

# Client Alert

November 2015

## With Staggering Outlet Store Growth, Fiercely Savvy Shoppers Aim to Challenge Retailer Advertising at Every Turn

Over the last 18 months, patrons of the nation's most popular outlet stores have hit well-known retailers, including Gap Outlet, Banana Republic Factory Store and Saks Off 5th, with a flood of class action lawsuits for false and misleading advertising. In early 2014, four members of Congress wrote to the Federal Trade Commission ("FTC") asking the agency to begin an investigation into the sales practices at outlet stores.

Meanwhile, class action suits against outlet and discount stores over alleged unlawful pricing practices continued to pour in during 2015, including ongoing cases against Burlington Coat Factory, the TJX Companies, Inc. and Columbia Sportswear Co. Likewise, courts have been issuing some stinging results, including, in Alameda County, a \$6.8 million judgment in a case brought by California district attorneys against online retailer Overstock.com; a New York federal judge's approval of a \$4.87 million settlement to resolve a similar class action suit against Michael Kors Outlet Stores; and, earlier this month, J.C. Penney Corp. Inc. agreed to a \$50 million settlement for plaintiffs in a class action lawsuit that accused the retail chain of false advertising practices.

In the following Q&A, **Phyllis Marcus**, former FTC chief of staff of the Bureau of Consumer Protection's Division of Advertising Practices and counsel in Hunton & Williams' competition practice, and **Wally Martinez**, the firm's managing partner, discuss the latest trends in consumer protection and consumer false advertising and reflect on the legal challenges in the thriving \$25 billion outlet and retail discount market.

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### ***Consumer false advertising class action lawsuits have surged in the past year. What is driving this, and what are some of the triggers for these suits?***

**PM:** It is true that there has been a huge wave of retail sales pricing class action lawsuits. The allegations involve the potential fabrication of inflated prices in order to compare to the actual price. The plaintiff's claims are relatively simple: "I went into this store; I bought this item. The store represented to me that the item had previously been sold or was available on the open market at a particular price. I relied on that differential between the high price and the price I was paying to make my purchasing decision. Therefore, I have been injured in some way."

Outlet malls are a huge growth sector in the apparel and consumer item industry. As far back as 2011, these stores saw about a 17 percent increase in apparel sales, whereas overall apparel sales for that same period increased by only 1.45 percent — massive growth in an overall slower market.

The overwhelming rise in popularity of discount merchandise makes this sector an obvious target. The injury is hard to wrap your head around — it's a bursting of the bubble of adrenalin a shopper gets when he thinks he has saved money. A lot of very sophisticated shoppers feel this way.

Determining the nature of the injury is tricky. The consumer gets the item, can touch and feel and assess its quality, and does know the price he or she paid for the item. But, the consumers have been able to survive class dismissals based on an injury of potential savings and they have been backed by California law, and by the FTC's guides against deceptive pricing. Those guides remain on the books, although they don't appear to be actively enforced by the FTC.

### ***How has the FTC been engaged?***

**PM:** The FTC's recent guidance focuses on how to be a more savvy consumer and how to make sure you are getting the benefit of your own bargain when you go to an outlet store, as featured in an [FTC blog post](#) by the agency's consumer education team.

What may have driven this particular category of class actions is a set of letters written by members of Congress to the Federal Trade Commission last year expressing concern over outlet store pricing policies, and warning that consumers may be deceived by the quality of items they purchase from these stores.

While originally outlets were formed to sell off retailers' damaged merchandise or excess merchandise, now goods are created specifically for the outlet market. The FTC's guidance explains that the quality of goods consumers get at outlets might be less-refined. There might be differences in a designers' high-end apparel line and the line that shows at an outlet. Consumers can make educated decisions whether or not to buy particular items by examining them. If it is important to the consumer to have an item of fashion from a designer with the understanding that this is the designer's secondary line, then the price is what the price is.

One of the key pieces of advice that the FTC has given is that once you recognize that you are buying something that looks new and undamaged, recognize that the price may be lower for a reason: the quality of the goods may be less, the stitching may be less elaborate and the fabric itself may be lighter weight. The FTC says consumers should also ask whether the merchandiser sells things that are made for outlet only, whether there are multiple lines of the designer's product, or whether the merchandise that is available in the outlet came originally from a retail store and then was brought as overstock or was damaged. That latter scenario is the old way, but that is not the new way.

### ***How are the courts reacting?***

**PM:** Whereas the FTC hasn't been active on the law enforcement front, class action lawyers and California district attorneys have jumped into the fray, alleging violations of California consumer laws. The suits have been brought in various federal courts and in California state courts, where the law is very favorable to consumers.

**WM:** These class actions present some serious obstacles for the retailers to overcome: fighting against class certification and fighting against damages claims. Hunton & Williams has tremendous depth not only in false advertising and class actions, but also in the successful defense of the spectrum of retailers, manufacturers, technology companies, major building products and appliance companies, among others, in cases involving product defects, trademark infringement, personal injury, antitrust, unfair competition and deceptive trade practices. Some of these class actions have involved staggeringly high numbers of plaintiffs. In the case of a major appliance company, the lawsuit involved more than 50 million products with millions of potential class members against our client, for whom we managed to strike almost the entire damages claim.

### ***How are the retailers reacting?***

**PM:** I think the retailers are scared, because these suits are not going away so fast. There are some

obvious things that retailers can do to avoid being targets, the most obvious of which is to avoid price comparisons if selling in an outlet environment.

The Overstock.com ruling sent shockwaves through the industry. I think people were very surprised. Whereas previously you might have been able to poll people who would have said the suits would not have traction, now people are starting to get worried. It is not clear whether pricing strategies have changed, but these suits seem to be coming fast and furiously without abatement, and are being validated by judges.

**WM:** Retailers and those in the burgeoning outlet and discount market must be concerned about these recent class actions because these cases have spiked in just the past two years, and while California district attorneys are predominantly the ones alleging violations of California consumer law, we are going to begin seeing more cases in jurisdictions across the country. In fact, an important piece of advice for our clients — anywhere — would be that they be very aware not just of what FTC pricing guidelines say, but also of what the pricing guidelines are in their own jurisdictions. Hunton & Williams is intimately familiar with the class action and judicial landscapes throughout the US, whereby we can foresee the challenges, particularly in consumer protection and class actions, within certain jurisdictions — a unique skill set that has come from decades of defending retailers and manufacturers in national class action cases.

***What are some of the recommendations for retail clients, particularly outlet and discount sellers?***

**PM:** Our retail clients should be considering how to minimize the risk, such as avoiding the price comparisons altogether on labels. The Overstock.com suit involved a detailed look at the algorithms the company used to determine its “compare at” prices. It’s best not to indicate that there was a retail price if the item has not been sold at retail. Just offer the price. Use labels that indicate that the goods are being sold at the outlet store, and not just the generic brand. Sell goods at outlet that are also sold at ordinary stores so that if you are going to advertise a price comparison, it is an accurate price comparison.

**WM:** In terms of defending against a class action lawsuit, our clients should know that we have represented, defended and advised hundreds of clients in important, high-profile class action cases. Beyond the cases themselves, Hunton & Williams provides ongoing counseling for retail and compliance obligations set forth in FTC rules and guides, including the Energy Labeling Rule, the Green Guides, Dot Com Disclosure guidelines, Made in the USA Standard, and the Endorsements and Testimonials guidelines. We counsel clients on marketing practices for promotions, sweepstakes, loyalty programs, gift cards, rebates and social media, which is becoming a very complex platform for advertising. We have spent years representing and advising companies that have faced federal investigations and regulatory charges, and, in doing so, we’ve maintained close ties with these clients, who continue to seek from our lawyers regular counseling and guidance in a fluctuating and volatile retail and consumer marketplace.

**PM:** Most importantly, I encourage our clients to seek advertising advice from our team. We’ve got a deep bench of consumer protection attorneys here, who can help our clients figure out pricing and sales strategies to assist with these lawsuits.

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