conducts administrative proceedings. The second proviso—the text following the phrase "*Provided further*"—permits the FTC to seek a permanent injunction from a court in "proper cases." In the initial years after Section 13(b)'s enactment, the FTC primarily relied on the first proviso, using it to seek preliminary injunctions in federal court while its administrative enforcement proceedings were ongoing. In an administrative enforcement proceeding, an Administrative Law Judge hears the FTC's complaint against a respondent, and the FTC is limited to seeking cease-and-desist orders. It may seek civil penalties in federal district court only after a respondent violates a cease-and-desist order.

By the mid-1980s, however, the FTC increasingly used the second proviso as an independent basis to bring enforcement actions due to numerous U.S. courts of appeal interpreting the proviso broadly. Some circuit courts had held that the FTC could seek permanent injunctions under Section 13(b)'s second proviso without initiating administrative proceedings. Furthermore, several circuit courts held that the second proviso's express grant of a permanent injunction provided inherent power to grant all equitable relief. "Equitable" relief—historically meaning those remedies provided by the English Court of Chancery—includes injunctions, disgorgement, and restitution in contrast to "legal" remedies, such as damages or penalties. Relying on the Supreme Court doctrine that a district court may use all "inherent equitable powers" to enforce a statute unless "otherwise provided by a statute," circuit courts held that the FTC could seek all forms of equitable relief under Section 13(b)'s second proviso. Because of the wider range of equitable remedies available, the FTC prefers Section 13(b) actions over administrative enforcement.

Shire ViroPharma

The FTC may need to rethink this preference, however, if the Third Circuit upholds the district court's decision in *Shire ViroPharma.* In *Shire ViroPharma, Inc.*, the FTC sued the pharmaceutical company ViroPharma under Section 13(b) in U.S. District Court for the District of Delaware, seeking a permanent injunction and other equitable relief. The FTC alleged ViroPharma violated Section 5 of the FTC Act by filing meritless petitions with the U.S. Food and Drug Administration (FDA) designed to obstruct and delay approval of a genetic drug. ViroPharma moved to dismiss, arguing that the first proviso's threshold requirement that the FTC have a "reason to believe" the respondent "is violating, or is about to violate" the law also applies to suits under Section 13(b)'s second proviso.

The district court agreed with ViroPharma. Noting that ViroPharma's argument raised a "novel" issue that had not been decided by any other courts, the court analyzed the statute's text and structure. It reasoned that the second proviso's use of the phrase "may seek"—rather than the phrase "may bring suit," as used in the first proviso—demonstrates that Section 13(b) only gives the FTC authority to seek a permanent

injunction "once it is properly in federal court" pursuant to the first proviso. The court further noted that the manner in which the "second proviso follows from the first," including its use of the phrase "provided further," "demonstrates that [it] applies to cases already in federal court pursuant to the first proviso." In addition to these textual considerations, the court emphasized that the "limited legislative history" supported its conclusion. Citing a Senate Report, which states that the "purpose of the section" is to "bring an immediate halt" to unfair or deceptive acts or practices, the court concluded that Congress "intended for Section 13(b) to address violations requiring quick or immediate action by a federal district court."

After holding that the FTC must show a "reason to believe" that ViroPharma "is violating, or is about to violate" the law, the district court addressed the standard of proof for this showing. The court rejected the FTC's argument that it only had to show the violation was "likely to recur," which is the showing the FTC Act requires the FTC to make to obtain injunctive relief when the defendant has ceased the offending conduct. Reasoning that the FTC confused the standard for awarding a particular remedy with its authority to bring suit, the court noted that applying the "likely to recur" standard would "ignore the plain language of the statute." While the court did not articulate an alternative standard, it held that the facts alleged did not "plausibly suggest" that ViroPharma "'is about to violate' a law enforced by the FTC." The court reasoned that the alleged conduct "ceased five years before the filing of the complaint" and the FTC's complaint only stated in a "conclusory fashion" that there was a cognizable danger ViroPharma would engage in similar conduct. Accordingly, the court dismissed the FTC's complaint without prejudice, allowing leave for the FTC to amend its complaint.

Since the district court's decision in *ViroPharma*, at least one other district court has reached a similar conclusion regarding the scope of Section 13(b). In *FTC v. Hornbeam*, the U.S. District Court for the Northern District of Georgia similarly held that the "reason to believe" requirement in the first proviso "plainly creates a precondition to the FTC's statutory authority to bring suit" in Section 13(b) actions. Regarding the standard of proof, it agreed with *Shire ViroPharma* that the statute's "plain language" demanded a greater showing than the "likely to recur" standard for injunctive relief, noting that the phrase "about to violate" "evokes imminence." Beyond the *Hornbeam* court's specific holding on the "reason to believe" standard, it criticized more broadly, in dicta, the judicial "encrustations" that have been added to Section 13(b) over time. It noted in particular the "ubiquitous holdings of the courts of appeals" that equitable relief "other than injunctions is available" even though such relief is "not supported by the plain text of the statute."

Future of Section 13(b) and legislative considerations

The Third Circuit's decision in *Shire ViroPharma* may have significant implications for the future of FTC enforcement under Section 13(b). The Third Circuit's affirmance of the district court's opinion might impede the FTC's ability to bring enforcement actions based on defendants' past conduct. In its appellate brief, the FTC argued that it would need to allege specific facts showing that a future violation is imminent rather than citing past violations to argue that future violations are "likely to recur." As a consequence, if the Third Circuit holds that Section 13(b)'s "about to" language requires a showing of imminence, the FTC may need to rethink its enforcement strategy.

Beyond the "reason to believe" standard, the *Shire ViroPharma* and *Hornbeam* district courts' textualist approach to Section 13(b) may signal that courts may be willing to reconsider not only the standard for bringing an action under Section 13(b), but also the scope of relief available under the second proviso as previously interpreted by courts. Indeed, *Hornbeam*'s statement that equitable relief beyond injunctions is "not supported by the plain text of the statute" directly questions the panoply of equitable relief that courts have read into Section 13(b).

In light of these legal developments and the FTC's key role in competition and consumer protection enforcement, the scope of Section 13(b) may be of interest to Congress. As of now, no bills have been introduced in the 115th Congress that would amend this provision. However, certain issues remain unresolved, including (1) whether the FTC must show a "reason to believe" the defendant is "is violating, or is about to violate" the law before bringing suits under the second proviso, (2) the standard of proof for the "reason to believe" requirement, and (3) the range of equitable relief available in suits under the second proviso.

Author Information

Chris D. Linebaugh
Legislative Attorney

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