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Chris Jay Hoofnagle

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PART I

The history, powers, and procedure of the Federal Trade
Commission

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History of the Federal Trade Commission

INTRODUCTION

How did a small, independent antitrust agency come to be among the most important forces in consumer protection and privacy law? This chapter explains the founding of the Federal Trade Commission (FTC, “Agency,” or “Commission”), how it quickly pivoted to handle false advertising issues, and how its role and powers grew even while it was subject to periodic, withering criticism. Several themes emerge: First, the FTC has cycles where it is criticized for inactivity, but when it takes an activist posture, Congress sometimes punishes it. Second, until recently, the FTC has been plagued by mediocre appointments. Its reputation has improved greatly as a result of better appointments. Third, compromises in the passage of the FTC’s organic act (the Federal Trade Commission Act, or “FTC Act”) caused broad disagreements about the purpose of the Agency. Today, we see this as conflicts between those who want the FTC to help businesses comply with laws versus those who want it to strongly enforce laws. Fourth, the FTC was a revolutionary concept at its time, breaking away from the strictures imposed by the common law. Modern agency critics have never quite accepted the rationale for departing from the common law and seek to reimpose common law elements to cabin the Commission’s activities. Finally, the FTC’s genesis in antitrust and false advertising matters profoundly shapes how it handles all consumer protection issues, including privacy. Familiarity with FTC precedents in policing false advertising provides context for how the Agency addresses privacy.

The FTC was created in 1914 to address the problem of monopoly and of trusts – large, powerful business conglomerates. These organizations posed economic and social problems that became a major social concern.¹ The FTC did not formally have a consumer protection mission until the passage of the Wheeler–Lea Amendments in 1938. However, the FTC’s first reported matters concerned false

¹ For an early-twentieth-century summary of the trust problem, see JEREMIAH WHIPPLE JENKS, JR., *THE TRUST PROBLEM* (1903).

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advertising.² The FTC's early foray into advertising regulation came at the request of the advertising industry itself.³ These were matters where a deception, sometimes made directly to a consumer, harmed competition.

The 1938 amendments dramatically increased the power and jurisdiction of the FTC, as did the rise of the administrative state, subsequent amendments to the FTC Act, and judicial deference to the Agency.

The Agency's roots in the trust problem and the characteristics of the powers it needed to address it shed light upon the FTC's modern consumer protection mission. Similarly, the special dynamics of advertising regulation embedded in the FTC Act help inform its current efforts to police privacy.

THE PROBLEMS OF MONOPOLY AND TRUST

Business became "big" after the Civil War. A wave of consolidation and growth among companies triggered a public debate concerning "bigness." Through gentlemen's agreements, issuance of stock, and pooling arrangements, companies could fix prices and outputs, effectively stopping competition and raising prices for the consumer.⁴ Concerns were so intense that the period saw a break with dominant ideologies. The nineteenth century was the last period of a laissez-faire business environment. But the perceived unfairness and fears raised by consolidation caused even price controls to be considered as a remedy for heavily concentrated industries. The Progressive Era reflected an unparalleled antibusiness sentiment,⁵ and perhaps never in history has it been as intense as at the turn of the century.

This antibusiness sentiment was driven by a substantial number of mergers that gave control over key industries to small groups of businesses. Where companies did not merge, other arrangements could have the same effect of combination.⁶ Conglomerates controlled most or almost all of the relevant industries that produced

² See *FTC v. Yagle et al.*, 1 F.T.C. 13 (1916); *FTC v. Muenzen*, 1 F.T.C. 30 (1917). "In 1925, for example, the percentage of cases directed primarily to the protection of customers against deceptive trade practices constituted 70 percent of the whole number of complaints issued, as against the average of 59 percent for the preceding decade." Myron W. Watkins, *The Federal Trade Commission: A Critical Survey*, 40(4) Q. J. ECON. 561 (1926). The emphasis on false advertising only increased, according to Watkins. By 1932, 91 percent of cases concerned false advertising. Myron W. Watkins, *An Appraisal of the Work of the Federal Trade Commission*, 32(2) COLUMBIA L. REV. 272 (1932).

³ Commission minutes show an informal conference between all five commissioners and representatives of four advertising self-regulatory groups in November 1915. This attention to deceptive advertising came in part from requests from advertiser self-regulatory groups such as the Associated Advertising Clubs of the World and the Vigilance Committee, which urged the Agency to consider false advertising as a form of unfair competition. Jack Crespin, *A History of the Development of the Consumer Protection Activities of the Federal Trade Commission* 112 (1975)(Ph.D. dissertation, New York University). See also Daniel Pope, *Advertising as a Consumer Issue: An Historical View*, 47(1) J. SOC. ISSUES 41 (1991).

⁴ FRANCIS W. HIRST, *MONOPOLIES, TRUSTS AND KARTELLS* (1905).

⁵ RICHARD HOFSTADTER, *THE PARANOID STYLE IN AMERICAN POLITICS AND OTHER ESSAYS* (1964).

⁶ See Louis D. Brandeis, *How the Combiners Combine*, 58 HARPER'S WEEKLY, November 13, 1913.

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household necessities. Goods used in production were also the products of highly concentrated trusts, such as the United States Steel Corporation and the International Paper Company. Concerns about industrialization and a changing economy, with shifting norms for personal lives, triggered a popular antitrust movement.

By 1888, both the Republican and Democratic parties included measures to address trusts in their party platforms. States began to regulate trusts through railroad commissions, and by 1890 Congress enacted the Sherman Act to address the trusts. In enacting it, Congress prohibited “every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations.”⁷ Congress took a broad approach, similar to the strategy it applied almost twenty-five years later in creating the FTC. Nevertheless, mergers continued and even accelerated. United States Steel became the first billion-dollar corporation, and by 1900, this single company produced most steel in the nation. Increased concentration was attributed to the Sherman Act’s provisions (which were so broad that they invited judges to evaluate the reasonableness of restraints of trade), to inadequate prosecutorial resources, to a prosecutorial concentration on the biggest trusts, and to the powerful economic factors that caused firms to merge.⁸

THE PROGRESSIVE PARTY PLATFORM OF 1912

We believe that true popular government, justice and prosperity go hand in hand, and so believing, it is our purpose to secure that large measure of general prosperity, which is the fruit of legitimate and honest business, fostered by equal justice and by sound progressive laws.

We demand that the test of true prosperity shall be the benefits conferred thereby on all the citizens not confined to individuals or classes and that the test of corporate efficiency shall be the ability better to serve the public; that those who profit by control of business affairs shall justify that profit and that control by sharing with the public the fruits thereof.

We therefore demand a strong National regulation of inter-State corporations. The corporation is an essential part of modern business. The concentration of modern business, in some degree, is both inevitable and necessary for National and international business efficiency. But the existing concentration of vast wealth under a corporate system, unguarded and uncontrolled by the

⁷ Sherman Antitrust Act, 26 Stat. 208 (1890).

⁸ See generally GERALD C. HENDERSON, *THE FEDERAL TRADE COMMISSION: A STUDY IN ADMINISTRATIVE LAW AND PROCEDURE* (1924); Huston Thompson, *Highlights in the Evolution of the Federal Trade Commission*, 8 GEO. WASH. L. REV. 257 (1939). For an exhaustive overview of antitrust challenges of the time, see JOSEPH E. DAVIES, *TRUST LAWS AND UNFAIR COMPETITION* (1916).

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Nation, has placed in the hands of a few men enormous, secret, irresponsible power over the daily life of the citizen – a power insufferable in a free government and certain of abuse.

This power has been abused, in monopoly of National resources, in stock watering, in unfair competition and unfair privileges, and finally in sinister influences on the public agencies of State and Nation. We do not fear commercial power, but we insist that it shall be exercised openly, under publicity, supervision and regulation of the most efficient sort, which will preserve its good while eradicating and preventing its evils.

To that end we urge the establishment of a strong Federal administrative commission of high standing, which shall maintain permanent active supervision over industrial corporations engaged in inter-State commerce, or such of them as are of public importance, doing for them what the Government now does for the National banks, and what is now done for the railroads by the Inter-State Commerce Commission.

Such a commission must enforce the complete publicity of those corporation transactions which are of public interest; must attack unfair competition, false capitalization and special privilege, and by continuous trained watchfulness guard and keep open equally to all the highways of American commerce.

Thus the business man will have certain knowledge of the law, and will be able to conduct his business easily in conformity therewith; the investor will find security for his capital; dividends will be rendered more certain, and the savings of the people will be drawn naturally and safely into the channels of trade.

Under such a system of constructive regulation, legitimate business, freed from confusion, uncertainty and fruitless litigation, will develop normally in response to the energy and enterprise of the American business man.⁹

The Supreme Court's 1911 decision in *Standard Oil v. United States* was a watershed moment for the creation of the FTC. In *Standard Oil*, the Court applied a "rule of reason" to Sherman Act cases, in effect holding that the government could not prevent all activities in restraint of trade. Instead, courts would evaluate the context and fairness of contracts. Unreasonable restraints of trade violated the Sherman Act, and judges would ultimately decide what was reasonable and what was not. Presumably, conservative judges would find trusts acceptable, leading to a general unraveling of antitrust policy.

A rule of reason for antitrust meant the death of the Sherman Act to some, and for different reasons, both businesses and individuals clamored for intervention.¹⁰ Businesses were concerned that the economic theories of the Supreme Court and

⁹ Platform of the Progressive Party, August 7, 1912.

¹⁰ Dow Votaw, *Antitrust in 1914: The Climate of Opinion*, 24 ABA ANTITRUST SEC. 14 (1964).

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inferior tribunals could result in no or unpredictable enforcement. Additionally, prosecution of the Sherman Act, if left to the attorney general, could become too political, and thus it needed to be cared for by an independent agency.

Others thought the prevention of unlimited economic power animated the Sherman Act, and whether this power resulted in unreasonable restraints of trade was beside the point. Economic power itself had to be checked. Thus a rule of reason that parsed out efficient versus inefficient arrangements did not serve the political end of ensuring liberty against market power. For instance, declaring “the trusts have won,” William Jennings Bryan devoted seven pages of critique and analysis of the decision in his weekly progressive newspaper, *The Commoner*, eleven days after the decision was released.¹¹

THE DEMOCRATIC PARTY PLATFORM OF 1912

A private monopoly is indefensible and intolerable. We therefore favor the vigorous enforcement of the criminal as well as the civil law against trusts and trust officials, and demand the enactment of such additional legislation as may be necessary to make it impossible for a private monopoly to exist in the United States.

We favor the declaration by law of the conditions upon which corporations shall be permitted to engage in interstate trade, including, among others, the prevention of holding companies, of interlocking directors, of stock watering, of discrimination in price, and the control by any one corporation of so large a proportion of any industry as to make it a menace to competitive conditions.

We condemn the action of the Republican administration in compromising with the Standard Oil Company and the tobacco trust and its failure to invoke the criminal provisions of the antitrust law against the officers of those corporations after the court had declared that from the undisputed facts in the record they had violated the criminal provisions of the law.

We regret that the Sherman antitrust law has received a judicial construction depriving it of much of its efficiency and we favor the enactment of legislation which will restore to the statute the strength of which it has been deprived by such interpretation.¹²

The concern about economic power occupied a central role in political debates, with critics of “bigness” arguing that concentration was an affront not only to household economics but also to political freedom itself.¹³ The word “tyranny”

¹¹ Williams Jennings Bryan, *The Trusts Have Won*, 11(20) *THE COMMONER*, May 26, 1911.

¹² Democratic Party Platform of 1912, June 25, 1912.

¹³ Rudolph J. Peritz, *The “Rule of Reason” in Antitrust Law: Property Logic in Restraint of Competition*, 40 *HASTINGS L. J.* 285 (1988–1989); RICHARD HOFSTADTER, *THE PARANOID STYLE IN AMERICAN POLITICS AND OTHER ESSAYS* (1964).

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was invoked to describe the problem not of government power but of economic concentration.¹⁴ Far from its agrarian roots, the country had evolved to a nation of employees, as then antitrust advocate (and sometimes lawyer to trusts)¹⁵ Louis D. Brandeis put it. Brandeis published an eleven-part series of editorials in *Harper's Weekly* castigating the trusts for their "curse of bigness" and calling them "inefficient oligarchs." The spirit of these skeptics of bigness is reflected today in advocates calling for the FTC to police the powers gained from aggregation of personal information.

THE REPUBLICAN PARTY PLATFORM OF 1912

The Republican party is opposed to special privilege and to monopoly. It placed upon the statute-book the interstate commerce act of 1887, and the important amendments thereto, and the antitrust act of 1890, and it has consistently and successfully enforced the provisions of these laws. It will take no backward step to permit the reestablishment in any degree of conditions which were intolerable.

Experience makes it plain that the business of the country may be carried on without fear or without disturbance and at the same time without resort to practices which are abhorrent to the common sense of justice. The Republican party favors the enactment of legislation supplementary to the existing antitrust act which will define as criminal offences those specific acts that uniformly mark attempts to restrain and to monopolize trade, to the end that those who honestly intend to obey the law may have a guide for their action and those who aim to violate the law may the more surely be punished. The same certainty should be given to the law prohibiting combinations and monopolies that characterize other provisions of commercial law; in order that no part of the field of business opportunity may be restricted by monopoly or combination, that business success honorably achieved may not be converted into crime, and that the right of every man to acquire commodities, and particularly the necessities of life, in an open market uninfluenced by the manipulation of trust or combination, may be preserved.

Federal Trade Commission

In the enforcement and administration of Federal Laws governing interstate commerce and enterprises impressed with a public use engaged therein, there

¹⁴ At this same time, Americans were awakening to the idea that the power of private actors created problems for personal privacy. See David J. Seipp, *The Right to Privacy in American History* (July 1978) (Ph.D. dissertation, Harvard University).

¹⁵ THE WASHINGTON POST, BRANDEIS THE REFORMER, July 26, 1912 (attacking Brandeis for trust-busting activities while representing the Western Shoe Trust).

is much that may be committed to a Federal trade commission, thus placing in the hands of an administrative board many of the functions now necessarily exercised by the courts. This will promote promptness in the administration of the law and avoid delays and technicalities incident to court procedure.¹⁶

DYNAMICS OF SOLVING THE TRUST PROBLEM

To address the trust problem, Congress chose to endow an agency with a number of different attributes. Later in 1938, when Congress explicitly gave the FTC a consumer protection mission, these attributes shaped how the Agency dealt with consumer problems. The attributes are well suited for the FTC's modern role in policing privacy.

The need for expertise

In 1903, Congress created the Bureau of Corporations to help document and understand the trust problem. Empowered to investigate and make recommendations about the regulation of almost all industries, it served an information forcing and investigatory role against the trusts.¹⁷ As a component of the then Department of Commerce and Labor, the Bureau of Corporations was partisan and subject to control of the ruling executive. The Bureau of Corporations reported on several industries and the Agency's investigative activity helped focus the antitrust enforcement of the attorney general.

The need for certainty

After the 1911 *Standard Oil* decision, a number of factors militated toward the creation of some entity more powerful than the Bureau of Corporations. Supporters of greater antitrust enforcement felt that the Bureau's investigation and publicity functions were inadequate. The business community felt that the Sherman Act was too broad and that it provoked too much uncertainty.¹⁸ Business leaders also thought that it was unfair to be sued by the attorney general for violation of its terms, given its breadth. The business community wanted to avoid the chill of the Sherman Act by having options to obtain advice and even clearance and immunity from prosecution when that advice was followed.¹⁹ There was also a great concern that

¹⁶ Republican Party Platform of 1912, June 18, 1912.

¹⁷ Act Establishing the Department of Commerce and Labor, Pub. L. No. 57–87, § 6, 32 Stat. 825 (1903).

¹⁸ Danny A. Bring, *The Origins of the Federal Trade Commission Act: A Public Choice Approach* (1993) (Ph.D. dissertation, George Mason University).

¹⁹ Woodrow Wilson, Address to a Joint Session of Congress on Trusts and Monopolies, January 20, 1914 (“The business of the country awaits also, has long awaited and has suffered because it could not obtain, further and more explicit legislative definition of the policy and meaning of the existing

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judges would apply their own economic ideas about trusts in Sherman Act cases, and that an expert body should make these decisions.

The need for flexibility

The legislative process revealed the many limitations of laws that banned specific business wrongdoing. The kinds of unfair behavior were too numerous to enumerate, and legislative prohibitions of them invited businesses to engage in practices that fell though minor loopholes.²⁰ To address the trust problem, Congress eventually took both the specific prohibition (in the Clayton Act) and the broad prohibition approach in the FTC Act.

The need for quick, preventative action

The Sherman Act approach tended to focus prosecution on industries that had already consolidated. There was a need for an agency to focus on incipient concentration and on smaller trusts. Joseph Davies, who then directed the Bureau of Corporations, recommended to President Wilson that the FTC have a quasi-judicial role. Under Davies' proposal, which was largely adopted, the FTC could make findings and formal recommendations to companies to take effect in sixty days, thereby aiding the courts and providing a quick remedy.²¹

The need for compromise

The trust problem invoked strongly held beliefs that went to the core of individuals' political identity. A product of compromise, the FTC Act's vagueness allowed different political actors to ascribe different and conflicting purposes for the Agency. The FTC Act's legislative process gave the Agency two functions:

antitrust law. Nothing hampers business like uncertainty. Nothing daunts or discourages it like the necessity to take chances, to run the risk of falling under the condemnation of the law before it can make sure just what the law is. Surely we are sufficiently familiar with the actual processes and methods of monopoly and of the many hurtful restraints of trade to make definition possible, at any rate up to the limits of what experience has disclosed. These practices, being now abundantly disclosed, can be explicitly and item by item forbidden by statute in such terms as will practically eliminate uncertainty, the law itself and the penalty being made equally plain [...] And the business men of the country desire something more than that the menace of legal process in these matters be made explicit and intelligible. They desire the advice, the definite guidance and information which can be supplied by an administrative body, an interstate trade commission.")

²⁰ Eugene R. Baker & Daniel J. Baum, Section 5 of the Federal Trade Commission Act: A Continuing Process of Redefinition, 7 VILL. L. REV. 517 (1962).

²¹ Joseph E. Davies, Memorandum of Recommendations as to the Trust Legislation by Joseph E. Davies, Commissioner of Corporations, in ARTHUR S. LINK, THE PAPERS OF WOODROW WILSON, Vol. 29, pp. 78–85 (1979).