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Reconsidering Fictitious Pricing

David Adam Friedman

Article

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David Adam Friedman[†]

INTRODUCTION

On Black Friday, 2014, United States Senator Richard Blumenthal stood in front of a prominent regional retail outlet mall[1] to "look at some of the merchandise and see what shoppers [were] doing."[2] Earlier that day, Senator Blumenthal expressed concern "that some outlet store bargains featuring allegedly reduced prices on brand name products may actually be selling goods of lesser quality using deceptive pricing."[3] The Senator, invoking a "where there's smoke, there's fire" argument, remarked that eleven class action lawsuits had been filed nationally involving deceptive-pricing practices at retail outlet stores.[4] His public demonstration echoed a letter he and three other members of Congress had sent to the chairwoman of the Federal Trade Commission (FTC), urging enforcement action against outlet stores engaging in deceptive pricing, including

† Associate Professor of Law, Willamette University. B.A., Yale College; J.D., Yale Law School. Thank you to Laura Appleman, Curtis Bridgeman, Jim Hawkins, Chris Jay Hoofnagle, Michael Mannheimer, Peter Molk, Jeffrey Standen, Ahmed Taha, and Spencer Weber Waller for extensive comments. The faculties of Northern Kentucky Chase College of Law and the Willamette University College of Law also offered insights and suggestions, as did participants at the 2015 International Contracts Conference at UNLV Boyd School of Law. Librarian Mary Rumsey provided valuable support.

1. The Federal Trade Commission (FTC) defines "outlet stores" as "retail stores, shops and other establishments in which manufacturers sell their stock and other merchandise directly to the public through factory-direct-to-consumer branded store locations at discounted prices, and which are often used by manufacturers to liquidate stock." Simon Prop. Grp., Inc., 151 F.T.C. 23, 36 (2011).

2. Gregory B. Hladky, *Blumenthal Warns Holiday Shoppers About Outlets Using Deceptive Pricing, Advertising*, HARTFORD COURANT (Nov. 28, 2014), http://www.courant.com/politics/hc-blumenthal-outlet-shop-warning-20141128-story.html.

3. *Id.*

4. *Id.*

representing current prices as discounts from a fictitious regular price.[5] This letter marked the highest profile federal-level call to address fictitious-pricing practices in decades. The FTC, after decades of frequent enforcement, ceased prosecution of fictitious-pricing actions in 1969.[6]

Beyond congressional letters and press events, the acceleration of deceptive discount pricing practices has drawn critiques from other quarters. Referring to advertised discounts as "silliness," a former senior Sears executive confessed to the *Wall Street Journal*, that "the original price from which [a retail-price] discount is computed is often specious . . . because items hardly ever sell at that price, which makes the discount less legitimate."[7]

This Article uses "fictitious pricing" to describe this common advertising tactic frowned upon by the FTC Guides. Advertisers offer discounts based off a prior-reference price. An item advertised for sale at $80 at "20% off" presumably was offered for sale in good faith at a reference price of $100. If the advertiser never offered the good at $100, the prior-reference price was "fictitious," rendering the entirety of the price presentation "fictitious." The FTC Guides advise sellers that "[i]f . . . the former price being advertised is not bona fide but fictitious—for example, where an artificial, inflated price was established for the purpose of enabling the subsequent offer of a large reduction—the 'bargain' being advertised is . . . *false*."[8]

5. *See* Letter from Sheldon Whitehouse, U.S. Senator, et al. to Edith Ramirez, Chairwoman, Fed. Trade Comm'n (Jan. 30, 2014), http://www.whitehouse.senate.gov/news/release/sens-and-rep-to-ftc-outlet-stores-may-be-misleading-consumers. The FTC declined the invitation to investigate the allegations because it had not "received enough consumer complaints." Hladky, *supra* note 2. Blumenthal deemed this a "ridiculous, ludicrous reason," because "the FTC has no particular threshold number of consumer complaints necessary to trigger a probe." *Id.* Also, an individual consumer may have difficulty detecting harm through the fog of the deceptive scheme.

6. The last standalone FTC mention of "fictitious" pricing appeared in an order on December 31, 1970, a follow-through of a holdover complaint filed in 1969. *See* Hollywood Credit Clothing Co., 77 F.T.C. 1594, 1604–05 (1970). In 1969, the FTC confronted high-profile, broad, and blunt critiques that through "bureaucratic inertia" and "lethargy," the agency had an unfortunate tradition of wasting resources on "trivial pursuits." Matthew A. Edwards, *The FTC and New Paternalism*, 60 ADMIN. L. REV. 323, 343–44, 349 (2008); *see also* William MacLeod et al., *Three Rules and a Constitution: Consumer Protection Finds Its Limits in Competition Policy*, 72 ANTITRUST L.J. 943, 943 (2005).

7. Suzanne Kapner, *The Dirty Secret of Black Friday "Discounts*,*"* WALL ST. J. (Nov. 25, 2013), http://www.wsj.com/articles/SB10001424052702304281004579217863262940166.

8. 16 C.F.R. § 233.1 (2014) (emphasis added).

As a marketing practice, discount advertising, bona fide and fictitious, has proliferated recently.[9] Discounting has increased in frequency and in degree. According to one analysis, from 2009 to 2012, the number of discount offers increased sixty-three percent.[10] Over the same time period, the average discount offered moved from twenty-five percent to thirty-six percent.[11] Given the increased frequency of overall discounting, does fictitious pricing warrant concern? Does fictitious pricing inflict harm?

An individual or collective *remedy* may be challenging to frame for consumers claiming that false prior-reference prices induced their transaction. However, "a large body of evidence show[s] that the presence of a reference price increases consumers' deal valuations and purchase intentions and can lower their search intentions . . . ."[12] Writ large, this type of practice has a broad effect on the integrity of competition in retail markets and consumer welfare, which regulators should address. Basic behavioral economics amplifies the effect of fictitious pricing because the tactic can induce transactions by enhancing the perceived value of a transaction. For welfare reasons, deceptive-pricing practices deserve renewed scrutiny.

Though a dormant area for public federal enforcement since 1969,[13] private litigants recently have invoked fictitious

9. *See* Larry D. Compeau et al., *Comparative Price Advertising: Believe It or Not*, 36 J. CONSUMER AFF. 284, 284 (2002) ("Advertisers' attempts to enhance consumers' perceptions of the value of a deal by using comparative price advertisements, in which they . . . compare the selling price to some suggested reference price, is widespread . . . . [A] crucial issue concerns the deceptive power of comparative price advertising that provides inflated and exaggerated reference prices.").

10. Kapner, *supra* note 7 (describing tracking of discount practices at thirty-one retailers).

11. *Id.*

12. Gorkan Ahmetoglu et al., *Pricing Practices: A Critical Review of Their Effects on Consumers*, 21 J. RETAILING & CONSUMER SERVS. 696, 699 (2014); *see, e.g.*, Dhruv Grewal & Larry D. Compeau, *Comparative Price Advertising: Informative or Deceptive?*, 11 J. PUB. POL'Y & MARKETING 52, 55–58 (1992) [hereinafter Grewal & Compeau, *Comparative Price Advertising*] (containing a meta-analysis cited by the Ninth Circuit in *Hinojos* and serving as a "credible basis" for Professor Compeau's testimony in the *Overstock.com* litigation). A more recent analysis also supported findings that fictitious pricing negatively affects welfare. *See* Mark Armstrong & Yongmin Chen, *Discount Pricing* 25–26 (Univ. of Oxford, Dep't of Econ., Discussion Paper Series No. 605, 2012), http://www.economics.ox.ac.uk/materials/papers/5819/paper605.pdf.

13. *See* discussion *supra* note 6; *see also* Carleton A. Harkrader, *Fictitious Pricing and the FTC: A New Look at an Old Dodge*, 37 ST. JOHN'S L. REV. 1, 3–4 (1962) (noting that fictitious pricing actions emerged as the "leading type of deception practiced in violation of the FTC Act").

pricing claims with mixed results—in part because harm proves difficult for private litigants to allege.[14] A recent spate of private class actions involving retail-outlet fictitious pricing,[15] if successful, may resurrect scrutiny of this suspect advertising practice. Some states have sporadically filled the federal enforcement vacuum,[16] bringing different statutory standards,[17]

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14. For a typical result favoring the advertiser, see *Kim v. Carter's, Inc.*, 598 F.3d 362, 365–66 (7th Cir. 2010) (holding that there was no identifiable pecuniary harm to the consumer if an item was sold at a discount from a fictitious price because the actual price charged at the point-of-sale served as the contractual price); *see also* B. Sanfield, Inc. v. Finlay Fine Jewelry Corp., 258 F.3d 578 (7th Cir. 2001) (affirming judgment where a small retailer failed to prove that a competitor's fictitious pricing caused harm); Johnson v. Jos. A. Bank Clothiers, Inc., No. 2:13-cv-756, 2014 WL 4129576 (S.D. Ohio Aug. 19, 2014) (dismissing class action claims for failure to allege actual damages); Camasta v. Omaha Steaks Int'l, Inc., No. 1:12-cv-08285, 2013 WL 4495661 (N.D. Ill. Aug. 21, 2013) (dismissing a claim brought under Illinois Consumer Fraud and Deceptive Business Practices Act); Camasta v. Jos. A. Bank Clothiers, Inc., No. 12 C 7782, 2013 WL 3866507 (N.D. Ill. July 25, 2013) (dismissing a consumer complaint for failure to allege actual damages); Mulligan v. QVC, Inc., 888 N.E.2d 1190 (Ill. App. Ct. 2008) (granting summary judgment to a retailer when a consumer failed to establish damages). For an atypical result favoring the consumer, see *Hinojos v. Kohl's Corp.*, 718 F.3d 1098, 1105 (9th Cir. 2013) where the plaintiff consumer successfully

> allege[s] an economic injury under [California statutes]. [He alleges] that the advertised discounts conveyed false information about the goods he purchased, i.e., that the goods he purchased sold at a substantially higher price at [the retailer] in the recent past and/or in the prevailing market. He also alleges that he would not have purchased the goods in question absent this misrepresentation.

This was deemed sufficient for the plaintiff to proceed.

15. As of December 2014, at least eleven private civil complaints about fictitious pricing in retail outlet stores had been filed. *See, e.g.*, Complaint, Rubenstein v. Neiman Marcus Grp. L.L.C., No. CV 14-07155 SJO (JPRx) (C.D. Cal. Mar. 2, 2015), 2015 WL 1841254; Complaint, Branca v. Nordstrom, Inc., No. 3:14-cv-2062 MMA JMA (S.D. Cal. Sept. 2, 2014), 2014 WL 4313226; First Amended Complaint, Gattinella v. Michael Kors (USA), Inc., No. 1:14-cv-5731 (WHP) (S.D.N.Y. Sept. 2, 2014). It does appear that some of these cases were brought by the same law firm in a coordinated manner.

16. *See, e.g.*, People v. Overstock.com, Inc., No. RG10-546833, 2014 WL 657516 (Cal. Super. Ct. Feb. 5, 2014) (finding Overstock.com in violation of California Fair Advertising Law); Assurance of Discontinuance Pursuant to New York Executive Law § 63(15), *In re* Michaels Stores, Inc. (2011) [hereinafter Assurance of Discontinuance, Michaels] (on file with author) (consent decree between New York Attorney General and Michaels Stores concerning misleading sales promotions); Assurance of Discontinuance Pursuant to New York Executive Law § 63(15), *In re* Jos. A Bank Clothiers, Inc. (2004) [hereinafter Assurance of Discontinuance, Jos. A. Bank], http://www.ag.ny.gov/sites/default/files/press-releases/archived/sep14a_04_attach1.pdf (consent decree between retailer and the New York Attorney General that includes a mandate for the retailer to comply with the FTC Guides on Prior-Reference Pricing).

17. *See generally* Robert Pitofsky et al., *Pricing Laws Are No Bargain for Consumers*, 18 ANTITRUST 62, 64 (2004) [hereinafter Pitofsky, *Pricing Laws*]

complicating compliance for national retailers.[18] If these private and state actions prove unsuccessful and yield uneven results, the FTC should consider, in measured form, resurrecting enforcement of fictitious pricing in a manner that directly addresses welfare harm from the practice.

The FTC discontinued enforcement of fictitious pricing because, as Robert Pitofsky[19] explained in 1977, the Commission determined that discount retailers needed to be nurtured to foster price competition.[20] Regulatory intervention, Pitofsky argued, would dampen the aggression of these rising retailers. Today's retail marketplace, however, presents a vastly changed landscape that compels reconsideration of enforcement.

Public intervention would be required to dampen fictitious pricing, given that private civil actions and piecemeal state actions have not effectively addressed this growing phenomenon. In Part I, this Article describes and adopts the FTC's definition of fictitious pricing. This Article further explains, using basic tenets of behavioral economics, why discount pricing proves effective, which further informs why fictitious pricing warrants extra scrutiny. In Part II, this Article describes the challenge of conceptualizing individual harm and fashioning appropriate direct remedies for consumers. Recent private litigation under Illinois and California law illustrates these challenges. Part III presents evidence of a broader, negative welfare impact from fictitious pricing, justifying a degree of regulatory intervention. This Article explores the literature supporting this conclusion. This Article further argues that the courses recently taken in California and New York mirror a sensible analytical framework for regulators. In Part IV, this Article prescribes exploring targeted federal regulatory intervention to dampen fictitious-pricing practices, after a nearly fifty-year hiatus. The FTC should start by regulating in narrower spheres where retailers emphasize discounts of high-quality brands, or heavily market their sales channels as discount-focused. Federal regulation would proactively enable retailers to enjoy the uniformi-

(describing the practical difficulties created by varying state laws).

18. *See generally id.* at 63–64.

19. Pitofsky has been described as a "Founding Father" of the "modern Federal Trade Commission." Timothy Muris, *Robert Pitofsky: Public Servant and Scholar*, 52 CASE W. RES. L. REV. 25, 25 (2001).

20. Robert Pitofsky, *Beyond Nader: Consumer Protection and the Regulation of Advertising*, 90 HARV. L. REV. 661, 687–88 (1977) [hereinafter Pitofsky, *Beyond Nader*]. In a shorter piece in 2004, Pitofsky reiterated similar concerns about enforcing fictitious pricing. *See* Pitofsky, *Pricing Laws*, *supra* note 17, at 62.

ty that state enforcement will not offer.[21]

I. FICTITIOUS PRICING AND THE POWER OF DISCOUNT ADVERTISING

In early years, the FTC prosecuted fictitious-pricing actions without any guidance to sellers about how to comply with standards for pricing. In 1958, the FTC first brought form to the boundaries of lawful prior-reference pricing through the promulgation of the Guides Against Deceptive Pricing.[22] The FTC relaxed the Guides in 1964,[23] and in 1967 it shaped them into their current form.[24] Until 1969, FTC fictitious-pricing actions were fairly common.[25] After a major overhaul of the FTC and the Commission's priorities in the early Nixon Administration,[26] federal public enforcement stopped completely, and this posture holds today.[27] Moving to the present, in December of

21. *See generally* Pitofsky, *Pricing Laws*, *supra* note 17, at 63–64. (advocating for the eradication of state regulation).

22. Guides Against Deceptive Pricing, 23 Fed. Reg. 7965 (Oct. 15, 1958).

23. 16 C.F.R. § 14.10(a)(2) (1966) (adopted Jan. 8, 1964).

24. 16 C.F.R. § 233.1(a) (2015); 32 Fed. Reg. 15534–36 (Nov. 8, 1967). This version of the Guides enjoyed a short shelf life for FTC usage, given subsequent non-enforcement.

25. Right until the drastic changes of 1969, the FTC continued to pursue enforcement vigorously and with a measure of institutional pride. In the 1968 FTC Annual Report, the FTC prominently mentioned fictitious pricing: "In addition to . . . complaint[s] received by mail, 570,142 . . . advertisements were monitored . . . to determine how best they could be corrected. The diversity was legion but among the favorites were . . . . fictitious pricing of countless products." FTC, ANNUAL REPORT OF THE FEDERAL TRADE COMMISSION 8 (1968).

26. Edward F. Cox, *Reinvigorating the FTC: The Nader Report and the Rise of Consumer Advocacy*, 72 ANTITRUST L.J. 899, 900–01 (2005). Cox, the author of the article, was a "Raider." *Id.* at 899; *see also* ABA, REPORT OF THE ABA COMMISSION TO STUDY THE FEDERAL TRADE COMMISSION 86, 95 (1969) [hereinafter 1969 ABA REPORT] (criticizing the direction of the FTC prior to 1969); RICHARD A. HARRIS & SIDNEY M. MILKIS, THE POLITICS OF REGULATORY CHANGE 165 (2d ed. 1996) (describing changes to the FTC in the late 1960s); JUSTIN MARTIN, NADER: CRUSADER, SPOILER, ICON 81 (2002) ("Nader's FTC raid really did accomplish something; his seven children really did manage to lead the adults. In 1969 Richard Nixon, newly elected as president, asked the American Bar Association to conduct an independent investigation of the FTC. [The ABA's conclusions were] remarkably similar to the conclusions of Nader's Raiders . . . ."); Letter from President Richard Nixon to William T. Gossett, President, Am. Bar Ass'n (Apr. 18, 1969).

27. *See* discussion *supra* note 6. In 1980, all four instances of "fictitious pricing" behavior referenced in FTC consent judgments were accompanied by primary charges of related deceptive practices, like bait-and-switch, or false energy-saving claims. FTC, ANNUAL REPORT OF THE FEDERAL TRADE COMMISSION 26–27 (1980). After 1980, all mentions of "fictitious pricing" completely disappeared from the FTC Reporter.

2014 the *New York Times* presented findings[28] from the shopping-advocacy websites *The Wirecutter*[29] and *Sweethome*[30] that less than one percent of 54,000 "holiday deals," were "worth your time."[31] Not all of these deals were deemed "bad deals" due to improper discounting. However, the website researchers singled out as "one of the most common holiday gimmicks," the presentation of an item as discounted from a prior "suggested price"—a price that does not reflect a "normal sales price."[32]

As an example of "improper discounting," the editor of the websites cited an online deal offered by Macy's for a toaster oven.[33] Macy's priced the toaster oven at $252, presenting it as a discount off a special sale price of $280, a reduction compounded by an additional ten percent offer-code discount, ultimately reflecting an advertised regular price of $417.[34] Amazon and Best Buy advertised this very same toaster at a straight-up price of $250 for several months but without a reference price that would have reflected the "discounts" listed by Macy's.[35] If $417 truly reflected the Macy's bona-fide price offering at one time in the past, the advertised discount would be powerful but not fictitious.[36]

Why would a retailer signal a price discount off of such a questionable calculation? Among other reasons, perhaps to exploit consumer behavioral tendencies by presenting a pricing "anchor" to shoppers that signals that the item has high value and that the consumer is getting a bargain. Some consumers will take the discount as a signal to stop shopping, even though

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28. Farhad Manjoo, *Online Deals for Holiday Shopping: Buyer Beware*, N.Y. TIMES, Dec. 11, 2014, at B1; *see also* Lydia DePillis, *Holiday Sales Are a Dirty Lie*, WASH. POST (Nov. 26, 2013), https://www.washingtonpost.com/news/wonkblog/wp/2013/11/26/holiday-sales-are-a-dirty-lie (describing Black Friday "doorbuster" discount sales as an "elaborate con").

29. WIRECUTTER, http://wirecutter.com (last visited Nov. 24, 2015).

30. SWEETHOME, http://sweethome.com (last visited Nov. 24, 2015).

31. Manjoo, *supra* note 28. The editors of the sites dedicate twenty full-time writers to investigate retail deals during the holiday season. *Id.*

32. *Id.*

33. *Id.*

34. *Id.*

35. *Id.*

36. Macy's defended this advertised markdown practice with a series of non-sequiturs, noting that:

> advertised 'regular' prices are 'based on many different factors, including the cost of the item, overhead, benefits we offer . . . as well as our ability to offer the item at a lower price during sale events' and further, that Macy's had expressly disclaimed the representation that any sales had been made at $417.

Id.

in the case of Macy's they could have saved a few dollars had they continued. Consumers who bought from Macy's before finding the lowest price paid almost a one-percent premium over a purchase from a competitor. More significant, perhaps, Macy's would take a sale away from an honest competitor at a gross margin likely above thirty percent, a compelling motive to employ this advertising tactic.[37]

In Section A, this Article moves from the above Macy's anecdote toward a formal definition of fictitious pricing. For the purposes of this Article, the definition of fictitious prior-reference pricing offered by the FTC and flesh out its boundaries by exploring a hypothetical retail scenario. Having established the definition of fictitious pricing, in Section B, this Article explains the behavioral economics that make discount advertising powerful, with the notion that extra scrutiny of discount pricing is warranted because of the potential for manipulation of consumer biases.

A. FICTITIOUS PRICING DEFINED

This Article uses "fictitious pricing" and "deceptive pricing" interchangeably with "false prior-reference pricing." Broadly, "deceptive pricing," as defined by the FTC Guides, encompasses a related range of pricing tactics,[38] from fictitious former-price comparisons,[39] to false retail-price comparisons,[40] misleading use of a manufacturer's suggested price,[41] and bargains based on the purchase of other articles.[42]

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37. *Cf. Macy's Gross Profit Margin (Quarterly)*, YCHARTS, https://ycharts.com/companies/M/gross_profit_margin (last visited Nov. 24, 2015) (indicating that Macy's gross profit margin has been over 30% for the past five years).

38. 16 C.F.R. § 233 (2014).

39. *Id*. § 233.1(a) ("[W]here an artificial, inflated price was established [by the advertiser] for the purpose of enabling the subsequent offer of a large reduction—the 'bargain' being advertised is a false one . . . .").

40. *Id.* § 233.2(a) ("[A]dvertising . . . pric[ing as being] lower than those being charged by others for the same merchandise in the advertiser's trade area . . . may be done . . . but . . . the advertised higher price must . . . not be fictitious or misleading.").

41. *Id.* § 233.3(a) ("[If] suggested retail prices do not in fact correspond to prices at which a substantial number of sales of the article in question are made, the advertisement of a reduction [from the suggested retail price] may mislead the consumer.").

42. *Id.* § 233.4(a) ("Frequently, advertisers choose to offer bargains in the form of additional merchandise to be given a customer on the condition that he purchase a particular article at the price usually offered by the advertiser. . . . Representative of the language frequently employed in such offers are 'Free,' 'Buy One—Get One Free,' '2-For-1 Sale,' 'Half Price Sale,' '1¢ Sale,' '50% Off,' etc. . . . . It is important . . . that where such a form of offer is used, care be

The FTC guidance on fictitious pricing reflects a consideration of the useful functions of honest discount pricing. Discount-pricing advertising, if *truthful* in presenting the former price, benefits both buyers and sellers. Express presentation of the former price as a reference point provides consumers valuable information. The seller signals that a "bargain" opportunity, a departure from "regular" pricing, exists. Such a deal will likely draw more attention from consumers than items that hold to a "regular" price. Sellers can benefit by moving previously overpriced (or mispriced) inventory, and more buyers will enter the market to purchase at the lower price, especially when informed about the special nature of the low price. Competitors may, in turn, respond to discounts with more price cuts, which benefit consumers.

However, if the advertised former reference price is expressly or implicitly a false representation, meaning that the method for selling the good involved luring consumers by representing something untrue, then the advertised price is fictitious. The effects of fictitious pricing can be unduly distortive. The FTC, in the past, regulated prior-reference discounting behavior through enforcement[43] of Section 5 of the FTC Act, which declares unlawful "unfair or deceptive acts or practices."[44] The FTC provides sellers with more detailed "Guides" on a range of market behaviors, including deceptive pricing.[45] FTC Guides do not have the force of law, but they "provide the basis for voluntary and simultaneous abandonment of unlawful practices by members of industry. Failure to comply with the guides *may* result in corrective action by the Commission under applicable statutory provisions."[46] The FTC situated guidance on fictitious

taken not to mislead the consumer.").

43. *See* 15 U.S.C. § 45(b)–(c) (2012) (describing the FTC's enforcement authority).

44. *Id.* § 45(a). Though advertising practices can be regulated either through "unfairness" or "deception," the FTC has prosecuted most advertising cases through the "deception" standard. The deception standard differs from the unfairness standard, and both standards evolved separately. *See* JOHN A. SPANOGLE ET AL., CONSUMER LAW: CASES AND MATERIALS 67 (3d ed. 2007); *see also* DEE PRIDGEN & RICHARD M. ALDERMAN, CONSUMER PROTECTION AND THE LAW § 11:1 (2015).

45. *See, e.g.*, 16 C.F.R. § 233.1.

46. 16 C.F.R. § 1.5 (2014) (emphasis added). The FTC has long held that the Guides must be subject to consistent interpretation. Crown Publishers Inc., 66 F.T.C. 1488, 1496 (1964) ("[W]ords and phrases of the type set out in the '*Guides*' must be consistently dealt with by the Commission or its decisions will have no meaning or value. Only by consistent interpretation can some order be brought to the semantic jungle of advertising." (quoting Gimbel Bros. Inc., 61 F.T.C. 1051, 1073 (1962))). *Gimbel Bros.* "practically gives the Guides

pricing within the guidance on deceptive pricing.[47] Though fictitious pricing encompasses practices broader than former-price comparisons, such as competitor comparisons, this Article focuses on fictitious pricing in the former price-comparison context.

1. FTC Guide on Former Price Comparisons

The FTC Guide on Former Price Comparisons describes what constitutes deception[48] when a seller offers an article at a price that expressly references a prior price by that seller.[49] The Guide first defines a "true bargain":

> If the former price is the actual, bona fide price at which the article was offered to the public on a regular basis for a reasonably substantial period of time, it provides a legitimate basis for the advertising of a price comparison. Where the former price is genuine, the bargain being advertised is a true one.[50]

Then, the FTC informs sellers where discount-pricing tactics cross over into dishonest and deceptive territory:

> If . . . the former price being advertised is not bona fide but fictitious—for example, where an artificial, inflated price was established for the purpose of enabling the subsequent offer of a large reduction—the "bargain" being advertised is a false one; the purchaser is not receiving the unusual value he expects. In such a case, the "reduced" price is, in reality, probably just the seller's regular price.[51]

Examples of deceptive prior-reference price discounting offered by the Guide include a scenario where a seller tests a higher price point for an article for "only a few days," and then, after the test fails, lowers the price back to the regular price, labeling it as a discount. This discount is "not genuine."[52] The Guide further points to practices where the seller "might use a price at which he never offered the article at all," or one "not used in the regular course of business . . . [nor] used in the recent past but at some remote period in the past, without making disclosure of that fact."[53] A "non-genuine" bargain "might

the force of a legal presumption." Ira M. Millstein, *The Federal Trade Commission and False Advertising*, 64 COLUM. L. REV. 439, 472 n.165 (1964); *see also* Matthew A. Edwards, *The Law, Marketing and Behavioral Economics of Consumer Rebates*, 12 STAN. J.L. BUS. & FIN. 362, 397 (2007) (describing the FTC's approach to enforcing Section 5 and guiding commercial actors).

47. 16 C.F.R. § 233.

48. More precisely, what the FTC warned sellers could constitute deception, potentially triggering an action.

49. 16 C.F.R. § 233.1.

50. *Id.* § 233.1(a).

51. *Id.*

52. *Id.* § 233.1(c).

53. *Id*. § 233.1(d).

use a price that was not openly offered to the public" or one that was offered but was immediately reduced after an unreasonable period of time.[54] Note that the current Guide does not require proof of actual sales of the article at the reference price in order to establish the reference price, but the original 1958 Guide did.[55] The current Guide lowered the bar for seller behavior; sellers merely have to prove that the article was *offered* at the prior price in good faith.

The Guide also advises sellers to take caution whenever accompanying price terms with words like "Regularly," "Usually," and "Formerly."[56] Even the plain use of the word "Sale," according to the Guide, should cause the advertiser to "take care that the amount of reduction is not so insignificant as to be meaningless. It should be sufficiently large that the consumer, if he knew what it was, would believe that a genuine bargain or saving was being offered."[57]

The Guide effectively provided retailers a rulebook—a quasi-safe harbor—useful in the era when the FTC pursued enforcement. Pricing tactics that have emerged as the modern retail norm regularly cross the Guide's boundaries of lawful behavior. Applying the Guide's standards to a real example from the market illustrates this point.

2. Illustrative Application of Guide

For context about the complexity of regulating pricing strategies, consider this actual example of how a major retailer marked and priced sweaters:

> A supplier sells the sweater to a retailer for roughly $14.50. The suggested retail price is $50, which gives the retailer a roughly 70% markup. A few sweaters sell at that price, but more sell at the first markdown of $44.99, and the bulk sell at the final discount price of $21.99 [advertised over fifty-percent off]. That produces an average unit retail price of $28 and gives the store about a 45% gross margin on the product.[59]

How would the Guide apply to this factual scenario? If the original price of $49.99 constituted the "actual, bona fide price . . . offered to the public on a regular basis for a reasona-

54. *Id.*

55. *See infra* Part I.C.

56. 16 C.F.R. § 233.1(e).

57. *Id.* The Guides clarify: "An advertiser who claims that an item has been 'Reduced to $9.99,' when the former price was $10, is misleading the consumer, who will understand the claim to mean that a much greater, and not merely nominal, reduction was being offered." *Id.*

59. *See* Kapner, *supra* note 7 (discussing an example provided by a retail industry consultant).

bly substantial period of time," the advertised former price would be "genuine," the comparison basis "legitimate," and the bargain, "true."[60] By the Guide's criteria, the duration of the $50 offer is material. The Guide advises that the duration of "only a few days" would not suffice, but a longer time lays foundation for offering the price on a "regular basis" or a "substantial period of time."[61]

Complicating the matter, however, the Guide indicates that discounting tactics cross the line when "the purchaser [does] not receiv[e] the unusual value he expects."[62] Given the prevalence of discounting practices, a purchaser may have, especially after decades without federal enforcement, a low threshold for the "value he expects." In an environment of omnipresent discounting, consumers may have skewed perceptions of value. Though it is hard to imagine that an enforcement-focused FTC would allow the deceptive behavior to negate the rule by defining the norm downward, it is possible that policymakers are not frothing to intervene because consumers have no expectation of honest pricing.[63] The problem may be that when consumers get a perceived bargain, they do not look back at the pricing history of an item to see if they were misled. Such a deception might be difficult to detect—and personal post-purchase research would be costly.

The above sweater marketing practice likely constitutes lawful price discrimination. Urgent buyers who wish to pay the higher price will do so sooner, while the less urgent will value the offering at a lower point. They will transact later at a lower price, perhaps as the "sweater season" passes. Advertising the price in conjunction with a prior-reference price point might seize the attention of bargain hunters, with whom the seller would never transact, had the offer been at $28 the entire time, (or perhaps even at $21.99).[64] Most important, for the purpose of deceptive pricing, the initial sweater price would constitute a

60. *See* 16 C.F.R. § 233.1(a).

61. *Id.* § 233.1(a), (c).

62. *Id.* § 233.1(a).

63. This absence of expectation, combined with the difficulty for consumers to obtain information to identify fictitious pricing, may in part explain the low amount of complaints received by the FTC about retail outlet shopping. In fact, the FTC's response to Senator Blumenthal "for not launching an investigation" into retail outlet fictitious pricing was that "they [had not] received enough consumer complaints about [the] issue." Hladky, *supra* note 2. The Senator labeled this response "ridiculous" and "ludicrous" because the FTC has no set number of complaints required for initiating an investigation. *Id.*

64. *See* Armstrong & Chen, *supra* note 12, at 25.

bona fide offer. Expectations of value would not be unduly manipulated and consumer search would retain integrity.

By using the reference point to establish a value baseline, the retailer may be manipulating the consumer into a purchase, further exploiting the built-in behavioral biases that this Article discusses in Part I.B. This manipulation might cause consumers to overestimate product value, purchase something that they might not have otherwise purchased, spend more on an item than they might have, or even prematurely stop their shopping before they found their best bargain.[65]

Is the consumer truly harmed by offers referencing fictitious former prices, considering that the retailer ultimately offers the items at a definitive numeric price at the point of sale and in the end, the consumer accepts the price? As this Article discusses throughout, factors countervail, but in the end, overwhelming evidence exists that fictitious pricing reduces welfare. A starting point for assessment of fictitious-pricing enforcement begins with locating what makes the practice powerful for advertisers, informed by basic behavioral economics.

B. BEHAVIORAL INFLUENCE ON CONSUMERS

"I don't even get excited unless it's 40% off."

- Lourdes Torres, browsing the sales rack at Macy's.[66]

1. Anchoring Effects

"Anchoring" describes the human tendency to cast disproportionate weight on the first piece of information that they receive when making subsequent decisions.[67] In this context, the prior-reference price could be the first piece of information that sets the course for subsequent transactional decisions. This phenomenon might explain the import of "40%" to the aforementioned Ms. Torres.

Daniel Kahneman and Amos Tversky famously demonstrated that decision makers "evaluate outcomes" based on "initial reference point[s]."[68] The anchoring of the sale price to a

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65. *See* Kwikset Corp. v. Superior Court, 246 P.3d 877, 887–88 (Cal. 2011).

66. Kapner, *supra* note 7.

67. Program on Negotiation, *Anchoring Effect*, HARV. L. SCH., http://www.pon.harvard.edu/tag/anchoring-effect (last visited Nov. 24, 2015).

68. Christine Jolls et al., *A Behavioral Approach to Law and Economics*, 50 STAN. L. REV. 1471, 1535 (1998); Daniel Kahneman & Amos Tversky, *Prospect Theory: An Analysis of Decision Under Risk*, 47 ECONOMETRICA 263, 263

"former price" makes the sale price more attractive than the price would have been had it stood alone. Behavioral economist Richard Thaler elaborated that if a "suggested reference price" is offered, "a lower selling price will provide positive transaction utility."[69] A higher *fictitious* "former price" disingenuously causes the consumer to attach a higher level of value to an item than it would have had the pricing been honest.[70]

One meta-analysis of the power of anchoring in *deceptive* prior-reference pricing concluded:

> [A]n abundance of evidence . . . show[s] that advertised reference prices (ARPs) influence a range of consumer price-related responses, including increasing perceptions of the fair price, the normal price, the lowest available price in the market, the potential savings and the purchase value . . . . The effects of reference pricing on consumer deal evaluations and behaviour have been replicated fairly consistently . . . .[71]

Retailers can use discounting—genuine or fictitious—powerfully to their advantage if they execute with precision. As this Article discusses next, a high prior-reference price can manipulate transactions by signaling that an offer brings higher value but at a lower price.

2. Price Effect on Perceived Quality

Consumers may also use a former reference price as a signal of quality, especially in markets where quality may prove difficult to discern.[72] If the price signal is genuine—i.e., the good was once offered in a bona fide manner at a higher price, the advertised discount communicates the availability of a true bargain. Perhaps the benefit of waiting for seasonal clothing or sporting goods to fade out of season, or the impending introduc-

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(1979) (critiquing expected utility theory as descriptive model of decision-making and promoting prospect theory instead).

69. Richard H. Thaler, *Mental Accounting and Consumer Choice*, 27 MARKETING SCI. 15, 24 (2008).

70. *See* Grewal & Compeau, *Comparative Price Advertising*, *supra* note 12, at 55.

71. Ahmetoglu et al., *supra* note 12; *see also* Donald R. Lichtenstein, *Price Perceptions, Merchant Incentives, and Consumer Welfare*, 14 J. PROD. & BRAND MGMT. 357, 358 (2005) ("ARPs work, a lot of research shows they do, and retailer practice and returns shows that they do. This is nothing new—it is widely known. If I advertise a sale price of, say, $29.95 and accompany it with an ARP of, say $39.95, in most contexts, sales will increase relative to a no ARP present situation. Sales will likely increase as I increase my ARP to $49.95, to 59.95, to 69.95.").

72. *See generally* Kyle Bagwell & Michael H. Riordan, *High and Declining Prices Signal Product Quality*, 81 AM. ECON. REV. 224 (1991) (discussing signaling distortion's relation to pricing).

tion of a new model of an electronics item can be realized through a discount. If the signal proves false, however, the consumer transacts on a false association of quality. If the advertiser never offered a sweater for a bona fide price of $100, the consumer may be left with the impression that the sweater was once tagged with $100 quality, and a moderate discount may trigger the false notion that the seller is offering extra value.[73] In that scenario, a consumer purchase would be a mismatch of payment and expected value, but it might be difficult for the consumer to feel a loss without knowing that more shopping could have yielded a better deal.

One well-known analysis describes how consumers link price and quality in the context of the rollout of a new product:

> Consider a market in which a firm introduces a new product possessing some innovative feature of uncertain quality. Some consumers can ascertain the quality, while others cannot, but all understand that a higher-quality product is more costly to produce. The most efficient way for the firm to signal high quality is to charge a price too high to be profitable if the product were in fact of lower quality . . . . [U]ninformed consumers rationally infer higher quality from the higher price.[74]

This stylized analysis benefits from a few extensions. The scenario fits best with new products but also fits with established product lines where consumers have difficulty discerning quality and associated price values. Some offerings must be evaluated post-purchase in order for consumers to judge quality.

In addition to exploiting the anchoring effect and perceived quality, fictitious pricing also enables retailers to exploit consumer tendencies and biases in the valuation of bundles of gains and losses. This Article further elaborates on that point in its discussion of prospect theory.

3. Prospect Theory

The presentation of a discount price can lead consumers to believe that they are receiving extra value because of the way people cognitively assess gains and losses—especially when gains are segregated and losses are bundled. At the core of prospect theory, Daniel Kahneman and Amos Tversky demonstrate that for individuals, losses loom larger than gains of

73. *See* ROBERT B. CIALDINI, INFLUENCE: SCIENCE AND PRACTICE 12 (4th ed. 2001) (discussing the "Drubek" anecdote, which describes a mistake but invokes similar consumer psychology).

74. *Id.* at 224–25.

equivalent magnitude.[75] When losses are presented as a bundle, however, the perceived total loss diminishes. Conversely, when gains are segregated, the perception emerges on net that total value is higher.[76] The classic illustration of this phenomenon comes from an example provided by Richard Thaler, involving a lottery experiment. Subjects who win a lottery twice, (once for $50, once for $25) tend to enjoy more satisfaction than those who win the lottery once for $75.[77]

How does discounting tap into prospect theory? A discount offers the buyer segregated gains and a consolidated loss, enhancing the perceived value of the transaction. Consider three scenarios for a necktie offering at an outlet store:

Tie offered without discount advertising for $100.

Tie offered for twenty-percent off with a price tag of $125. ($100 at register).

Tie offered for twenty-percent off with a price tag of $125 ($100 at register), but ties were never sold at a bona fide price of $125.

The first scenario offers the consumer one consolidated gain (the tie) and one consolidated loss ($100 payment). The second and third scenarios keep the loss consolidated but segregate the gains. The consumer receives the tie (one gain), the $25 "savings" (a second gain), and experiences one consolidated loss ($100). Effectively, the consumer receives the same value but enjoys an experience similar to winning the lottery twice.[78] If the third, "fictitious" presentation causes the transaction to take place because it apparently maximizes utility, *should* its fictitious nature matter to the consumer? Should regulators let the consumer proceed in ignorance, enjoying the utility from the two gains, or should they intervene?

These questions cut to one of the essences of the problem with regulating fictitious pricing. Is there harm to the individual consumer? Framing the harm proves difficult. After all, the consumer saw the tie, saw the final price offered at the cash register, and transacted. Perhaps, post hoc, the consumer would object to the transaction or claim that he would have withheld expenditure. Nonetheless, the consumer might have behaved differently but for the fictitious discount, perhaps con-

75. *See* Kahneman & Tversky, *supra* note 68, at 268.

76. *See* Thaler, *supra* note 69, at 18–24.

77. Richard H. Thaler, *Mental Accounting Matters*, 12 J. BEHAV. DECISION MAKING 183, 187 (1999).

78. *See id.* Mental accounting proves nuanced. A payment is not necessarily a "loss," for example. *See id.* at 188.

tinuing to shop, perhaps transacting at a lower "loss" or price. As this Article discusses in Part II, pleading individual pecuniary harm has proven frustrating for private plaintiffs.[79] The difficulty of demonstrating individual harm may lead to the conclusion that addressing the welfare problem may be left solely in the hands of regulators.

II. THE CHALLENGE OF DEMONSTRATING INDIVIDUAL CONSUMER HARM

Prior to 1969, in the heyday of FTC enforcement of fictitious pricing, the FTC almost exclusively focused on harm to the "marketplace" rather than harm to individual consumers. An emphasis on a broader injury to "competition" or "competition in commerce" may have reflected several dynamics. First, the FTC's statutory mandate emphasized regulation of commercial behavior over—but not to the exclusion of—redressing individual injury. Second, the "unfair methods" and the "unfair or deceptive acts or practices" may have been easier to prove than injury. The simplest regulatory approach may have been to enjoin the fictitious-pricing practices.

In Section A, through an exploration of FTC actions before 1969, this Article shows the regulatory approach toward addressing "marketplace harm" rather than individual harm—an approach that warrants revisiting today. Interpretation of state law offers another avenue for exploring the concept of individual harm. In Section B, this Article shows that Illinois law requires proof of consumer and competitive injury in order for a private fictitious pricing claim to proceed. This barrier for private litigation in Illinois led Judge Frank Easterbrook to declare that such actions belonged in the province of an attorney general. In Section C, this Article shows the recent evolution of California law through *Kwikset v. Superior Court* and *Hinojos v. Kohl's.* California leans toward penalizing this tactic and enjoining advertisers from employing it.

A. HISTORIC APPROACH: MARKETPLACE INJURY

The FTC took action against fictitious pricing shortly after the agency's creation.[80] In the 1920s, a decade noted for expan-

79. As Part III discusses, public regulators can have trouble matching an appropriate remedy, too.

80. For a history of deceptive-pricing regulation from 1920 until 1962, as well as a contemporary account of the state of regulation and the retail market in 1962, see Harkrader, *supra* note 13.

sion of mass production and the mass consumer market,[81] retailers had already embarked on reference-price promotional campaigns.[82] The very first *FTC Reporter* reports cases where the FTC deemed promotion of fictitious "sales" of vacuum cleaners as an "unfair method of competition."[83] Two 1920 FTC cases involving retail sales of pianos typify the nature of actions taken in that era.[84] In *Holland Piano Manufacturing Co.*,[85] the FTC found that Holland Piano stenciled "high fictitious prices on pianos . . . and allow[ed] radical reductions therefrom," leaving purchasers with the impression that the pianos were offered at reduced prices at retail.[86] These "reduced prices" suspiciously aligned with the "full resale prices received for pianos of equal quality and grade" elsewhere.[87] This scheme constituted an "unfair method[] of competition."[88] The FTC unsuccessfully pursued similar claims that same year in *FTC v. P.A. Starck Piano Co.*, along with claims of false advertising with respect to "special sales" and "economical shipping methods."[89] Note that both actions invoked *unfair competition*, per the original FTC Act language, indicating that the FTC deemed such practices impermissible in the marketplace. The FTC did not consider the issue of individual consumer harm in these matters.

In the post-war era, the FTC pursued cases against both manufacturers and retailers. For example, in *Orloff Co.*,[90] the manufacturer, Orloff, shipped watches to retailers with price tags affixed. The manufacturer tags displayed high prices, but Orloff understood that the watches would be sold by retailers at

81. *See generally* Joseph A. Schumpeter, *The American Economy in the Interwar Period, the Decade of the Twenties*, 36 AM. ECON. REV. 1 (1946) (discussing the utility of history for testing economic analysis).

82. *See* Harkrader, *supra* note 13, at 3.

83. Muenzen Specialty Co., 1 F.T.C. 30 (1920). Just before *Muenzen Specialty*, a candy manufacturer was found to engage in unfair competition by falsely stating that it had priced its candy "below cost." E.J. Brach & Sons, 1 F.T.C. 186 (1918).

84. The Federal Trade Commission Act established the FTC in 1914, replacing the Federal Bureau of Corporations, which had been established in 1903. *See* NAT'L ARCHIVES, GUIDE TO FED. RECORDS, RECORDS OF THE FEDERAL TRADE COMMISSION 122.1 (1976), http://www.archives.gov/research/guide-fed-records/groups/122.html.

85. 3 F.T.C. 31 (1920).

86. FTC, ANNUAL REPORT OF THE FEDERAL TRADE COMMISSION 148 (1920).

87. *Id.*

88. *Id.*

89. *Id.*

90. 52 F.T.C. 709 (1956).

substantially lower prices.[91] The FTC found that Orloff "knowingly[92] placed into the hands of retailers a means and instrumentality whereby members of the purchasing public may be misled and deceived as to the usual and regular selling prices of [Orloff's] watches . . . ."[93]

Orloff typified this era of fictitious-pricing enforcement, linking consumer deception in fictitious pricing to substantial injury to *competitors* and "*competition in commerce*."[94] Upon promulgation of the Guides Against Deceptive Pricing in 1958, nearly thirty percent of all FTC cease-and-desist orders were attributable to "fictitious pricing."[95] Fictitious-pricing actions emerged as the "leading type of deception practiced in violation of the FTC Act."[96] The 1958 version of the Guides required *actual sales* of an item at the reference price, signaling a low tolerance for the practice.[97] The FTC pursued actions more aggressively in this period than at any other time.

The fictitious-pricing scheme confronted by the FTC in 1964 in *Crown Publishers* provides another typical scenario.[98] Crown had been selling copies of a book to retailers with a price mark of $6.00, while recommending to sellers that they in turn mark down the book to $2.98.[99] Crown knew that no retailer ever sold copies of that book for $6.00.[100] The FTC found that the publisher had "the tendency and capacity to mislead and deceive [consumers] into believing that by purchasing the book . . . at $2.98 or at any price less than $6.00, they [would be] saving the difference between the lower price and $6.00."[101] The FTC found Crown's actions to be "all to the prejudice and injury of the public and of respondents' competitors and constitute unfair and deceptive acts and practices and unfair meth-

91. *Id.* at 711.

92. *Id*. at 715 ("It is absurd to suppose that [Orloff] would . . . engage in the empty and financially wasteful practice of supplying retail price tags to their customers if such tags were not being used by [retailers] to advantage in the sale of [the] watches . . . . [Orloff] cannot therefore deny their authorship of, or escape responsibility for, a device which to their knowledge is being widely used for deceptive purposes.").

93. *Id.* at 717.

94. *Id*. at 716.

95. Harkrader, *supra* note 13, at 4 n.10.

96. *Id.* at 3–4.

97. *See* Guides Against Deceptive Pricing, 23 Fed. Reg. 7965, 7966 (Oct. 15, 1958).

98. Crown Publishers, Inc., 66 F.T.C. 1488 (1964).

99. *Id.* at 1489.

100. *Id.* at 1499.

101. *Id.* at 1517.

ods of competition . . . ."[102] Here, the FTC recognized the concept of potential injury to consumers but focused on "competitive injury."

These actions show how the FTC played the role of marketplace referee before 1969. The FTC aimed primarily to preserve integrity and fairness among competitors with only a secondary concern for consumer welfare. These enforcement efforts foreshadowed the tenor of the 1983 Policy Statement on Deception, which permits a finding of materiality without requiring evidence of tangible consumer harm. In *Crown Publishers*, the FTC indicated that consumer testimony about deception, though worthy of incorporating in the record, was not required for determining whether a practice constitutes deception.[103] The FTC had room to find deception, even without proof of injury to consumers or competitors, though some finding of both might support a case.

In *Exposition Press, Inc. v. FTC*,[104] the Second Circuit did not even require the FTC to prove that *competitors* demonstrated an injury.[105] The "inference that [a marketer] by its misleading initial approach attracted business which it would not otherwise have obtained" was permissible.[106] Again, in this era, the FTC and the courts focused more on the nature of the activities, assuming a general harm to the marketplace. "The law is violated if the first contact . . . is secured by deception . . . even though the true facts are made known to the buyer before he enters into the contract of purchase."[107] Under this approach,

102. *Id.* at 1516.

103. *Id.* at 1497 ("Actual consumer testimony is in fact not needed to support an inference of deception by the Commission.").

104. 295 F.2d 869 (2d Cir. 1961).

105. *Exposition Press* is a general deception case that addresses FTC standards for proof of injury, which implicate deceptive discounting cases. *Id.* In this case, the FTC "did not explicitly marshal evidence of the existence of other [sellers] competing with [the target], the fact that there are such publishers emerges amply from a reading of the record as a whole." *Id.* at 873.

106. *Id*. Actual proof that one actor injured another specific actor in a crowded marketplace would resemble a burden of proof similar to private claims brought under the Section 4 of the Clayton Act. 15 U.S.C. § 15 (2014); *see, e.g.*, Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 583 (1986) (determining that price-•xing did not inflict injury and that claimant actually stood to gain from the higher market prices); Cargill, Inc. v. Monfort of Colo., Inc., 479 U.S. 104, 118–19 (1986) (rejecting a lost-pro•ts claim based on lower market prices resulting from a merger which may have caused injury because the resulting lower prices were not anti-competitive).

107. *Exposition Press*, 295 F.2d at 873 (quoting Carter Prods., Inc. v. FTC, 186 F.2d 821, 824 (7th Cir. 1951)); *see also* Book-of-the-Month Club, Inc. v. FTC, 202 F.2d 486 (2d Cir. 1953); Progress Tailoring Co. v. FTC, 153 F.2d 103

even if the buyer discovers that an item was fictitiously priced before buying it, the absence of pure "benefit-of-the-bargain" damages did not absolve the seller. Proof of injury to the *public interest* took primacy in enforcement. Even if consumer harm had not been proven, harm to the public could be found and remedied by the FTC.

However, after the FTC ceased enforcement, most private litigants, often using a class action mechanism, did have to show pecuniary injury. The abandonment of fictitious pricing emerged from a host of sweeping changes at the FTC in 1969. A "wild and wooly group of students known as 'Nader's Raiders'" berated the FTC for focusing on trivial abuses at the expense of more serious fraud.[108] The Raiders criticized the Commission for "lethargy among the legal staff, political favoritism, inept management, and a poorly functioning monitoring system."[109] Though the Raiders' critique was not the first sharp critique of the FTC, nor was the critique itself novel, unlike previous studies, "[i]t sparked a series of political actions that eventually revitalized the agency."[110]

The Nader Report spurred President Nixon to ask the American Bar Association (ABA) to study reform of the FTC and make recommendations.[111] In the 1969 ABA Report, Richard Posner concluded that deceptive-pricing enforcement wasted resources.[112] The other committee members did not disagree. Posner concluded that the more than five million dollars that the FTC "expended in the area of fraudulent and unfair marketing practices" in the 1963 fiscal year "bought precious little consumer protection."[113]

After President Nixon received the 1969 ABA Report, he charged the FTC "'to initiate a new era of vigorous action' to protect the consumer."[114] "Sound economic analysis" would prove central to setting priorities for the Bureau of Consumer

(7th Cir. 1946).

108. PRIDGEN & ALDERMAN, *supra* note 44, § 8:2.

109. *Id.*

110. Cox, *supra* note 26 (quoting HARRIS & MILKIS, *supra* note 26). Cox, the author of the article, was a "Raider." *Id.* at 899.

111. *See* 1969 ABA REPORT, *supra* note 26; Letter from President Richard Nixon to William T. Gossett, *supra* note 26. *See generally* MARTIN, *supra* note 26 ("[The ABA's conclusions were] remarkably similar to the conclusions of Nader's Raiders . . . .").

112. *See* 1969 ABA REPORT, *supra* note 26, at 61–82.

113. *Id.* at 77.

114. Cox, *supra* note 26, at 906 (quoting HARRIS & MILKIS, *supra* note 26, at 166).

Protection, a newly established FTC division.[115] FTC fictitious-pricing enforcement ceased contemporaneously with this reorganization.

The states continued to see activity, including from private actors enforcing state consumer statutes. In Sections B and C, this Article discusses the approaches of Illinois and California, respectively, in addressing private fictitious-pricing claims. Illinois law appears to close the door to private consumer litigants. California leaves the door open but offers scant guidance on remedies.

B. PRIVATE LITIGATION AND INDIVIDUAL HARM

Recent private fictitious-pricing cases litigated under Illinois and California law show the challenge of demonstrating economic harm.[116] Applying Illinois law, a federal district court declined to find a remedy for a private plaintiff claiming harm from fictitious-pricing deception.[117] Nonetheless, a transaction borne in deception might inflict *some* consumer harm in *some* cases. In one private consumer action under California law, the Ninth Circuit focused on problems inherent in the underlying deception, building a case for discerning actual economic harm without offering a satisfactory theory for framing pecuniary damages.

Private actors attempting to sue retailers under deceptive-pricing statutes can have difficulty pleading a theory of damages. Where statutory damages are unavailable, implicitly, economic or "actual" damages must be proven by private parties, or at least alleged, in the class action context.[118]

This degree of difficulty may explain why there are few reported cases where private consumer fictitious-pricing actions have been brought. Nonetheless, the facts of these modern cases illustrate the nature of the harm, and this Article explores them here.

1. Illinois Approach

Courts have recently confronted private fictitious-pricing

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115. *Id.*

116. This Article defers discussion of public state enforcement approaches until Part III.

117. See *infra* Part II.B.1 for a discussion of the Illinois statute and case law.

118. *See* Kim v. Carter's Inc., 598 F.3d 362, 365 (7th Cir. 2010) ("A private party, however, must show 'actual damage' in order to maintain an action under the ICFA."); *see also* 815 ILL. COMP. STAT. 505/10a (2007).

actions brought under the Illinois Consumer Fraud and Deceptive Business Practices Act (ICFA).[119] In *Camasta v. Jos. A Bank Clothiers, Inc.*,[120] the plaintiff consumer claimed that the clothing retailer Jos. A. Bank Clothiers (JABC) advertised "sales prices" which induced him to buy six shirts at one of the retailer's stores.[121] The consumer alleged that he later discovered that the price he paid was not the product of a "temporary price reduction," but rather the result of "a sales practice of advertising the normal retail price as a temporary price reduction at all of its 31 retail locations in Illinois."[122]

The *Camasta* plaintiff claimed that had he known that the advertised "sale" price was actually the regular price, he "would not have been induced to purchase [the shirts], could have purchased [the shirts] for less than the amount paid, or could have gone to another retail store for a true 'sale' price of a comparable item, or shopped around and obtained a better price in the marketplace."[123] This plaintiff struggled to demonstrate a pecuniary injury. If the plaintiff knew the price at the point-of-sale, had the opportunity to walk away, and still engaged in the exchange, was there harm? The *Camasta* court found none, drawing upon prior appellate interpretations of ICFA.[124]

In *Kim v. Carter's Inc.*[125] and *Mulligan v. QVC, Inc.*,[126] the Seventh Circuit and Illinois Court of Appeals, respectively, found similar complaints bereft of claims for contractual damages (i.e., deprivation of the "benefit of the bargain").[127] For example, in *Kim*, the plaintiff claimed that Carter's sold t-shirts at a thirty-percent discount off a fictitious "suggested price."[128] The Seventh Circuit again held that there was no pecuniary harm to the consumer if an item was sold at a discount from a fictitious price, because the actual price offered and accepted at the ultimate point of sale served as the contractual price.[129] Therefore, no tangible, identifiable economic damages had been inflicted. In *Mulligan*, for similar reasons, the Illinois appellate court found that even if seller QVC (a television marketing

119. *Id.* 505/1–/12.
120. No. 12-C-7782 (N.D. Ill. July 25, 2013).
121. *Id.* at 2.
122. *Id.*
123. *Id.*
124. *Id.* at 5.
125. 598 F.3d 362 (7th Cir. 2010).
126. 888 N.E.2d 1190 (Ill. App. Ct. 2008).
127. *Kim*, 598 F.3d at 365; *Mulligan*, 888 N.E.2d at 1196–97.
128. *Kim*, 598 F.3d at 363.
129. *Id.* at 365–66.

channel) compared fictitious "actual retail prices" against QVC prices, ICFA would not offer the plaintiff economic damages.[130] Without economic damages, the private mechanism does not enable consumers to police the market in the courts.

Competitors can also make claims against other competitors for injuriously deceptive discount pricing. Sellers rarely appear to pursue actions against rivals engaging in fictitious pricing, probably because causation and damages are difficult to prove. First, proving that competitive damage emanated from one particular seller in a crowded marketplace presents a challenge. Second, proving that price confusion was the proximate cause that led customers to switch a purchase to the cheating competitor, also presents difficulty. These injuries are not difficult to conceptualize—but they are quite difficult to prove. The Restatement of Unfair Competition also notes the difficulty of "establish[ing] a clear nexus" between fictitious pricing and harm to a particular seller.[131]

The only recent reported seller-against-seller dispute offers an example of the difficulty of proving a "horizontal claim." In *B. Sanfield, Inc. v. Finlay Fine Jewelry Corp.*,[132] a jewelry retailer brought an unsuccessful fictitious-pricing claim against a competitor, based on the Illinois statute[133] and the Lanham Act.[134] In *B. Sanfield*, a local, stand-alone jewelry store in Rockford, Illinois sued a retailer, Finlay Fine Jewelry, which operated within department stores at over 800 locations.[135] Finlay regularly sold its affordable wares at a declared fifty-percent discount.[136] This discount was "phony,"[137] as the discounts were

130. *Mulligan*, 888 N.E.2d at 1196–98.

131. RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 1 cmt. d (AM. LAW INST. 1995).

132. 999 F. Supp. 1102 (N.D. Ill. 1999), *vacated*, 168 F.3d 967 (7th Cir. 1999), *remanded to* 76 F. Supp. 2d 868 (N.D. Ill. 1999), *aff'd*, 258 F.3d 578 (7th Cir. 2001).

133. ILL. ADMIN. CODE tit. 14, § 470.220 (1989).

134. 15 U.S.C. § 1125(a)(1) (2012) ("Any person who . . . uses in commerce any word, term, name, symbol, or device, or any combination thereof, or any . . . false or misleading description of fact, or false or misleading representation of fact, which . . . (B) in commercial advertising or promotion, misrepresents the nature . . . of his or her or another person's goods, services, or commercial activities, shall be liable in a civil action by any person who believes that he or she is or is likely to be damaged by such act."). The Seventh Circuit ultimately consulted the FTC's Guides Against Deceptive Pricing, 16 C.F.R. § 233.1, for application of the Lanham Act. *See B. Sanfield, Inc.*, 258 F.3d 578, 579–80 (7th Cir. 2001).

135. *B. Sanfield, Inc*., 999 F. Supp. 1102, 1103–04 (N.D. Ill. 1999).

136. *B. Sanfield, Inc.*, 258 F.3d at 579.

137. *Id.*

rarely suspended, and few items were ever sold at the "one-hundred percent" full reference price. Occasionally, "but never on a Saturday or during December[,] Finlay remove[d] . . . 'sale' signs and [offered] items at higher prices, but less than 3 percent of its sales [were] made that way-and if a customer ask[ed] for the 50 percent discount during regular-price days, Finlay . . . happ[ily] obliged."[138]

The district court held that such practices "were not false or even misleading because customers see through the ruse."[139] The Seventh Circuit, however, rejected this conclusion, noting that the lower court had conflated injury with falsity.[140] A practice need not injure in order to meet the falsity threshold, according to the appellate court, but injury would still need to be demonstrated for relief.[141] The Seventh Circuit vacated the original district court ruling for failing to make such a determination,[142] and the district court subsequently found no injury.[143] On appeal once again, the district court's finding of no injury was affirmed by the Seventh Circuit, defendant Finlay ultimately prevailing.[144]

Sanfield ultimately lost before the Seventh Circuit because of the challenge of proving injury in a horizontal claim.[145] Sanfield first claimed that it had to pay for corrective advertising to inform consumers that they should focus on absolute prices, not "phantom" prices, but it simply failed to establish this fact before the district court.[146] Sanfield also contended that customers demanded fifty-percent markdowns to match Finlay, and when Sanfield refused such demands, customers left the store.[147] The court found insufficient evidence to support a causal link between lost business and Finlay's fictitious offers:

> Many people who walk through Sanfield's door would fish for discounts even if Finlay were to change its business methods . . . . [T]he district judge sought . . . some evidence that Sanfield's sales were influenced by Finlay's practices. For example, did Sanfield's sales rise on weekdays, when Finlay was most likely to take down its "sale"

138. *Id.*
139. *Id.*
140. *Id.*
141. *Id.*
142. B. Sanfield, Inc. v. Finlay Fine Jewelry Corp., 168 F.3d 967, 967 (7th Cir. 1999).
143. B. Sanfield, Inc. v. Finlay Fine Jewelry Corp., 76 F. Supp. 2d 868, 874–75 (N.D. Ill. 1999).
144. *B. Sanfield, Inc.*, 258 F.3d at 582.
145. *Id.* at 580–82.
146. *Id.* at 580–81.
147. *Id.* at 581.

> signs? The district judge observed that Sanfield's sales rose during the months covered by its claims and that attributing any particular lost business to Finlay is difficult: "Finlay and Sanfield did not compete exclusively with each other; rather, there were numerous other competitors for sales of the gold jewelry at issue." If these other rivals sold for less than Finlay, then they would be the likely source of diverted business . . . .[148]

Private relief was not available, but the court indicated in dicta that regulators would have had a much easier time proving a fictitious-pricing claim; they would not have had to demonstrate injury to a seller or consumer. As Judge Easterbrook noted in his collective interpretation and review of the Lanham Act, the FTC Guides, and Illinois law, "if the FTC or the Attorney General of Illinois were to bring an action . . . the court would issue an injunction in a trice. But . . . the plaintiff . . . is not a public prosecutor. It is a jewelry store, one of [the defendant's] rivals . . . and to prevail it must show injury."[149] His opinion concluded with a repetition of this point: "[The plaintiff] fancies itself a private attorney general, but it has not been appointed to that office, and as a private litigant must show injury, which it did not."[150]

Judge Easterbrook begs the question—if Sanfield cannot be a private attorney general, where is the public attorney general? Where is the FTC? The FTC would have an easier path to put a stop to confusing fictitious-pricing behavior (in a "trice"), had the matter been before it. As this Article discusses in Part IV, the FTC justified discontinuing fictitious-pricing enforcement under the logic that larger, incumbent department stores would urge the FTC to harass discounters. In this case, ironically, a local single-store retailer brought a complaint against an 800-location seller operating out of department stores.[151] In this "Bambi-Meets-Godzilla"-like[152] *Sanfield* conflict, Bambi cannot prove injury under Illinois law, despite Godzilla's attack. Only the regulators, according to Judge Easterbrook, can insulate Bambi from deceptive tactics. These activities could be much more easily ended by the FTC, which has the power to focus on marketplace behavior, rather than prove actual injury.

The complexity and difficulty of these Illinois private ac-

148. *Id*. (internal citations omitted).

149. *Id.* at 580.

150. *Id.* at 582.

151. B. Sanfield, Inc. v. Finlay Fine Jewelry Corp., 999 F. Supp. 1102, 1104 (N.D. Ill. 1998).

152. *See* Marv Newland, *Bambi Meets Godzilla*, YOUTUBE (Apr. 8, 2006), https://www.youtube.com/watch?v=BXCUBVS4kfQ.

tions, consumer and seller, demonstrate that private actions will not police fictitious pricing. Regulators are best situated to do so, and the FTC can set that tone at the federal level[153] by moving away from zero enforcement. California offers a more open avenue for private claims, but direct consumer remedies may still prove elusive.

2. California Approach

California consumer law can have an outsized impact on national commercial norms.[154] California's fictitious-pricing regulatory regime, a product of legislation, voter referendum and case law, differs from Illinois in its approach toward discerning an injury. California's Unfair Competition Law (UCL) affords civil remedies to consumers who suffer injury from "unlawful, unfair or fraudulent business act[s] or practice[s]."[155] After California voters approved Proposition 64 in 2004,[156] revising the standing threshold for private actors in suits under the UCL,[157] and by reference, California's False Advertising Law (FAL),[158] a question arose about the nature of the injury that would need to be demonstrated for a private UCL suit to proceed.[159]

153. As noted in the Introduction, state action does not effectively address fictitious pricing. Paul Rubin argues that state regulation of advertising is less competent than federal regulation and is politically-driven while also understaffed. He also expresses concerns that multiple overlapping regulators might "lead to more restriction of advertising than is appropriate." Paul H. Rubin, *Information Regulation* (*Including Regulation of Advertising*), *in* 3 ENCYCLOPEDIA OF LAW & ECONOMICS 271, 274 (Boudewijn Bouckaert & Gerrit De Geest eds., 2000).

154. California's gross domestic product (GDP) was $2 trillion in 2011, constituting thirteen percent of the nation's output. The California economy equates to that of the ninth largest country in the world. LEGISLATIVE ANALYST'S OFFICE, 2013 CAL FACTS (2013), http://www.lao.ca.gov/reports/2013/calfacts/calfacts_010213.aspx#Californias_Economy.

155. CAL. BUS. & PROF. CODE § 17200 (West 2015). Also of note, local prosecutors have the authority to bring UCL actions. *See* Order of Final Judgment, California v. Southdale Kay-Bee Toy Inc. (Cal. Super. Ct. Aug. 2003) (No. 26-15784); Jay Goetting, *Toy Story: Napa To Get $200,000 in Lawsuit*, NAPA VALLEY REG. (Aug. 20, 2003), http://napavalleyregister.com/news/toy-story-napa-to-get-in-lawsuit/article_61d89f98-a858-5fe6-af0d-8f26459414e7.html.

156. TEXT OF PROPOSED LAWS 109–10 (2004), http://vig.cdn.sos.ca.gov/2004/general/propositions/prop64text.pdf.

157. Limiting standing to any person "who has suffered injury in fact and has lost money or property as a result of such unfair competition." *Id.*

158. *See* CAL. BUS. & PROF. CODE §§ 17200, 17500–17509 (West 2015); Korea Supply Co. v. Lockheed Martin Corp., 63 P.3d 937, 943 (Cal. 2003) (stating that the UCL can "borrow[] violations from other laws by making them independently actionable as unfair competitive practices").

159. *See* Kwikset Corp. v. Superior Court, 246 P.3d 877, 881–82 (Cal.

In *Kwikset Corp. v. Superior Court*, the California Supreme Court addressed the question of what a consumer would have to allege to show an "economic injury from unfair competition."[160] Though this case is not a private case, nor is it a fictitious-pricing case, the arguments lay a foundation for private fictitious-pricing litigation. The Court noted that there were "innumerable ways" for a consumer to show injury from unfair competition, such as:

> (1) surrender[ing] in a transaction more, or acquir[ing] in a transaction less, than he or she otherwise would have;
>
> (2) hav[ing] a present or future property interest diminished;
>
> (3) be[ing] deprived of money or property to which he or she has a cognizable claim; or
>
> (4) be[ing] required to enter into a transaction, costing money or property, that would otherwise have been unnecessary.[161]

Kwikset did not address fictitious pricing, but rather a deceptive "origin of the goods" claim.[162] The plaintiff's claim resulted from being misled about the origin of goods he purchased from Kwikset—locksets advertised as "Made in the U.S.A." that contained components manufactured overseas.[163] The plaintiffs alleged that before transacting, they "saw and read [Kwikset's] misrepresentations [about origin,] . . . relied on such misrepresentations in deciding to purchase . . . [the locksets] . . . and would not have purchased them if they had not been so misrepresented."[164] The false-origin claim caused the plaintiffs to buy products that they did not want causing them to "spend and lose . . . [the] money . . . paid for the locksets," thereby "suffer[ing] injury and loss of money."[165]

The *Kwikset* court, though discussing origin and not pricing, boiled down the problem: "Simply stated: labels matter. The marketing industry is based on the premise that labels matter [and] that consumers will choose one product over another similar product based on its label . . . ."[166] This logic should support an argument that *price* labeling "matters," and that price labeling tries to achieve the same goal of persuading consumers to choose one product over a similar one:

> For each consumer who relies on the truth and accuracy of a label and

2011).

160. *Id.* at 885.

161. *Id.* at 885–86.

162. *Id.* at 882–83.

163. *Id.* at 881–82.

164. *Id.* at 883.

165. *Id.*

166. *Id.* at 889.

> is deceived by misrepresentations into making a purchase, the economic harm is the same: the consumer has purchased a product that he or she *paid more for* than he or she otherwise might have been willing to pay if the product had been labeled accurately. This economic harm—the loss of real dollars from a consumer's pocket—is the same whether or not a court might objectively view the products as functionally equivalent.[167]

The analogy of an origin case to a deceptive pricing case is imperfect. A price is not a description of the goods. As the *Kwikset* court notes, wine labeled "Kosher" loses all value to the Kosher-observant consumer who discovers later that the wine origin is not Kosher.[168] With price, a moment of transactional reckoning comes at the cash register or on the checkout page of a website. The retailer presents the actual price at that moment and the consumer transacts at that price. The question is whether the presented actual price, if fictitious, caused economic harm to the consumer. A disgruntled Kohl's customer, armed with the *Kwikset* decision, received an affirmative response to that question from the Ninth Circuit, sharply contrasting with the Illinois outcome.

In *Hinojos v. Kohl's Corp.*, the plaintiff alleged a fictitious-pricing claim against retailer Kohl's, claiming that he purchased luggage and clothing items that were either routinely sold at the advertised "sale" price, or that the "advertised . . . 'regular' prices did not reflect prevailing retail market prices during the three months immediately preceding [their] publication."[169] Hinojos rounded out his complaint pleading "that he 'would not have purchased [these] products at Kohl's in the absence of Kohl's misrepresentations.'"[170] In his opinion, Judge Stephen Reinhardt opened with a diatribe about fictitious pricing:

> Most consumers have . . . purchased merchandise that was marketed as . . . "on sale" because the proffered discount seemed too good to pass up. Retailers, well aware of consumers' susceptibility to a bargain . . . have an incentive to lie to their customers by falsely claiming that their products have previously sold at a far higher "original" price . . . to induce customers to purchase merchandise at a purport-

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167. *Id.* at 890.

168. *Id.* at 889. For an argument for honoring consumer preferences with respect to the processes behind a product rather than the mere qualities of the product per se, see Douglas A. Kysar, *Preferences for Processes: The Process/Product Distinction and the Regulation of Consumer Choice*, 118 HARV. L. REV. 526, 526 (2004) (examining the conceptual distinction between "process-related information" and "product-related information").

169. Hinojos v. Kohl's Corp., 718 F.3d 1098, 1102 (9th Cir. 2013). The issue presented was whether the plaintiff had standing. *Id.* at 1103.

170. *Id.* at 1102.

> edly marked-down "sale" price. Because such practices are misleading—and effective—the California legislature . . . prohibited them.[171]

Judge Reinhardt accurately observed that the California legislature specifically addressed the marketing behavior that Hinojos alleged. The California FAL provides a crisp rule regarding unfair advertising with respect to former-price comparisons[172]:

> No price shall be advertised as a former price of any advertised thing, unless the alleged former price was the prevailing market price . . . within three months next immediately preceding the publication of the advertisement or unless the date when the alleged former price did prevail is . . . stated in the advertisement.[173]

The California standard for establishing the reference price is much less forgiving than the FTC Guides. The former price must be the prevailing market price, not an actual former price offered under some vague standard of good faith. If not, the retailer must actually declare with precision when the former price was offered. If enforced, the standard could provide consumers with greater confidence in the discounts that they observe—and retailers with concrete guidance about discount promotion. But risks associated with discount promotion might cause advertisers to shy away from such campaigns, which may reduce competition.

That aside, the California standard for establishing individual harm stands apart from Illinois. The facts of *Hinojos* matched the *Kwikset* requirements for recognizing an economic injury, thus establishing standing for the plaintiff.[174] Judge Reinhardt concluded that "price advertisements matter" in consumer decision making[175] and more specifically, "'regular' or 'original' price [advertisements matter,] provid[ing] important information about the product's worth and . . . prestige."[176] Citing marketing scholarship, Judge Reinhardt noted that discounts "created an impression of savings . . . enhancing . . . willingness to buy the product," while prematurely stopping the consumer's search for a lower price.[177] Reference-price misin-

171. *Id.* at 1101.

172. In turn, unfair advertising equates to unfair competition under the UCL. *Id.* at 1103.

173. CAL. BUS. & PROF. CODE § 17501 (West 2015).

174. *Hinojos*, 718 F.3d at 1107; *cf.* Kwikset Corp. v. Superior Court, 246 P.3d 877, 892–95 (Cal. 2011) (applying the requirements of the UCL and concluding that the plaintiff had standing).

175. *Hinojos*, 718 F.3d at 1107.

176. *Id.* at 1106.

177. *Id.* (citing Grewal & Compeau, *Comparative Price Advertising*, *supra* note 12, at 55).

formation would matter to consumers in the same way that any false label would.[178] *Kwikset* analogized that selling a falsely-labeled Rolex watch would inflict harm on consumers, even if the watch functioned and looked exactly like a Rolex.[179]

Judge Reinhardt contended that fictitious pricing could inflict even more injury than the deceptive-origin claim in *Kwikset*. "The deceived bargain hunter suffers a more obvious economic injury as a result of false advertising . . . because the bargain hunter's expectations about the product he just purchased is precisely that it has a higher perceived value and therefore has a higher resale value."[180]

Further, the *Hinojos* court pointedly rejected the defendant's argument, accepted in Illinois, that the plaintiff received the "benefit of the bargain," noting that the price-reference misrepresentation at issue was "material."[181] Judge Reinhardt referenced common-law definitions of materiality, but also noted that the deceptive-pricing prohibition made the misrepresentation per se material.[182] Hinojos' allegations "that Kohl's made material misrepresentations [inducing] him to buy products he would not otherwise have purchased" were sufficient to support the standing requirements for economic injury.[183]

Though the *Kwikset* and *Hinojos* cases proffer the notion that a fictitious-pricing plaintiff can formulate a sufficient injury claim to support standing, how to calculate that remedy remains unclear. The remedy may be material, but after departure from benefit-of-the-bargain theory, theorizing damages proves difficult. Though Judge Reinhardt locates private harm—harm that can be avoided not just through private enforcement, but also through public enforcement—the magnitude of that harm could prove difficult to measure. *Hinojos* does not explicitly solve the harm-measurement puzzle completely cast aside by Illinois law, but it raises the *Kwikset* questions that should weigh in the calculation of the benefits of renewed enforcement.

III. THE WELFARE IMPACT OF FICTITIOUS PRICING

A strong consensus supports the finding that fictitious pricing interferes with markets, yields inefficiency, and reduces

178. *Id.*
179. *Id*. (citing *Kwikset*, 246 P.3d at 890).
180. *Id.*
181. *Id.* at 1107.
182. *Id.*
183. *Id.*

welfare. However, regulators need to exercise precision in combatting fictitious pricing to ensure that price competition would not be truly diminished. There is a role for regulation and enforcement, even though none is happening on the federal level now. Even the harshest critics of fictitious-pricing enforcement concede that some scenarios are severe enough to warrant prosecution.[184]

In Section A, this Article discusses the welfare-driven arguments offered *against* enforcement by Robert Pitofsky. In Section B, this Article counters the arguments in Section A with conclusions from the body of economic and marketing literature that overwhelmingly show that fictitious pricing distorts competition and diminishes welfare. Finally, in Section C, this Article examines the approaches taken by the New York Attorney General in two settlement decrees, and by a California court in *People v. Overstock.com*. These approaches point toward the proper, welfare-maximizing approach, while avoiding the problem of demonstrating individual injury.

A. Welfare Arguments Against Enforcement

Robert Pitofsky's arguments for ceasing FTC enforcement warrant notice.[185] His 1977 *Harvard Law Review* article[186] provided the deepest publicly available insight into the rationale behind enforcement discontinuation. Pitofsky offered a rigorous framework for justifying regulatory intervention, identifying factors that would indicate an advertising-driven "market failure."[187] In sum, Pitofsky expressed certainty that retail markets, if left unfettered, would fail to consistently produce sufficient and accurate information about quality—and price. Yet,

184. *See* Pitofsky, *Pricing Laws, supra* note 17, at 62–63 (advancing multiple arguments for why it is unwise policy to prosecute fictitious pricing "except in the most extreme and egregious circumstances").

185. Pitofsky has been described as a "Founding Father" of the "modern FTC." Muris, *supra* note 19. In addition to working in academia, Pitofsky authored the historic 1969 ABA Report, headed the FTC's Bureau of Consumer Protection, and served as FTC Commissioner and Chairman. *Id.*

186. Pitofsky, *Beyond Nader*, *supra* note 20.

187. *Id.* at 663–66. From reading Pitofsky's article, it is possible to discern characteristics that suggest a market failure. They include (1) where consumers have difficulty tracking and comparing the variety of constantly changing offers and *pricing* information; (2) when competition does not always provide accurate information about price and quality—and "rivals . . . rarely . . . challeng[e] . . . questionable claims"; (3) when markets have limited competition due to market structure, leading to low-information advertising on price and quality; (4) when the cost of information provision proves too high when the consumer market remains small; and (5) where sellers have better use for their advertising budget than rebutting claims of rivals. *Id.*

Pitofsky rejected the notion that enforcing fictitious-pricing regulation would produce a net benefit for consumers.

Pitofsky shared at length his well-developed views of the aims of advertising regulation. He linked consumer access to "truthful data" with "effective competition in the market,"[188] observing that access to truthful advertising facilitates price comparison.[189] False advertising, he recognized, can lead to "misallocation of economic resources . . . by diverting trade to high priced premium products that differ from cheaper substitutes only in the quality and volume of advertising."[190] Pitofsky noted that "where product claims are viewed with utter suspicion, high price is adopted as an indication of quality, and price competition . . . become[s] economically irrational."[191]

Though these observations should raise concerns about fictitious pricing, Pitofsky believed consumers could fend for themselves on this front. Consumer protection from false advertising, he maintained:

> should not be a broad, theoretical effort to achieve Truth, but rather a practical enterprise . . . . [W]here consumers are fully capable, through common sense or simple observation, of protecting their interests against advertising exaggerations or distortions, there would be no reason for the law to intervene.[192]

Fictitious-pricing enforcement may "achieve Truth," but Pitofsky asks, at what cost? Would enforcement enhance, preserve, or harm price competition? Are consumers capable of "protecting their interests" through "simple observation" in this context?[193] Pitofsky viewed enforcement as unjustifiable.[194] Even in an era of renewed advertising regulation efforts, he questioned allocating resources toward pursuit of fictitious-pricing claims.[195]

Pitofsky acknowledged that fictitious-pricing tactics could inflict "competitive or consumer injuries" by misdirecting buyers "from the more efficient low-price seller, [causing execution of purchases] . . . that might not otherwise occur" or occur at that time.[196] He conceded that consumers might be deprived of

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188. *Id.* at 671.
189. *Id.*
190. *Id.*
191. *Id.*
192. *Id.*
193. *Id.*
194. *See id.* at 687–88 (arguing that fictitious pricing enforcement is unnecessary and costly).
195. *Id.*
196. *Id.* Armstrong and Chen more recently raised concern about this dy-

the "benefits of the bargain they *thought* they were receiving."[197]

Ultimately, however, Pitofsky dismissed the significance of fictitious pricing, labeling the tactics "innocuous." He assumed that price-comparison shopping would be frictionless, or that consumers would dismiss aggressive discount claims as puffery.[198] Pitofsky contended that if "consumers [were] accurately informed of the offering price, they [could] make sensible decisions."[199] This contention assumed away a fundamental problem—the "offering price" has not been "accurately informed" if the associated reference price providing context proves fictitious—and the earlier discussion of the role of behavioral economics explains why.

Pitofsky expressed structural concerns about the role of discount pricing in retail markets, particularly that fictitious-pricing enforcement would derail retail "discounters," key drivers of competition.[200] Enforcement would deter discounter market entry and disproportionately burden existing discounters. Pitofsky warned that incumbent "nondiscounters" would regularly report discounters to the FTC, using regulation as a weapon.[201] He summarized his argument that enforcement would *disrupt* price competition:

> Aggressive enforcement against discounters that forces them to hew close to the line of accurate information may tend to dampen competitive activity. Often . . . discount promotions . . . assist new entrants in penetrating concentrated markets . . . . [T]he cost . . . of ascertaining whether particular discount claims are accurate may deter [sellers] from making such claims at all.[202]

Pitofsky's position on fictitious pricing has proven durable. In 1991, Timothy Muris echoed the 1977 logic at length.[203]

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namic. *See generally* Armstrong & Chen, *supra* note 12, at 25 (describing economic models of consumer responses to discounted prices, and concluding, "[b]ecause of their incentive to mislead customers, in some—but not all—of the situations we discuss, there is a potential role for policy to prevent sellers advertising false discounts").

197. Pitofsky, *Beyond Nader*, *supra* note 20, at 688 (emphasis added).

198. *Id*. at 687–88 (arguing that "unlikely" claims such as "lowest price ever" or ambiguous discounts "will be ignored by almost all customers").

199. *Id.* at 688.

200. *See id.*

201. *Id.* Perhaps the observations about favor for high-quality incumbents in the wood, fur, and textiles industries, noted by Posner, and referenced in the 1969 ABA Report, explains this view. *See* 1969 ABA REPORT, *supra* note 26, at 34.

202. Pitofsky, *Beyond Nader*, *supra* note 20, at 688.

203. *See* Timothy J. Muris, *Economics and Consumer Protection*, 60 ANTITRUST L.J. 103, 111–16 (1991).

Muris also cited the 1989 Report of the ABA Antitrust Section Special Committee to Study the Role of the Federal Trade Commission (1989 Report) for the premise that excessive regulation of price advertising could ultimately injure consumers.[204] The 1989 Report concluded that "[e]xcessive regulation of pricing claims can harm consumers, as *experts* on advertising have come to appreciate."[205] The sole expert expressly cited in the 1989 Report was Pitofsky.[206]

In 2004, Pitofsky reiterated his criticisms of fictitious-pricing enforcement, with special emphasis on state-level enforcement activity.[207] Concerned about the "varied landscape of state laws," he suggested that states should repeal their consumer-protection statutes relating to fictitious pricing and only pursue enforcement in the "most extreme and egregious circumstances."[208] Since 1969, "extreme and egregious" fictitious-pricing circumstances may have presented themselves *somewhere*, but the FTC has not pursued *a single seller* during that period. Pitofsky repeated verbatim his 1977 concerns about the social and economic costs of enforcement, the "dampen[ing] of competitive activity" from having to "hew close to the line of accurate information," and the anti-competitive effects that would result from potential deterrence of discount claims.[209]

With the retail environment of the 1970s long gone, Pitofsky expressed the very same concerns about fictitious-pricing regulation in 2004, maintaining that "the FTC . . . made the judgment, correctly . . . that the chilling effect of deceptive pricing regulation on retailers, and the inherent subjectivity and difficulty in ascertaining compliance, have brought about more harm than good."[210] Pitofsky observed that informed consumers had better evaluative tools in 2004 for making price comparisons, noting the newfound ability to check prices with

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204. *Id.* at 112.

205. ABA, REPORT OF THE ABA ANTITRUST SECTION SPECIAL COMMITTEE TO STUDY THE ROLE OF THE FEDERAL TRADE COMMISSION 37 (1989) (emphasis added). The 1989 Report offered a straw-man argument in defense of non-enforcement. As an illustration of the horribles that could result from enforcement, the Report offered the hypothetical of regulators "prohibiting 'sales' featuring less than 10 percent price reductions" and warning that such a regulation "could increase price rigidity." *Id.* The Guides *never* deemed such a practice deceptive, and the FTC never contemplated considering such a reduction.

206. *See id.*

207. Pitofsky, *Pricing Laws*, *supra* note 17, at 62–63.

208. *Id.*

209. *Id.* at 63 (citing Pitofsky, *Beyond Nader*, *supra* note 20).

210. *Id.*

retailers like Amazon.com and e-Bay.[211]

Over time, as noted, private and state actions surfaced offering facts that could meet Pitofsky's "extreme and egregious" criteria for FTC enforcement.[212] These cases provide grounds for specific opportunities for intervention, but more recent evidence emphatically supports a broader policy that includes enforcement. In Section B, this Article reassesses the value of enforcement, reviewing the literature that has emerged to support the premise that fictitious pricing interferes with markets and reduces welfare.

B. WELFARE ARGUMENTS SUPPORTING ENFORCEMENT

Decades of marketing research have revealed the distortions that fictitious pricing can inflict on the market. The literature has, in fact, played a role in prominent recent fictitious-pricing litigation. In *Hinojos*, Judge Reinhardt expressed concern that fictitious pricing would stop a consumer from continuing to search for a truly lower price, citing a 1992 Dhruv Grewal and Larry D. Compeau literature survey as support.[213] In *Overstock.com*, the court, in ordering the company to comply with fictitious-pricing regulation, also gave weight to 1998 and 2004 analyses by Grewal and Compeau.[214] Nonetheless, the backdrop of advertising regulation reveals that intervention must be done with caution to avoid harming the pro-competitive effects of advertising. This Article explores that backdrop in Subsection 1. In Subsection 2, this Article describes the rich body of work that makes the fictitious-pricing

211. *Id.* at 64.

212. *See* cases cited *supra* note 15 and accompanying text.

213. Hinojos v. Kohl's Corp., 718 F.3d 1098, 1106 (9th Cir. 2013) (citing Grewal & Compeau, *Comparative Price Advertising*, *supra* note 12, at 55 (recommending closer policymaker scrutiny of prior-reference pricing practices, based on a survey of twenty-eight separate studies of former-price comparisons and closely related practices)).

214. People v. Overstock.com, Inc., No. RG10546833, 2014 WL 657516, at *12–13 (Cal. Super. Ct. Feb. 5, 2014). The *Overstock.com* case is presumably referencing Larry D. Compeau & Dhruv Grewal, *Comparative Price Advertising: An Integrative Review*, 17 J. PUB. POL'Y & MARKETING 257, 257 (1998) [hereinafter, Compeau & Grewal, *An Integrative Review*] (summarizing twenty years of analyses, concluding that comparative price advertising is effective, "with a strong opportunity for deception, requir[ing] careful management and monitoring"), and Larry D. Compeau et al., *Consumers' Interpretations of the Semantic Phrases Found in Reference Price Advertisements*, 38 J. CONSUMER AFF. 178 (2004) (concluding that pricing claims related to regular versus sales prices "may be . . . informative or deceptive depending on the meaning that the consumer attaches to the claim," much like other findings in consumer research).

arena an exception worthy of consideration for more regulatory scrutiny and enforcement.

1. Concerns About Regulatory Pricing Intervention

Advertising plays a critical role in signaling and market competition. Regulators should be generally reticent to impede advertising by correcting every flaw and imperfection. But where a deceptive activity is both common and injurious to welfare, the reticence should be eschewed in favor of vigilance. Before this Article discusses empirical evidence supporting the reassessment of regulatory intervention with fictitious pricing, this Article first addresses the general concerns about regulatory interference with retail-pricing disclosure.

Regulators have reason to exercise caution when intervening in regulating or restricting retail-price disclosure.[215] As Howard Beales et al. observed, mandating the withholding of information from the market can "inhibit competition, with consequent efficiency losses."[216] According to another analysis, "the prices of goods and services in places that restrict advertising tend to be higher than those in places that do not restrict advertising."[217] Beginning in the 1970s, evidence emerged supporting the notion that fewer restrictions on general advertising leads to lower prices. Deregulation of price disclosure in professions, notably optometry, provided an opportunity for comparative cross-state studies confirming this conclusion.[218] One other analysis from this era observed the downward impact on pharmaceutical pricing from price advertising.[219] More recently, studies of the impact of permitting price disclosure on

215. *See generally* REBECCA TUSHNET & ERIC GOLDMAN, ADVERTISING & MARKETING LAW: CASES AND MATERIALS 23–25 (2d ed. 2014); David Adam Friedman, *Debiasing Advertising: Balancing Risk, Hope, and Social Welfare*, 19 J.L. & POL'Y 539, 608–09 (2011).

216. Howard Beales et al., *The Efficient Regulation of Consumer Information*, 24 J.L. & ECON. 491, 514 (1981).

217. Zeynep K. Hansen & Marc T. Law, *The Political Economy of Truth-in-Advertising Regulation During the Progressive Era*, 51 J.L. & ECON. 251, 255 (2008).

218. *See, e.g.*, Lee Benham, *The Effect of Advertising on the Price of Eyeglasses*, 15 J.L. & ECON. 337, 351–52 (1972); Lee Benham & Alexandra Benham, *Regulating Through the Professions: A Perspective on Information Control*, 18 J.L. & ECON. 421, 427 (1975); John E. Kwoka, Jr., *Advertising and the Price and Quality of Optometric Services*, 74 AM. ECON. REV. 211, 211 (1984).

219. John F. Cady, *An Estimate of the Price Effects of Restrictions on Drug Price Advertising*, 14 ECON. INQUIRY 493, 493 (1976).

the price of alcoholic beverages[220] and permitting more general advertising for breakfast cereals[221] have revealed that lower prices result.[222]

As Beales et al. identified, carving out areas where regulators would be prudent to pursue "information remedies" related to deceptive advertising proves challenging in light of the pattern that less regulation seems to translate to more price competition.[223] The authors categorize "information remedies" in markets as "(a) removing restraints on information; (b) correcting misleading information; and (c) encouraging additional information."[224] Regulators would face the task of intervention, and as Beales and his coauthors observed, "remedying deficiencies in the information market is in some ways a more complex and subtle task than regulating product markets directly."[225] With respect to fictitious pricing, regulators face the challenge of "correcting misleading information" and "encouraging additional information," while not unduly restraining information.[226] The costs of compliance and risks of penalties should not be so burdensome as to prevent price competition.

Advertisers, however, may have turned a long-accepted observation about the nature of false advertising inside-out. In the 1970s, Phillip Nelson divided offering attributes into "search," "experience," and "credence" characteristics.[227] "Search" characteristics, (e.g., product size, shape, product category, and *price*) were deemed easier for consumers to verify and therefore of less concern for regulators. "Experience" characteristics presented more concern, as they were more difficult for consumers to observe and verify, like quality and nature of

220. Jeffrey Milyo & Joel Waldfogel, *The Effect of Price Advertising on Prices: Evidence in the Wake of* 44 Liquormart, 89 AM. ECON. REV. 1081, 1095 (1999) (discussing that lower prices result in certain circumstances).

221. C. Robert Clark, *Advertising Restrictions and Competition in the Children's Breakfast Cereal Industry*, 50 J.L. & ECON. 757, 759–60 (2007).

222. The results, however, are not always unambiguous. *See* WILLIAM W. JACOBS ET AL., FTC, IMPROVING CONSUMER ACCESS TO LEGAL SERVICES: THE CASE FOR REMOVING RESTRICTIONS ON TRUTHFUL ADVERTISING 123–27 (1984) (finding that while "in almost every case," attorneys who used advertising charged lower prices than attorneys who did not, "personal injury attorneys who advertised" charged about 3% more than personal injury attorneys who did not).

223. Beales et al., *supra* note 216, at 513.

224. *Id.* at 514.

225. *Id.*

226. *See* Friedman, *supra* note 215, at 569 n.99.

227. *See, e.g.*, Phillip Nelson, *Advertising as Information*, 82 J. POL. ECON. 729, 730 (1974); Phillip Nelson, *Information and Consumer Behavior*, 78 J. POL. ECON. 311, 312 (1970).

the item, until purchased, though consumers might be less likely to give such claims credibility.[228]

As Lillian BeVier posited, "incentives to falsify . . . advertisements should be understood as a function either of consumers' ability to verify claims prepurchase or of consumers' disinclination to believe self-interested claims."[229] BeVier contended that consumers had the power to retaliate against deceptive advertisers, and that "withhold[ing] repeat purchases" and negative word-of-mouth would work as "weapons" to deter dishonest advertisement.[230] She did not overextend this claim, concluding that "[w]hen this reality is fed into the calculus, the dimensions of the problem of deceptive advertising for experience qualities continue to shrink."[231]

The nature of fictitious pricing does not fit well with the Nelson model for two major reasons. First, consumers duped by fictitious pricing may not detect the "duping" as readily as they might a deficiency in advertised quality. Second, as Roger Schechter responded directly to BeVier,[232] once induced to try a product, consumers tend to continue purchasing a brand "until some external source brings [a] falsehood to [their] attention."[233] Having tried the brand, the consumer "may become 'hooked' on the objective features of the [product]."[234] In other words, advertisers may successfully use falsehoods—or fictitious pricing—to induce an initial experience.[235] After the initial experience the inclination to shop further, on price or other attributes, may diminish; the gathering of incremental shopping information may appear to the consumer to have decreasing returns.

Generally, the research into the effects of fictitious pricing emphasizes the power of the practice to stop consumer search—and the accompanying welfare impact. The harms that Schechter points out may be real—a misleading practice like fictitious pricing could hook a consumer on an item for the long term. But the individual harm would prove difficult to measure. To the extent that all advertising changes preferences, fic-

228. For a discussion of Nelson's work and subsequent critiques, see Lillian R. BeVier, *Competitor Suits for False Advertising Under Section 43(a) of the Lanham Act: A Puzzle in the Law of Deception*, 78 VA. L. REV. 1, 9–12 (1992).

229. *Id.* at 8.

230. *Id.* at 11.

231. *Id.* at 12.

232. *See* Roger E. Schechter, *Additional Pieces of the Deception Puzzle: Some Reactions to Professor BeVier*, 78 VA. L. REV. 57, 71 (1991).

233. *Id.* at 72.

234. *Id.*

235. *Id.*

titious pricing, by inducing a consumer to transact and commit to a product, may have the same effect. However, as this Article discusses next, the welfare effects of fictitious pricing have consistently been found to be significant.

2. Evidence Supporting Fictitious-Pricing Intervention

Price remains a basic search characteristic, but the incentives to manipulate the role of pricing in "search" are high if the prior-reference price stunts the search process. Verification of a false prior-reference price might prove logistically challenging—and those who verify and truly seek the lowest price either have significant expectations of financial savings from continued shopping or a low self-imputed value to their time.

The low likelihood that a consumer will notice individual harm from this type of falsity makes fictitious pricing tempting for advertisers. Compared with individual consumers, regulators can more readily identify the practice. The charge of the FTC, as well as the legal regime in states like California, enables prosecution of the practice under the notion of a general harm to welfare, without worry of proving individual harm.

One analysis of an adjacent problem proves informative. In 1990, Ian Ayres and F. Clayton Miller predicted that if automobile price-markup information became more available and accurate, shoppers would not need to shop as much to ensure that they were getting the right deal.[236] Ayres and Miller observed that accurate disclosure of "[m]arkup information [could] . . . serve as a dramatic substitute for consumer search."[237] The power of *accurate markup* information speaks to the power of *inaccurate markdown* information. Fictitious pricing provides a dramatic, *misleading* substitute for consumer search—one less likely to lead the consumer to the lowest price.

Mark Armstrong and Yongmin Chen provided the most recent economic analysis of discount pricing, including fictitious pricing.[238] They concluded that, "[b]ecause of their incentive to mislead customers, in some . . . situations . . . there is a potential role for policy to prevent sellers advertising false discounts . . . . In most cases, the overall impact on welfare of a

236. Ian Ayres & F. Clayton Miller, *"I'll Sell It to You at Cost": Legal Methods To Promote Retail Markup Disclosure*, 84 NW. U. L. REV. 1047, 1048 (1990).

237. *Id.*

238. *See generally* Armstrong & Cheng, *supra* note 12 (investigating discount pricing and discussing some reasons why a discounted price can make a rational consumer more willing to purchase an item).

policy which combats false discounting is positive."[239]

Integrating a description of underlying behavioral concepts,[240] Armstrong and Chen identified two ways that discounts (truthful and otherwise), as opposed to the plain presentation of a low price, can drive purchasing propensity among rational consumers. "First, the information that the product was initially sold at a high price may indicate the product is high quality. Second, a discounted price can indicate that the product is an unusual bargain, and that there is little point searching for alternative, lower prices."[241] As they noted, a fictitious price can prematurely discourage search—the search might stop because the pricing signal wrongfully deceived the consumer into stopping the search.[242] If consumers are tricked into ceasing a search for true lower prices, true price competition will likely be displaced as a means for competing for consumer attention.

The analysis shows that "false discounts discourage consumers from investigating rival offers[,] . . . depriv[ing] rivals of [the] opportunity to compete effectively. In these settings, preventing [fictitious pricing] can lead to more effective competition."[243] Because honest discounters might have fewer items on sale at any given time, dishonest sellers prevail in the market, exacerbating the price-competition problem.[244] The authors ultimately concluded that "[i]n most cases, the overall impact on welfare of a policy which combats false discounting is positive."[245] They prescribed a renewed enforcement policy with caution, however, and with less conviction than their analytical contribution. Armstrong and Chen conceded that no benefit can be realized without *some* measure of enforcement, but they declined to recommend a required enforcement level.[246]

The authors concluded that:

> Sellers have a strong motive to make their customers feel they are getting a special deal, and they have myriad ways to achieve this. It is unrealistic and undesirable to suppose that regulation can address all forms of false discounting without unduly restricting a seller's mar-

239. *Id.* at 25.
240. *Id.* at 1–5.
241. *Id.* at 25.
242. *Id.* at 5.
243. *Id*.
244. *Id.*
245. *Id.* at 25.
246. *Id.* at 25–26.

keting abilities, and regulators should focus only on flagrant examples of deception.[247]

This conclusion fits neatly with Pitofsky's proposed "extreme and egregious" threshold for taking action,[248] a threshold that appears to exist in theory only.

Previous studies comported with Armstrong and Chen's conclusions, but they supported the welfare argument with more certainty. The 1998 Compeau and Grewal study left "little doubt that comparative price advertisements work," finding that "the [overall] potential for deception seem[ed] rife because external reference prices have a strong influence on consumers, even when they are exaggerated."[249] The 1992 Grewal and Compeau meta-analysis remains the most thorough survey of the prior-reference-pricing literature, analyzing twenty-eight empirical studies.[250]

Grewal and Compeau extracted two notable consensus conclusions.[251] The first set of conclusions showed empirical support for the notion that a "reference price create[s the] impression of savings" and that "the presence of a higher reference price enhances subjects' perceived value and willingness to buy the product."[252] Further, the evidence demonstrates that "[i]f the reference price is not truthful, a consumer may be encouraged to purchase as a result of a false sense of value."[253]

The second set of conclusions indicated that "as discount size increases, consumers' perceptions of value and their willingness to buy the product increase, while their intention to search for a lower price decreases."[254] This implied that larger discounts associated with fictitious pricing "mislead the consumer and reduce search."[255] Grewal and Compeau concluded with a compelling set of recommendations to policymakers, most of them urging a more aggressive enforcement approach toward fictitious pricing.[256]

In sum, prior-reference pricing influences consumers, and

247. *Id.* at 26.
248. *See* Pitofsky, *Pricing Laws*, *supra* note 17, at 62–63.
249. Compeau & Grewal, *An Integrative Review*, *supra* note 214, at 263.
250. Grewal & Compeau, *Comparative Price Advertising*, *supra* note 12, at 55.
251. *Id.* ("Four key public policy implications of these studies are discussed . . . .").
252. *Id.*
253. *Id.* at 56.
254. *Id.*
255. *Id.*
256. *Id.* at 58–59.

fictitious prior-reference pricing disrupts retail markets in two primary ways. First, the practice misleads consumers with a signal that distorts perception of product quality. This signaling can lead to one distorted transaction or, as Schechter indicated,[257] a series of transactions following the initial commitment. Second, the practice distorts the very essence of price competition. Consumers rely upon a prior-reference price and associated discount as a measure of savings. Confronted with potential savings, consumers are more likely to stop their searching for a better value—whether that value is better quality, a lower price for the same quality, a different good entirely, or ultimately, a decision not to transact.

The approach taken by regulators in New York and by the Superior Court in the California *Overstock.com* case[258] bypasses the difficulty in discerning individual consumer harm. Because of state statutes, some regulators and courts have found a middle path in addressing this problem. Bypassing the knot of discerning consumer harm, as this Article shows in three examples in Section C, regulators and courts have ultimately favored civil fines, penalties, and injunctive relief directed at punishing and stopping the market-disrupting, fictitious-pricing behavior. Given the difficulties of discerning consumer remedies, this approach presents the clearest path to resolving this problem—an approach that the FTC should restore in measured fashion.

C. MODELS FOR A WELFARE-ENHANCING APPROACH

Models for welfare-enhancing enforcement can be found in a few high-profile instances of state-level public prosecution. State attorneys general[259] have pursued a few fictitious-pricing cases resulting in settlements that effectively prioritize addressing broader welfare harm over private, individual harm. The remedies in the *People v. Overstock.com* judicial opinion reflect the same pattern.[260] These state-level actions offer insight into a potential model for enforcement—one where the regulators stop the market-distorting behavior through penalties and injunctions, but avoid attempting to impose thornier individual remedies.

257. *See* Schechter, *supra* note 232.

258. People v. Overstock.com, Inc., No. RG104546833, 2014 WL 657516 (Cal. Super. Ct. Feb. 6, 2014).

259. And their equivalents.

260. *See Overstock.com*, 2014 WL 657516, at *35–39.

1. State-Level Settlements

State-level fictitious-pricing regulation, though sporadic, has proven successful enough to warrant attention from enforcement critics.[261] A few recent consent agreements show that individual harm has been moved aside in favor of general civil penalties and injunctive relief. For example, in 2011, the New York Attorney General reached a settlement with Michaels Stores, an arts-and-crafts retailer, over fictitious-pricing practices.[262] Michaels Stores had been engaging in "never-ending" sales—continuously advertising services at a prior-reference percentage (or absolute dollar) discount, meaning that the prior-reference point was not the regular price for those items.[263]

New York Attorney General Eric T. Schneiderman offered a nominal justification for enforcement rooted in *rhetoric* that the company hurt individual consumers by roping them into perceived deals: "For years, Michaels duped consumers into thinking they were receiving huge discounts, when in fact, they were simply paying the regular store price . . . . Through deceptive advertising practices, this company violated the law and took advantage of hardworking consumers trying to save money."[264] The New York Attorney General, however, did not ultimately require redress for individual harm or any form of restitution. Instead, the parties agreed that Michaels would pay $800,000 in civil penalties and give $1 million worth of arts-and-crafts supplies to public schools.[265] In essence, the penalty was punitive (and perhaps politically agreeable for both parties) but not restorative to consumers. Also, the agreement enjoined Michaels from continuing to engage in fictitious prior-reference pricing and related practices.[266]

Likewise, in 2004, Schneiderman's predecessor Eliot Spitzer reached an agreement with Jos. A. Bank Clothiers (JABC) over fictitious pricing.[267] The settlement references allegations that, in 2003, less than one percent of JABC's suits, formal wear, trousers, and blazers were offered at the regular

261. *See* Pitofsky, *Pricing Laws*, *supra* note 17, at 64–65.

262. *See* Assurance of Discontinuance, Michaels, *supra* note 16.

263. *Id.* at 2–3.

264. Press Release, Eric T. Schneiderman, Attorney Gen., N.Y., A.G. Schneiderman Secures $1.8 Million from Michaels Stores for Misleading Consumers (Sept. 19, 2011), http://www.ag.ny.gov/press-release/ag-schneiderman-secures-18-million-michaels-stores-misleading-consumers.

265. Assurance of Discontinuance, Michaels, *supra* note 16.

266. *Id.* at 5–7.

267. *See* Assurance of Discontinuance, Jos. A. Bank, *supra* note 16.

price, and only ten percent of dress shirts.[268] The Attorney General further alleged that merchandise was "perpetually 'on sale,'" noting that JABC's three best-selling items, the Signature, Executive, and Trio suits were on sale during all of 2003 with the exception of a few days.[269]

This settlement required JABC to pay $425,000 in civil penalties and $50,000 in costs to New York State.[270] More onerous than the one-time civil penalty, JABC agreed to comply not only with New York's false advertising laws, but also with the FTC Guides—16 C.F.R. § 233.1 (former price comparisons) and with all of 16 C.F.R. § 233 (deceptive pricing).[271] Ironically, New York State compelled JABC to comply with FTC Guides that the FTC does not enforce.

In both of these settlements, New York modeled potential future enforcement actions. Foremost, the state stopped the retailers from engaging in a market-distortive practice that stunts consumer shopping, causes misperceptions of value, and ultimately reduces welfare. The retailers paid a public penalty for untoward market behavior that affected overall welfare, and state avoided intellectual contortions by eschewing the individual remedy.

2. A Judicial Approach

"No one, in history, has ever been asked to do this or [was] sued for not doing it."[272]

- Patrick Byrne, CEO of Overstock, demonstrating unawareness of past and recent history,[273] subsequent to a ruling ordering the company to comply with California discounting regulations.

The reasoning of *People v. Overstock.com* provides an overlay for policymakers and those with discretion to bring fictitious-pricing cases. In *Overstock.com*, the People's complaint af-

268. *Id.* at 2.

269. *Id.*

270. *Id.* at 6.

271. *Id.* at 5.

272. Cade Metz, *Court Decision Could Change Rules for Online Price Comparisons*, WIRED (Jan. 6, 2014), http://www.wired.com/2014/01/overstock-price-ruling.

273. *See supra* text accompanying note 15 (listing active actions as of December 2014); *see also* Hinojos v. Kohl's Corp., 718 F.3d 1098 (9th Cir. 2013) (finding for plaintiffs in a case very similar to *Overstock.com*); *supra* Part III.C.2 (discussing the New York State Attorney General settlement decrees with JAB and Michaels).

forded an opportunity for a California Superior Court to expound upon the various elements of a fictitious-pricing action and explore appropriate remedies and sanctions. This case reveals a compelling logic for why private actions fail, and why public actions, appropriately reined in, provide the best avenue for addressing welfare damage from fictitious pricing.

The remedy imposed by a California court in *Overstock.com* offers guidance for how today's FTC enforcement regime *should* work. The *Overstock.com* case ultimately did not squarely turn on an "internal" prior-reference advertising claim;[274] the case turned on Overstock allegedly creating false list prices for the purpose of discounting.[275] The court found that the company based list prices off estimates from formulas or off the prices of different items.[276] "Every time Overstock displayed a list price based on a formula or a similar product rather than [the manufacturer's established list price] it made an untrue statement."[277]

The eight California district attorneys[278] prosecuting this case alleged that Overstock traded on false representations of discounting practices.[279] Broadly, the court focused on Overstock's practice of labeling and displaying "advertised reference prices" (ARPs) as "intend[ing] to convey to consumers that Overstock was a discounter and [that] very substantial savings could be enjoyed by purchasing from its site."[280] Of concern to the People, in light of literature's consensus about the competitive harm from search stunting, was Overstock's claim: "[W]e compare prices so you don't have to."[281] Ironically, the court found that "compare" labels were not false, per se, because they merely called on the consumer "to do something."[282]

Examining that slogan in conjunction with the false list

274. *See* People v. Overstock.com, Inc., No. RG104546833, 2014 WL 657516, at *32–33 (Cal. Super. Ct. Feb. 6, 2014).

275. *Id.* at *27.

276. *Id.*

277. *Id.*

278. *See id.* at *1. In California, district attorneys and city attorneys can play a role in enforcement. *See* CAL. BUS. & PROF. CODE § 17508, subd. (b) (West 2015). For other notable examples, see California v. Southdale Kay-Bee Toy, Inc., No. 26-15784, 2003 WL 25284541 (Cal. Super. Ct. Aug. 18, 2003); Goetting, *supra* note 155.

279. *Overstock.com*, 2014 WL 657516, at *1 ("At the beginning, most if not all of Overstock's offerings were products from manufacturers, retailers or jobbers who were liquidating excess or outdated inventory . . . .").

280. *Id.* at *3.

281. *Id.* at *2.

282. *Id.* at *27.

prices, however, the advertiser appeared to count on some degree of search stunting, emphasizing that the consumer should be confident in believing that pricing had been thoroughly vetted. Generally, "the People contend[ed] [that] Overstock used labels, formats[,] and practices that resulted in advertising [methods] that [were] often false or at least misleading" under California statutes, rendering them actionable.[283]

The court's remedy analysis confronted Overstock with significant sanctions and penalties that would, if upheld, lead to changes in the company's marketing practices. In enjoining fictitious-pricing behavior and levying penalties while declining to award individual relief, the outcome of *Overstock.com* resembled the two resolutions reached by the New York State Attorney General.[284]

Foremost, the injunctive relief granted to the People was significant in scope.[285] This flavor of injunctive relief echoes the remedies sought by the FTC prior to 1969. For example, Overstock was prohibited from "set[ting] . . . ARP[s] on any basis other than an actual price offered in the marketplace at . . . the time the advertisement is first placed."[286] Also, Overstock could no longer select "the highest price that may be found anywhere" as a reference price, unless Overstock disclosed the context of the discount.[287]

The People unsuccessfully prayed for restitution for individual consumers misled by the deceptive pricing. The People contended that "restitution should be the money that 'may have been acquired' by the false advertising."[288] Specifically, the plaintiffs suggested that all California consumers who purchased items from Overstock over the previous ten years should be given the choice to return the item for a refund or receive a "5% credit towards future purchases."[289]

The *Overstock.com* court viewed the pursuit of individual restitution as "wildly excessive" and "unjustified."[290] Evidence failed to support a claim that all Overstock purchasers were deceived.[291] The People failed to present credible evidence about

283. *Id.* at *3.
284. *See supra* Part III.C.
285. *See Overstock.com*, 2014 WL 657516, at *34–36.
286. *Id.* at *35.
287. *Id.*
288. *Id.* at *36.
289. *Id.*
290. *Id.*
291. *Id.*

pecuniary harm, and the court found the five-percent credit arbitrary.[292] The court concluded that the extensive record in the case did not offer a "reasonable metric . . . [or] methodology" for determining restitution and "identifying . . . who should receive it."[293] This struggle with remedy and injury echoes that of the private actions brought in Illinois, discussed earlier. Regulators should take a cue from this opinion and the New York settlements and avoid the thicket of individual remedy—and instead focus on stopping the general social harm. The *Overstock.com* court focused on the latter.

The court acknowledged that "the most powerful evidence . . . [was] that there was a reduction in search intentions, an increase in a perception of transaction value and a greater likelihood that the consumers would return to [Overstock]."[294] Recognizing market distortion, the court turned next to civil penalties.[295]

The court evaluated the "seriousness of [Overstock's] misconduct" as "moderate."[296] But considering willfulness[297] and Overstock's financial strength, the court imposed a $6,828,000 penalty.[298] The court deemed this amount "the minimum necessary to vindicate the purposes of the statutes."[299] In "vindicating" the statutes—while avoiding the thicket of individual harm—the court attempted to preserve the integrity of signals in the marketplace.

Even if higher courts alter this ruling, or if this matter reaches a settlement during the appellate process, the logic of the *Overstock.com* opinion has appeal particularly with respect to remedies. The *Overstock.com* tack could easily apply to prior-reference pricing, just as it did for external comparative reference pricing. The individual harms inflicted are difficult to identify, but fictitious-pricing behavior can be spotted more easily by regulators who track pricing than by individual consumers. The social harm can be addressed by civil penalties which serve as a deterrent, if not a true recovery mechanism. Future market distortion can be prevented with injunctive orders like the one in *Overstock.com* or stipulated agreements

292. *See id.*
293. *Id.*
294. *Id.* Compeau presented this evidence as an expert at trial. *Id.*
295. *Id.*
296. *Id.* at *38.
297. *Id.* at *39.
298. *Id.* at *38–39.
299. *Id.* at *39.

like those reached by the New York Attorney General in JABC and Michaels Stores. The focus of enforcement should rest on pinpointing social harms (like those identified in the literature), penalizing the infliction of harm, and preventing future harm—while staying out of the minefield of proving individual pecuniary harm.

Overstock attempted to mislead consumers and interfere with consumer decision making by manipulating price advertising. As Judge Easterbrook wrote in *B. Sanfield*, an attorney general would have been able to make a case about deception in "a trice," though the plaintiff in that case could not masquerade as a private attorney general in search of damages that could not be proven.[300] Here, Judge Easterbrook's public attorney general materialized. The California approach, extending from private actions in *Kwikset* to *Hinojos* to the public action in *Overstock.com*, should serve as models for enforcement of fictitious pricing.[301] In Part IV, this Article suggests that the FTC should revisit fictitious pricing, and this Article provides categorical examples of where the FTC might exercise discretion in enforcement.

IV. THE CASE FOR REVISITING ENFORCEMENT

The time for reassessing the viability of enforcement has arrived, especially given the FTC's plans for review of the Guides Against Deceptive Pricing in 2017.[302] The welfare benefits of fictitious-pricing enforcement should outweigh the costs, including costs of incremental enforcement, regulatory opportunity costs, and retailer compliance costs. Though the role of cost-benefit analysis is not entirely uniform across zones of regulation,[303] the FTC has effectively adopted this approach, which this Article describes next in Section A. In Section B, this Article describes the temporal context of the original justifica-

300. B. Sanfield, Inc. v. Finlay Fine Jewelry Corp., 258 F.3d 578, 580 (7th Cir. 2001).

301. Though Pitofsky disfavors all enforcement, this Article agrees with him that if enforcement is left only to states, the patchwork of regulation and varied compliance requirements could be messy. Institutionally, the FTC might be best positioned to address practices of regional and national retailers.

302. *See* Modified 10-Year Regulatory Review Schedule, 79 Fed. Reg. 14199, 14200 (Mar. 13, 2014).

303. The consensus about applying cost-benefit analysis varies across regulatory subject matter. *See* Eric Posner & E. Glen Weyl, *Benefit-Cost Analysis for Financial Regulation*, 103 AM. ECON. REV. 393, 393 (2013). *See generally* MATTHEW D. ADLER & ERIC A. POSNER, NEW FOUNDATIONS OF COST-BENEFIT ANALYSIS (2006) (giving an overview the history of cost-benefit analysis).

tion for nonenforcement and present the changes in retail markets since that time. The promotion of price competition by protecting "discounters" may have been paramount in 1977, but the structure of the industry is quite different today. In Section C, this Article offers some potential frameworks that the FTC could use for prioritizing opportunities for enforcement while recognizing the potential costs of enforcement.

A. COST-BENEFIT ANALYSIS AND FTC POLICY

Understanding the FTC approach toward enforcing fictitious pricing requires context about enforcement of unfair and deceptive practices under Section 5 of the FTC Act.[304] The FTC Act declares unlawful, "[u]nfair methods of competition in or affecting commerce, and *unfair* or *deceptive* acts or practices in or affecting commerce."[305] Though advertising practices can be regulated either through "unfairness" *or* "deception," the FTC has prosecuted most advertising cases through the "deception" standard.[306]

The FTC's application of "deception" proves central to understanding the approach to all federal advertising regulation, "deceptive pricing" included.[307] In 1983, a divided FTC adopted the "Policy Statement on Deception"[308] in response to a congressional inquiry. The 1983 Policy Statement listed three elements that "undergird all deception cases."[309] First, "there

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304. For a brief overview, see Joshua D. Wright, Comm'r, Fed. Trade Comm'n, Remarks at the Economics of Digital Consumer Protection: One Commissioner's View 3–7 (July 31, 2014), http://www.ftc.gov/system/files/documents/public_statements/573061/010731techfreedom.pdf.

305. 15 U.S.C. § 45(a)(1) (2012) (emphasis added).

306. Though the "disjunctive phrase 'unfair or deceptive' suggests that the FTC can pursue advertisers on unfairness per se, the FTC has not taken that path, opting for the deception angle." SPANOGLE ET AL., *supra* note 44; *see also* PRIDGEN & ALDERMAN, *supra* note 44 (providing an overview of the FTC's application of the deception standard to *deceptive* pricing (including bait and switch) as well as unsubstantiated advertising claims, visual deception, unfounded testimonials and endorsements, misleading comparative advertising, deceptive claims for tobacco products, misleading environmental advertising, and deceptive "made in the U.S.A." claims). The FTC also prosecutes deceptive pricing under Section 12 of the FTC Act, but this section is targeted at advertising of food, drugs, devices, services, and cosmetics. 15 U.S.C. § 52(a)(2) (2012).

307. *Cf.* PRIDGEN & ALDERMAN, *supra* note 44, §§ 11:1–5 (explaining the role of "deception" in some FTC prosecutions).

308. FTC Policy Statement on Deception, James C. Miller III, Chairman, Fed. Trade Comm'n (Oct. 14, 1983) (appended to Cliffdale Associates, 103 F.T.C. 110, 174 (1984)).

309. *Id.*

must be a representation, omission or practice that is likely to mislead the consumer." Such practices have been found to include "misleading price claims."[310] Second, the practice at issue must be examined from the standpoint of a "consumer acting reasonably in the circumstances," and third, the "representation, practice, or omission" at issue in the first prong must be "material."[311] If it is likely that the consumer would have "chosen differently but for the deception," "consumer injury" is likely, and materiality is established.[312] In some cases, materiality can be presumed, though other cases may require presentation of evidence.[313]

This deception standard can reach fictitious pricing if the FTC chooses to apply it. False information that misleads a reasonably acting consumer into making a different transactional decision would constitute "deception." Materiality, however, may not be "presumed" in the case of deceptive pricing because it does not fit into specific presumptive categories defined by the 1983 Policy Statement.[314] Nonetheless, materiality can still be proven with evidence "that the claim or omission is likely to be considered important by consumers." A showing "that the product . . . with the feature represented costs more than an otherwise comparable product without the feature, a reliable survey of consumers, or credible testimony" can serve as the required evidence.[315] The Policy Statement concludes:

> A finding of materiality is also a finding that injury is likely to exist because of the *representation*, omission, *sales practice*, *or marketing technique*. Injury to consumers can take many forms. Injury exists if consumers would have chosen differently but for the deception. *If different choices are likely, the claim is material, and injury is likely as well*. Thus, injury and materiality are different names for the same concept.[316]

This last catch-all paragraph, combined with the express mention of "misleading price claims," captures the notion that fictitious pricing would lead to material injury under these standards. The FTC can choose to bring a case under the prem-

310. *Id.*

311. *Id.*

312. *Id.*

313. *Id.*

314. Among the "presumptively material" categories are claims generally related to non-price attributes of the offering. *See id.* Also considered material are claims involving health and safety and claims concerning the purpose, safety, efficacy, cost, durability, performance, warranties, or quality of the offering. *Id.*

315. *Id.*

316. *Id.* (emphasis added).

ise that a deception that leads consumers to different choices equates to a "likely" injury. Courts typically require consumer plaintiffs to prove actual harm.

The FTC certainly would be within the bounds of statutory authority and its own policy statements and guides, were it to proceed with renewed enforcement.

B. CHANGING RETAIL MARKETS

The fundamental assumptions underlying the cost-benefit decision to discontinue enforcement should be revisited. Pitofsky argued that shielding retail discounters from enforcement would free them to offer competitive prices and discounts without worry of regulatory harassment.[317] However, discounters thrived during the era of post-war enforcement,[318] which would indicate that they *never* really required protection. Any notion that discounters were healthy during enforcement alleviates concerns that enforcement would undermine their role in price competition. Even if this concern about discounters *was* well founded in 1969, retailing has changed so drastically since then, that these changes should, at minimum, warrant reassessment of the cost-benefit analysis of enforcement.

1. Post-World-War-II Retail Dynamic

In 1962, prominent industry lawyer Carleton Harkrader observed that in spite of aggressive fictitious-pricing enforcement, discount retailers flourished after World War II, grabbing market share from traditional retailers like urban downtown department stores.[320] Ascribing the peak of enforcement to the emergence of a "retail revolution" of discounters, Harkrader[321] described an environment in which they thrived.[322] Before World War II, department stores dominated their terri-

317. *See* Pitofsky, *Pricing Laws*, *supra* note 17, at 63–64.

318. *See* Harkrader, *supra* note 13, at 4–5.

320. *See id.* at 4–6. Harkrader served as an attorney for the FTC before founding a prominent Washington, D.C. law firm in 1960. *See* T. Rees Shapiro, *Robert L. Wald, Antitrust Lawyer Helped Found Fast-Growing District Firm, Dies*, WASH. POST, Sept. 11, 2010, at B4.

321. In his article, the only contemporaneous academic account of fictitious pricing, Harkrader expressed concerns that one might attribute to an attorney tied into the established retail and manufacturer industry. He argued that the 1958 Guides provided a "rough," but "traversable," road for retailers but expressed special concern for manufacturers who used pre-ticketed prices bearing exposure from retailers who would lower those prices. Harkrader, *supra* note 13, at 27–28.

322. *Id.* at 4–6.

tory. Department stores would typically mark up their merchandise at a standard forty percent above the wholesale price, reflecting the manufacturers' suggested retail price (MSRP), offering different tiers of quality for each product category.[323] In this era, department stores provided higher levels of customer service and competed with each other on service more than price.[324]

In the 1950s, a "new brand of merchandiser" arrived and thrived—discounters,[325] the entities that regulators would later seek to protect from fictitious-pricing enforcement.[326] These new merchandisers "dispensed with expensive frills associated with the traditional department store[s]," emphasizing a "low-markup, high-volume, quick-turnover" approach.[327] The emergence of discounters brought "unprecedented competition," deploying a new business model that disrupted the establishment. Discounters emerged to serve a growing segment of post-war consumers that valued low prices over service.[328]

By minimizing operating expenses, discounters could afford to cut the forty-percent manufacturer markup in half and remain profitable.[329] Discounters enjoyed a relative cost advantage through implementation of self-service, moving to suburbs where the post-war consumers had migrated, and where commercial real estate was less expensive and parking abundant.[330] In 1962, these new stores were occupying "buildings that were often little more than warehouses."[331] This lower cost structure enabled discounters to gain market share from department stores in part through "flamboyant" low-price advertising.[332]

In 1962, discounters certainly did not seem to need much protection from competitors seeking regulatory help. They transformed the landscape. Many established department stores would fail as a result of these new players entering the

323. *See id.* at 4.
324. *See id.*
325. *Id.* at 4–5.
326. *See generally* Muris, *supra* note 19 (detailing Robert Pitofsky's contributions to FTC regulations and consumer welfare); Pitofsky, *Pricing Laws*, *supra* note 17 (examining the history of FTC fictitious pricing regulations).
327. Harkrader, *supra* note 13, at 4.
328. *Id.*
329. *Id.*
330. *Id.*
331. *Id.*
332. *Id.* at 5.

scene.[333] Other incumbents modified their formats or strategically played the discount game, lowering prices on select items. Thus began a "chain reaction of extravagant pricing claims by both kinds of merchants, often abetted by inflated [MSRPs]."[334] These price battles went beyond plain offering or declaration of lower prices, they involved referencing competitor prices.[335]

With discounters flexing their structural pricing advantage, the incumbent, legacy retailers changed tactics. Department stores could not favorably compare their prices to the discounters through direct comparison, so they pursued a different angle. According to Harkrader, the *department stores*—not discounters—initiated the practice of advertising selected sales that referenced a prior price or the MSRP.[336] After department stores entered the discounting game, on many items, the discounters had more difficulty winning through price comparison.[337] Discounters responded by referencing their discounts off the MSRP, too.[338] Retailers of all stripes were compelled to operate comparatively whether they preferred to or not. Prior-reference discount pricing followed.[339] The entry of discounters transformed sleepy pre-war retail competition into the modern era of perpetual discount-based competition. Discounters, even in the early post-war era, did not merely enter and survive—they sparked changes that led to the retail world of today.

After a decade, pricing presentation became indistinguishable between department stores and discount stores,[340] "[i]n the fierce competitive in-fighting for the consumer dollar, fictitious pricing has become a common vice of the [marketplace]."[341] Harkrader claimed that this dynamic left consumers "confused, critical and skeptical,"[342] contending that this sentiment drove the "agitation" for regulatory intervention and reform, culminating with promulgation of the 1958 version of the Guides.[343]

333. *Id.*
334. *Id.*
335. *Id.*
336. *Id.*
337. *Id.*
338. *Id.*
339. *Id.*
340. *Id.*
341. *Id.* at 27.
342. *Id.* at 6. For support, Harkrader cited an article in the popular national press, *Phony Price-Cutting: Threat to Advertising Confidence*, TIME, Nov. 10, 1958, at 78, that in turn cited a Duquesne University study about consumer suspicions about discounting. Harkrader, *supra* note 13, at 6 n.18.
343. Harkrader, *supra* note 13, at 6.

2. Post-1969 Retail Dynamic

The American retail sector transformed substantially since the late 1960s,[344] a factor ignored by Pitofsky and other enforcement critics. Focusing on just the largest industry players does not tell the entire story of retail history, but changes at the top can indicate significant changes in competition and industry structure. From 1970 through 1985, the leaders in the non-supermarket, non-drugstore, retail sector[345] remained fairly stable. In 1970, Sears-Roebuck held the position of largest retailer, followed by J.C. Penney, Montgomery Ward, Kmart, F.W. Woolworth, and Federated Department Stores.[346] In 1975 and 1980, demonstrating remarkable stability, all of these entities remained on the list of the five largest retailers, except for Montgomery Ward.[347]

By the mid-1980s, the same players more or less held ground, but this would change. From the list of top 1985 discounters, only Walmart survived intact in 2014.[348] These "origi-

344. For a discussion and illustration of these changes, see KPMG, THE EVOLUTION OF RETAILING: REINVENTING THE CUSTOMER EXPERIENCE 1, 6–8 (2009), https://www.kpmg.com/CN/en/IssuesAndInsights/ArticlesPublications/Documents/Evolution-retailing-o-200912.pdf.

345. Though supermarkets and drugstores comprise a significant part of retail, this Article wishes to focus this analysis on changes in purchasing that tend to be more discretionary.

346. *See The 50 Largest Retailing Companies*, FORTUNE, May 1971, at 196.

347. *See The 50 Largest Retailing Companies*, FORTUNE, July 1976, at 210; *The 50 Largest Retailing Companies*, FORTUNE, July 1981, at 122.

348. *See* Kapner, *supra* note 7; Wenti Xu, The Market Structure of the U.S. Retail Industry 1984–2003, at 116 (Aug. 2007) (unpublished Ph.D. dissertation, Purdue University). "Kmart" as it is known today, has been through merger and restructuring. *See Kmart History: Retailing Legend Is Born*, SEARS HOLDINGS, http://searsholdings.com/about/kmart/kmart-history (last visited Nov. 24, 2015). Woolworth closed its last U.S. stores in 1997. "Woolworth was 100 years ago what Walmart is today." Jennifer Steinhauer, *Woolworth Gives up on the Five-and-Dime*, N.Y. TIMES, July 18, 1997, at A1. As part of its 1990 emergence from bankruptcy, Ames Department Stores shut down the last remaining Zayres stores. Stanley Ziemba, *Ames Cuts To Wipe Out Ex-Zayres*, CHI. TRIB. (June 9, 1999), http://articles.chicagotribune.com/1990-06-09/news/9002170054_1_ames-department-stores-zayre-ames-shoppers. Ames itself would completely succumb in 2002. Bootie Cosgrove-Mather, *Ames Discount Chain To Close*, CBS NEWS (Aug. 14, 2002), http://www.cbsnews.com/news/ames-discount-chain-to-close. Rapid American spun off Lerner Stores to The Limited in 1985, and its other stores, McCrory and J.J. Newberry would all shut down. *See* Amy Worden, *Cashing out Last of Five-and-Dimes McCrory's Will Shut Its Doors Next Week in Harrisburg, as the Lone Remaining Original Variety-Store Chain Fades away*, PHILA. INQUIRER (Mar. 13, 2002), http://articles.philly.com/2002-03-13/news/25341228_1_mccrory-buxbaum-group-paul-buxbaum; Nancy Yoshishara, *Rapid American Agrees To Sell 796 Stores: Limited Plans To Buy Lerner Chain*, L.A. TIMES (Feb. 5, 1985), http://articles.latimes.com/1985-02-05/business/fi-4964_1_

nal" discounters fell victim to the "category killers" (or "big-box" retailers) arriving next, providing low pricing and superior merchandising through a narrower focus around product category. Broad-merchandising discounters like Sears and Kmart faced aggressive price competition from focused retailers like Toys "R" Us, the Home Depot, Barnes & Noble, Staples, the Sports Authority, Petco, and Best Buy. Warehouse clubs, like Costco, Price Club, and Sam's Club (Walmart's preemptive move into the warehouse arena), also began to chip away, not only at supermarkets but other retailers.[349]

By 2011, these second-wave discounters, the "category killers," found *themselves* in an accelerating competitive struggle with online competition, that some predict might end in a "tsunami wave."[350] After years of riding out (and joining in) online disruption of brick-and-mortar retail markets, the pre-2008 recession investment in physical locations by incumbent retailers put them at a significant cost and flexibility disadvantage to pure online retailers.[351] Book stores, electronic stores, and office-supply retailers all absorbed hits from online retailers.[352]

By 2012, the top grossing non-supermarket, non-drug retailers in the United States were Walmart, Target,[353] Costco,

mccrory. Shoe Corporation of America (SCOA) eventually merged with Hills Department Stores. Both entities are now defunct. *See* Isadore Barmash, *Hills Department Stores Files for Chapter 11 Bankruptcy*, N.Y. TIMES, Feb. 5, 1991, at D2; *Company Overview of Shoe Corporation of America, Inc.*, BLOOMBERG, http://investing.businessweek.com/research/stocks/private/snapshot.asp (last visited Nov. 24, 2015). Rose's Stores, a regional chain of over 100 stores, was purchased in a restructuring by Variety Wholesalers Incorporated. *About Us: About Variety Wholesalers*, VARIETY WHOLESALERS INC., http://www.vwstores.com/page/show/id/6528 (last visited Nov. 24, 2015).

349. ROBERT SPECTOR, CATEGORY KILLERS: THE RETAIL REVOLUTION AND ITS IMPACT ON CONSUMER CULTURE 31–51 (2005).

350. Rajiv Lal & Jose B. Alvarez, *Retailing Revolution: Category Killers on the Brink*, HARV. BUS. SCH. (Oct. 10, 2011), http://hbswk.hbs.edu/item/6813.html.

351. *Id.*

352. *Id.*

353. This Article includes Walmart (which includes Sam's Club), even though 55% of Walmart's United States sales originate in grocery (Walmart is America's largest grocer). *See* WALMART, 2013 ANNUAL REPORT 4 (2013), http://stock.walmart.com/files/doc_financials/2013/Annual/2013-annual-report-for-walmart-stores-inc_130221024708579502.pdf. The remaining non-grocery segment of Walmart's business is large enough that any discussion of the American retail landscape must include it. This Article includes Target because only 20% of its 2012 sales were attributable to groceries and pet supplies. Approximately 55% of sales were attributable to apparel, hardlines (electronics included), and home furnishings. *See* TARGET, 2013 ANNUAL REPORT 64 (2013), https://corporate.target.com/annual-reports/pdf-viewer-2013?cover=6725&parts=6724-6726-6727-6730-6728.

the Home Depot, Lowe's, Amazon.com, Best Buy, Sears, Macy's, and Apple Stores/iTunes.[354] Pitofsky offered his rationale for discontinuing enforcement in 1977. In 1977, with the exception of restructured versions of Sears and Macy's, these top 2012 retailers had low national profiles,[355] or were beyond conception, let alone at the top of any list.[356] By one account, the "traditional department store" had completely collapsed as an institution by 2013.[357]

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354. *See* David P. Schulz, *Top 100 Retailers*, STORES MAG., July 2013. Note that these stores mostly fall into big-box, discount, or online categories. Supermarkets and drugstores have proliferated on the larger list, as well.

355. In 1977, net Walmart sales were $479 million in 153 stores. Eric Francis, *Walmart at 50: A Not-So-Short History of the World's Largest Retailer*, ARK. BUS., July 2, 2012, at 12. By 2012, domestic Walmart sales were $328 *billion*. Schulz, *supra* note 354, at S7. In 1979, the Target store brand only existed in seventy-four stores in eleven states. *Target Through the Years*: *1979*, TARGET, https://corporate.target.com/about/history/Target-through-the-years (last visited Nov. 24, 2015). Costco, an enormous warehouse discounter, opened its doors under the name Price Club in 1976, and the first Costco labeled warehouse opened in 1983. Costco grew to $3 billion in sales in six years, claiming a retail record. *About Us*, COSTCO, http://www.costco.com/about.html (last visited Nov. 24, 2015). The Home Depot was founded in 1978. *See Our History*, HOME DEPOT, https://corporate.homedepot.com/ourcompany/history/pages/default.aspx (last visited Nov. 24, 2015).

356. Although this Article has excluded food and drugstore chains from the basic analysis, many, like Kroger, Walgreen, and CVS Caremark have also emerged at the top of the overall list. *See* Schulz, *supra* note 354, at S7.

357. *See* Joe Weisenthal, *You Might Not Have Realized Just How Much the "Department Store" Has Collapsed*, BUS. INSIDER (Aug. 31, 2013), http://www.businessinsider.com/department-store-decline-2013-8. Indeed, department store sales have steadily declined 29% from their most recent peak in January 2001 to February 2014. *See Retail Trade: Department Stores (Excluding Leased Departments)*, FED. RESERVE BANK OF ST. LOUIS ECON. RES. (Oct. 14, 2015), http://research.stlouisfed.org/fred2/series/RSDSELD. In 1977, Pitofsky expressed concern that "the usual complainants [about discounting practices] have been nondiscounters who emphasize service and reliability rather than price" at the expense of discounters who promote competition. Pitofsky, *Beyond Nader*, *supra* note 20, at 688. The steep sales decline reveals traditional players in the department store industry no longer have the same market share or power. As this Article discusses *infra*, electronic retailing and algorithmic discounting are playing an increasing and still growing role in the retail sphere, though smaller than one might expect. The share of e-commerce retail sales as a percentage of total sales rose from 0.6% at the end of 1999 to 6% at the end of 2013, seasonally adjusted. *See E-Commerce Retail Sales as a Percent of Total Sales*, FED. RESERVE BANK OF ST. LOUIS ECON. RES. (Aug. 17, 2015), http://research.stlouisfed.org/fred2/series/ECOMPCTSA. Nonstore retail sales grew at a compound annual rate of 9% between 1992 and 2013. *See Retail Trade: Nonstore Retailers*, FED. RESERVE BANK OF ST. LOUIS ECON. RES. (Oct. 14, 2015), http://research.stlouisfed.org/fred2/series/RSNSR. Discount department stores grew at a compound annual rate or 1% between 1992 and 2013, while supercenters and warehouse stores categorized as general merchandise stores grew at 13%. *See* U.S. CENSUS BUREAU, MONTHLY RETAIL TRADE REPORT (2015), http://www.census.gov/retail/index.html (click on the

The methods and metrics for assessing change in the retail sector can be debated and challenged, as can the causes of success and failure for different retailers and different types of retailers. However, a few developments since 1969 are apparent. The original discounters emerged, the category killers followed, e-commerce arrived. Some traditional retailers survived, some discounters survived, and some electronic retailers have performed better than others. Over the years, this has added up to remarkable competitive change at many stages—and the face of retailing today looks quite different than 1969.

In retrospect, Pitofsky's 1977 position could be viewed two ways in light of the evolution of retail markets. These transformations that have seemingly served consumers well have unfolded in an environment unfettered by federal fictitious pricing enforcement. However, the initial emergence and early success of discounters coincided with the height of enforcement, so separating out the effects of non-enforcement proves difficult, if not impossible—especially given other massive economic factors. Nonetheless, the stark changes in the retail industry alone justify a revisit of the FTC's nearly fifty-year old stance.

3. Recent Developments

Though inexpensive technology now offers real-time tools to facilitate consumer price comparison, the impact of this innovation might be overstated. Some consumers shop increasingly with mobile or internet price comparison technology, but many do not.[358] The Internet's promise of price transparency has not been realized. In light of the notion that the Internet has been perceived as the consumer's "best friend," the apparent "explosion of less-than-stellar deals advertised on the

link entitled "Excel (1992-present)" next to the "Retail and Food Services Sales" statement under the "Monthly Retail Trade Report" header to download an Excel spreadsheet of the data from which these numbers were calculated).

358. Survey data tend to vary, but though they show shifts toward technology-driven price shopping, not all consumers claim to shop that way. In 2013, only half of American adults had a smartphone rendering access to in-store comparisons. AARON SMITH, PEW RES. CTR., SMARTPHONE OWNERSHIP 2013 (2013), http://www.pewinternet.org/2013/06/05/smartphone-ownership-2013. According to one 2012 private study, of those visiting mobile retail sites, 19% indicated that "looking up price information" was their "primary task." FORESEE, FORESEE MOBILE SATISFACTION INDEX: RETAIL EDITION 1, 10 (2012), http://www.foresee.com/assets/foresee-mobile-index-retail-edition.pdf. Of course, these data are in flux. As the *Overstock.com* case indicates, the Internet might not enable people to escape deceptive-pricing traps. Also, it remains unclear whether a mobile device would yield useful comparative information to a consumer shopping at an outlet mall, for example.

web . . . is a bit surprising" for some, given the widespread anticipation that it would "liberate [consumers] from price gimmicks."[359]

Though the web and associated mobility tools offer more avenues for price comparison, advertised discount deals still proliferate,[360] and the lowest final price might not always prevail. Even though price comparison technology can lower search costs, time remains scarce, leaving room for suboptimal deals.[361] Not to be forgotten, brick-and-mortar retail continues to adapt quickly.[362] For example, the aforementioned "outlet" or "factory outlet" format for retail clothing distribution has grown at the expense of other formats.[363] Since World War II, the entirety of the retail sector has continuously evolved.[364]

Though making conclusions about the role of fictitious pricing in these contexts may require more study, it is incontrovertible that the changes in retail over the past forty years have been dramatic. These changes in competition might have shifted the optimal amount of enforcement away from none, given that competition has proven quite robust. Because the literature supports the conclusion that fictitious pricing harms welfare, and that discounting has proliferated, this Article contends that at the very least, this justifies experimentation with

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359. Manjoo, *supra* note 28. As author William Poundstone noted, though many predicted, "the Internet was going to usher in a golden age for consumers, where everyone would start comparison-shopping . . . . [B]ut we are all busy, distracted, and we have limited time and attention to devote to research, so we all fall victim to these tricks." *Id.*

360. They proliferate even on transparent Internet sites. For example, Barnes & Noble's website displays David Lat's novel, *Supreme Ambitions*, at a regular or manufacturers' price of $22.95, with a discount of 30% and a price of $16.02. *See Supreme Ambitions: A Novel*, BARNES & NOBLE, http://www.barnesandnoble.com/w/supreme-ambitions-david-lat/1119652044 (as of Dec. 27, 2014). If the Barnes & Noble's discount prevented further searching, Amazon's price of $15.87 (also displayed against a price of $22.95) would be missed. *Supreme Ambitions: A Novel*, AMAZON, http://www.amazon.com/Supreme-Ambitions-David-Lat/dp/1627220461 (as of Dec. 27, 2014). *See* Compeau et al., *supra* note 9, at 291.

361. *See* Manjoo, *supra* note 28.

362. *See supra* Part IV.B.3.

363. In a 2011 snapshot, factory-outlet apparel sales grew at 17.9%, while total industry apparel sales grew at just over 1%. *Consumers Shopping for Value Propel Growth Trends*, NPD GRP. (July 12, 2011), https://www.npd.com/wps/portal/npd/us/news/press-releases/pr_110712. Evidence shows that this channel strategy has proven successful. *See* Yi Qian et al., *Multichannel Spillovers from a Factory Store* (Nat'l Bureau of Econ. Research, Working Paper No. 19176, 2013) (introduction of a factory store channel tends to boost sales across a retailer's channels).

364. *See supra* Part IV.B.1.

enforcement.

C. POTENTIAL ENFORCEMENT ZONES

Fictitious-pricing enforcement should be reintroduced gradually and with an eye toward empirical measurement of impact on pricing and advertising. Evaluating the impact of the actions taken against Michaels Stores and JABC by New York State Attorney General would provide a starting point, for example, to measure whether the targets complied, how their competition reacted, and how pricing and competition changed in comparison to nearby states. Beyond that, certain zones may be ripe candidates for investigating fictitious pricing practices and follow-up enforcement, if required. This Article does not offer an exclusive list of zones for enforcement, nor venues within each zone. However, recognizing the FTC's cost-benefit approach, this Article offers ideas for where the FTC (or state attorneys general) might begin enforcement experimentation.

1. Strong Brands, Credible Discount Channels

Where brands have strong quality credibility, and the selling channel has strong "discount" credibility, consumers may be more prone to expect that they will receive items of high quality while receiving believable advertised discounts. The discounts come with an implicit narrative explaining their existence. Retail discount outlets, for example, offer consumers an implied representation that their stores sell brand items that may have been overstocked or moved from flagship stores, or that the item is offered at a lower price than the flagship store. With outlet-mall pricing, Senator Blumenthal may have selected the right place to plant a pulpit for advocating renewed federal enforcement of fictitious pricing.[365]

An investigation into the pricing practice of retailers who use this fast-growing format might reinforce pricing integrity.[366] Non-outlet retailers offering *genuine* discounts may recover share if consumers pause before using the "outlet model / overstock" representation as a search characteristic and then instore pricing as a compounded search characteristic in that

365. Senator Blumenthal expressed concern that when forming the discount offers, outlet items were not being matched to similar quality items at the flagship stores. Hladky, *supra* note 2. He references a form of deceptive reference point pricing somewhat different from fictitious pricing.

366. This Article concedes that an investigation might clear these retailers of fictitious pricing practices, which would serve a public purpose of building confidence in an "honest" channel.

context. Outlet stores, as noted previously, are a fast growing brick-and-mortar channel, and intervention might make it more likely for consumer searches to stop at the "best offering."[367] Experimental enforcement in this zone would be warranted.

2. Discount-Promotion Zones

Retailers that rely upon discount pricing as part of their brand are also prime candidates for investigation. A retailer that constantly promotes discounts tries to lure buyers to its offerings—and the advertised discounts may stunt the search, especially if the location is physical. The *Overstock.com* case offered an example of a retailer expressly marketing as a discounter online. Retailers that offer, either expressly or implicitly, that they "compare prices so [the consumer] don't have to"[368] should be subject to scrutiny because they are explicitly encouraging consumers to end the search. Perhaps retailers that promote that they will "match or beat any price" are also trying to stunt the search, with the implication that the retailer probably already has the lowest price—or one close enough not to warrant continued consumer search. These representations or practices may not necessarily mislead, but that these retailers are relying heavily on pricing representations warrants scrutiny. Again, this Article suggests regulatory investigation, and if there is subsequent enforcement, measurement of the regulatory impact to see if enforcement has a net social benefit.

In sum, an approach similar to the one reached by the *Overstock.com* court should be applied to situations that fall in these categories. Injunctive relief would be paramount for protecting consumers, and penalties would deter. Because individual harm is difficult to conceptualize, it need not be recovered—the broader social harm should be remediated and prevented. Such actions should only be pursued if the costs prove to outweigh benefits, but such a determination has not been made since enforcement ceased in 1969.

CONCLUSION

Today's retail environment vastly differs from the one that regulators faced in 1969, when the FTC demoted fictitious-pricing enforcement as an agenda priority to a non-concern. In

367. *See supra* Part IV.B.3.

368. People v. Overstock.com, Inc., No. RG10-546833, 2014 WL 657516, at *3 (Cal. Super. Ct. Feb. 5, 2014) (citation omitted).

1969, the core works undergirding behavioral economics had not yet been written, though circumstantial evidence indicates that marketers believed that discounts and fictitious discounts induced sales. Today, regulators have the benefit of dozens of detailed studies into the welfare impact of fictitious pricing. The current marketplace immerses consumers in a competitive retail environment with an entirely new class of retailers and omnipresent discounting.

Given the accumulated knowledge since 1969 about the power of discounting in influencing consumer behavior—and the established consensus that fictitious prior-reference pricing diminishes welfare—it is time to revisit regulatory acquiescence to what has become a commercial tradition. Federal regulators should reexamine enforcement of fictitious pricing. If welfare is enhanced as a product of early enforcement forays, then the FTC should judiciously accelerate enforcement at least until welfare returns diminish.