Simpson Thacher

Memorandum

Price Gouging Considerations in the Wake of COVID-19

April 22, 2020

Historically, complaints regarding price gouging have arisen following hurricanes, tornados or other natural disasters. These disasters usually affect a limited geographic area and lead to local price increases for food, supplies or gasoline at brick-and-mortar retailers. However, the coronavirus disease 2019 ("COVID-19") pandemic has resulted in a wave of price gouging complaints in the context of a worldwide public health emergency. COVID-19 price gouging complaints present new challenges because of the combination of the global reach of internet commerce businesses and the global effects of COVID-19. The goods that have primarily been affected thus far include hand sanitizer, sanitizing wipes and face masks, and everyday grocery items like chicken, rice and milk.

There have been a variety of responses to COVID-19 price gouging, including:

- Federal legislation, investigation and enforcement.
- State investigation and enforcement.
- Industry self-regulation.

Federal Legislation, Investigation and Enforcement

There is currently no federal law that specifically prohibits price gouging. In March and April 2020, at least seven bills seeking to prohibit price gouging were introduced in Congress, including the COVID-19 Price Gouging Prevention Act, Ending Price-Gouging During Emergencies Act, and Disaster and Emergency Pricing Abuse Prevention Act. Previous attempts at passing a federal price gouging statute have failed, with the most recent attempt occurring in the U.S. House of Representatives in 2013. Lawmakers may be more receptive to a federal statute now given the nationwide effects of the COVID-19 crisis and the concern that the patchwork system of state and federal enforcement fails to create consistent and sufficient protection for all Americans.

EXECUTIVE ORDER ON HOARDING AND PRICE GOUGING

Under Section 102 of the Defense Production Act, the U.S. President may prohibit the hoarding of needed resources. Pursuant to that act, President Donald J. Trump signed an Executive Order on March 23, 2020 to address hoarding that threatens the supply of necessary health and medical resources, including the hoarding of products to sell above prevailing market prices.

To implement the Executive Order, the President has delegated to the Secretary of the U.S. Department of Health and Human Services ("HHS") the authority to designate resources as scarce or otherwise vulnerable to hoarding. On March 25, 2020, the Secretary of HHS issued a notice designating 15 categories of health and medical supplies that must not be hoarded or sold for exorbitant prices. These include certain types of personal protective equipment ("PPE"), sanitizing and disinfecting products, drugs with certain active ingredients and ventilators. The Federal Emergency Management Agency ("FEMA") subsequently issued a temporary rule prohibiting the export of five categories of these scarce materials without FEMA's explicit approval: N95 filtering facepiece respirators; other filtering facepiece respirators; elastomeric, air-purifying respirators; PPE surgical masks; and PPE gloves or surgical gloves. The FEMA Administrator may consider potential hoarding or price-gouging concerns when determining whether to return any scarce materials detained by the U.S. Customs and Border Protection for domestic use or to permit the intended export.

The U.S. Department of Justice ("DOJ") will work with HHS to enforce the anti-hoarding provisions of the Executive Order, as it is a crime for a person to hoard the scarce materials designated by HHS or to sell such materials in excess of prevailing market prices. The DOJ will also prioritize the detection, investigation and prosecution of fraudulent activity and price gouging related to scarce materials and will work with FEMA when appropriate. In addition, Attorney General William Barr issued a memorandum creating the COVID-19 Hoarding and Price Gouging Task Force to investigate and prosecute COVID-19-related hoarding and price gouging. The DOJ is also working with state and local law enforcement to investigate and prosecute illegal hoarding and price gouging.

Two Senators have urged the DOJ to vigorously enforce the Executive Order. On April 7, 2020, Senators Amy Klobuchar and Chuck Grassley sent a letter to Attorney General Barr seeking details about the DOJ's efforts to enforce the Executive Order, its plans to investigate and prosecute hoarding and price gouging, and how the DOJ plans to coordinate with HHS, FEMA, other federal agencies, and state and local enforcement authorities.

FEDERAL TRADE COMMISSION ENFORCEMENT

Section 5(a) of the Federal Trade Commission ("FTC") Act prohibits "unfair or deceptive acts or practices in or affecting commerce" and empowers the FTC to investigate and take enforcement action against individuals and businesses engaging in unfair acts or practices. FTC Chairman Joe Simons issued a statement on March 26, 2020 announcing that the FTC is working to protect consumers during the COVID-19 crisis, and will not tolerate companies that deceive consumers, violate well-established consumer protections or take unfair advantage.

On March 27, 2020 several U.S. Senators, including Bernie Sanders and Elizabeth Warren, sent a letter to the FTC urging it to "do everything in its power" to address price gouging. The letter calls on the FTC to use its authority to prevent "unfair or deceptive acts or practices," which the Senators argue should include inflating prices for health products desperately needed by consumers. The letter asserts that the FTC has been reticent to employ the full extent of its authority under Section 5 of the FTC Act under normal circumstances, but should explore the limits of its consumer protection authority under these extraordinary circumstances.

APPLICABILITY OF ANTITRUST LAWS

From a federal antitrust perspective, businesses are generally free to make unilateral decisions regarding the price at which to sell their goods and services.[1] However, critical industry participants will be held to account through state price gouging laws for any material changes in the pricing of their products. Thus, during this emergency period, companies should ensure that their pricing decisions are made independently and take into consideration applicable price gouging restrictions.

State Investigation and Enforcement

Approximately 40 states have laws that prohibit price gouging and the statutes vary from state to state. Many state statutes are triggered by a declaration of emergency from a city or county executive, a governor or the President, although some statutes, as in New York, can be triggered by certain circumstances even in the absence of a formal emergency declaration. In response to the COVID-19 crisis, several state attorneys general, including the California and New York AGs, have announced their intention to take action against price gouging under their respective state laws.

CALIFORNIA

Section 396 of California's Penal Code prohibits charging a price for consumer goods or food that is more than 10% higher than the price of these items immediately before a declaration of a national, state or local emergency. California's statute applies to goods as well as services used for emergency cleanup, emergency supplies, medical supplies, home heating oil, building materials, housing, transportation, freight and gasoline.

Under the law, an exception exists for certain price increases. A price increase is not unlawful if it is directly attributable to additional costs imposed by the supplier of the goods (or due to additional costs for labor or materials used to provide the services) and the price is no more than 10% greater than the total cost to the seller plus the markup customarily applied by the seller for that good or service immediately prior to the declaration.

A violation of Section 396 is a misdemeanor and can result in imprisonment for up to one year and a fine of up to $10,000. A violation of Section 396 also constitutes an unlawful business practice and an act of unfair competition under Section 17200 of the California Business and Professions Code. Violators are subject to civil penalties of up to $2,500 per violation, injunctive relief and mandatory restitution.

California Governor Gavin Newsom declared an official statewide state of emergency on March 4, 2020. Almost immediately, California Attorney General Xavier Becerra issued a price gouging alert to remind all Californians that price gouging is illegal during the declared state of emergency.

[1] For more information on antitrust concerns in the context of COVID-19, *see* Simpson Thacher & Bartlett LLP, *COVID-19 Response Planning: Minding the Antitrust Gap*, Mar. 24, 2020.

On March 27, 2020, Attorney General Becerra issued a statement addressing supply chain price gouging and reminding businesses that California's price gouging statute applies to all sellers, meaning that the law applies equally to transactions between manufacturers, wholesalers, distributors, and retailers as well as to transactions between retailers and consumers.

NEW YORK

New York's price gouging law is codified in Section 396-r of the New York General Business Law. The provisions of that statute can be triggered either by a declaration of a state of emergency by the governor or an "abnormal disruption of the market." On March 7, 2020, New York Governor Andrew Cuomo declared a state of emergency, leaving no doubt that the provisions of New York's price gouging law had been triggered.

New York's statute prohibits the sale of goods and services that are necessary for the health, safety, and welfare of consumers at an "unconscionably excessive" price during any abnormal disruption of the market. An abnormal disruption of the market is any change in the market, whether actual or imminently threatened, resulting from stress of weather, convulsion of nature, power outage, strike, civil disorder, war, military action, national or local emergency, or other causes which result in a state of emergency declaration.

Whether a price is unconscionably excessive is a question of law for the court. The court's determination is based on whether: (i) the amount of the excess in price is unconscionably extreme; (ii) there was an exercise of unfair leverage or unconscionable means; or (iii) a combination of both of these factors.

The New York State Office of the Attorney General ("OAG") is tasked with enforcing New York's price gouging statute. The Attorney General can seek to enjoin or restrain alleged price gouging. Civil penalties are not to exceed $25,000 and, where appropriate, a court may order restitution.

On March 10, 2020, New York Attorney General Letitia James ordered two New York City merchants to cease and desist charging customers excessive prices for hand sanitizers and disinfectant sprays. OAG investigators confirmed that an Ace Hardware in midtown Manhattan was charging customers $79.99 for 40 oz. of hand sanitizer, and City Fresh Market in Astoria, Queens was charging customers $14.99 for a 19 oz. bottle of disinfectant spray. On March 20, 2020, Attorney General James sent a letter to counsel for Craigslist.com, ordering Craigslist to remove posts that allegedly violate New York's price gouging law by attempting to sell, for example, a 40 oz. bottle of Purell for $222.

Industry Self-Regulation

INTERNET COMMERCE BUSINESSES URGED TO TAKE ACTION

The harm created by COVID-19-related price gouging can be particularly far reaching given sellers' access to online retail platforms that enable them to reach much larger numbers of buyers spread across a far broader geographic area. Some of these sellers operate by buying scarce consumer products at brick-and-mortar retail outlets to resell online at substantial price increases.

On March 25, 2020, more than 30 state attorneys general sent letters to a number of large online retailers urging them to crack down on price gouging in real time.[2] The attorneys general argued that it was "especially important" that "unscrupulous sellers do not take advantage of Americans by selling products at unconscionable prices" during the COVID-19 pandemic.

After noting examples of alleged price gouging found on these websites, the attorneys general stated that even though the companies have introduced new protections, they "have failed to remove unconscionably priced critical supplies." The attorneys general then urged these companies to implement a number of measures to prevent price gouging, including by:

- **Setting policies and enforcing restrictions on price gouging.** Rather than addressing price gouging after it has already occurred, companies are urged to prevent unconscionable price increases from occurring in the first place by creating and enforcing strong policies that prevent sellers from deviating in any significant way from prices prior to an emergency. These policies should consider the prices historically set by the seller in question as well as other sellers of the same or similar products.
- **Triggering price gouging protections before emergency declarations.** Noting that price gouging on online retail platforms often begins before an official emergency declaration, a company's price gouging protections should be triggered when their system detects pricing spikes generally (for example, by scarcity caused by a recession or stock market crash), or when conditions exist that could lead to price gouging (for example, pending weather events or future health emergencies).
- **Creating and maintaining a "Fair Pricing" page on their websites.** This feature would allow customers to directly report instances of price gouging. A page should include a request for the vendor's name, the item for sale, the alleged unfair price, and the complainant's state of residence. This is intended to allow companies to quickly identify and freeze or remove bad actors, as well as facilitate appropriate referrals for enforcement or prosecution.

The attorneys general additionally called on these companies to devise and implement other solutions, in addition to the ones discussed above, to protect consumers.

TRADEMARK LITIGATION TO COMBAT PRICE GOUGING

In response to various resellers allegedly engaging in price gouging concerning its N95 respirators, 3M has filed a number of lawsuits alleging federal and state trademark law violations, among other claims. 3M claims that their

[2] This coalition of attorneys general includes those from California, Colorado, Connecticut, Delaware, District of Columbia, Hawaii, Idaho, Illinois, Iowa, Louisiana, Maine, Maryland, Massachusetts, Michigan, Minnesota, Montana, Nebraska, Nevada, New Hampshire, New Jersey, New Mexico, New York, North Dakota, Ohio, Oregon, Pennsylvania, Puerto Rico, Rhode Island, Utah, Virginia, Vermont, Washington and Wyoming.

brand is harmed by the defendants' improper association of its trademarks with price gouging. 3M is the largest producer of N95 respirators in the U.S. and reports that it has not raised its prices in response to the COVID-19 pandemic. In the lawsuits, 3M claims that the defendants misused 3M trademarks to mislead buyers into believing they were authorized distributors of 3M and that 3M had authorized their prices (in some instances, at over 500% above the list price). Some of the affected buyers include the HHS Strategic National Stockpile and New York City procurement officials. 3M is seeking preliminary and permanent injunctive relief and has stated that any penalties, costs or fees recovered will be donated to charitable COVID-19 relief efforts. *3M Co. v. Doe*, No. 20-05549 (N.D. Tex.); *3M Co. v. Geftico, LLC*, No. 6:20-cv-00648 (M.D. Fla.); *3M Co. v. Performance Supply, LLC*, No. 20-cv-02949 (S.D.N.Y.); *3M Co. v. Rx2Live, LLC*, No. 20-cv-00523 (E.D. Cal.).

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