Legal Opinion Letter

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STATE HIGH COURT CAN REIN IN CALIFORNIA'S "LITTLE FTC ACT"

by
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California's "Little FTC Act" has become a staple of practically all consumer class action cases brought in California. Although every state has enacted its version of the Federal Trade Commission Act, few have done with theirs what California has done with its law, set forth in Business & Professions Code §17200. The California Supreme Court appears poised to decide three cases next year that could alter three important aspects of that law. This LEGAL OPINION LETTER reviews those three aspects and the four key cases that have addressed or will address them.

The Law's Troubling Features. The first feature is unique to California. It allows a named plaintiff to recover money on behalf of nonparties without having to bring the case as a true class action. This is the "non-class class," a feature of §17200 that prompted a member of the California Supreme Court to recently refer to §17200 as an "unbridled" statute, a "growth industry," and a "standardless, limitless attorney fee machine."

The second feature is the statute's prohibition against "unfair" business practices. While the federal FTC Act and most state "Little FTC Acts" also prohibit "unfair" practices, the difference is that California's prohibition is essentially undefined. As a result, it exposes California businesses to a regulatory regime of after-the-fact decision-making by a court.

The third feature concerns the remedy. Unlike some other states' "Little FTC Acts," Section 17200 does not allow recovery of damages, only restitution. But the courts have eroded the meaning of "restitution" to the point where it is indistinguishable from damages.

Stop Youth Addiction v. Lucky Stores. The first case, *Stop Youth Addiction v. Lucky Stores, Inc.*, 17 Cal.4th 553 (1998) has already been decided. The suit was a Frankenstein of section 17200's creation. A lawyer founded a corporation whose only shareholder was his mother and whose only business was filing lawsuits. It set up a private "sting" operation, hiring underage youths to buy cigarettes from retailers, mostly "mom and pop" grocery stores. The lawyer would threaten to file a section 17200 suit unless the retailer paid money to his mother's organization. He asked for $10 billion in restitution to be paid to the State.

The issue was whether an unelected private lawyer can sue civilly under §17200 to vindicate a criminal statute. The state Supreme Court said yes. Thus, *Stop Youth Addiction* stands for the privatization of the criminal laws. Section 17200 can now be used to "piggyback" a criminal law violation into a civil claim.

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Kraus v. Trinity Management. *Kraus v. Trinity Management*, 57 Cal. App. 4th 709 (Cal. Ct. App. 1997), addresses the validity of one of the most curious aspects of §17200: the "non-class class." In *Kraus*, six former tenants claimed that their landlord had charged them illegal security deposits. They sought return of the fees for themselves and 4,500 other former tenants but did not bring a class action. The court found for plaintiffs, enjoined the landlord from continuing to take security deposits, and awarded almost $1 million in restitution. The court ordered the money paid into a trust fund whose purpose was to finance future litigation against other landlords.

The problems of the "non-class class" are numerous. If the landlord had won, no one but the six tenants who sued would be bound. As it was, the landlord lost, yet its $1 million payment into the trust fund would not preclude the 4,500 other tenants from suing and recovering their fees. That is a classic "no-win" situation for defendants.

Cortez v. Purolator. The third case to be decided next year is *Cortez v. Purolator Air Filter Products, Inc.*, 64 Cal. App. 4th 1437 (Cal. Ct. App. 1997). There, the court of appeal allowed a "non-class" class of 175 former employees of the defendant to proceed, awarding them back wages, denominated "restitution," even though back wages are "damages" which are not recoverable under § 17200. It also allowed the "class" claims to reach back four years — the § 17200 statute of limitations, though the Labor Code prescribes just a one-year statute of limitations.

Cel-Tech Communications v. Los Angeles Cellular. The fourth section 17200 case that will be decided next year is *Cel-Tech Communications v. Los Angeles Cellular*, 59 Cal. App. 4th 436 (Cal. Ct. App. 1997), an antitrust case brought by a seller of cellular telephones against a company that provides phone service. The provider won at trial, but on appeal, the court of appeal said that even though the defendant broke no law and was exonerated on the antitrust claims, this can still violate section 17200's "unfairness" prong.

"Unfairness" is the great undefined term in the statute. All that has to be shown to prove a violation of § 17200's prohibition against "unfair acts" is that the harm to the victim outweighs the benefits to the defendant. This standard unfortunately results in regulation by hindsight. It leaves California businesses with little more guidance in terms of compliance than trying to guess whether a certain practice might offend some future unknown judge's sensibilities.

Conclusion. Historically, the California Supreme Court hears a section 17200 case perhaps once every five years. Next year, it will hear three. If *Kraus* and *Cel-Tech* are reversed, it would put California's Little FTC Act on roughly the same footing as the Little FTC Acts in most other states. Section 17200 would remain an important cause of action asserted in most typical consumer class action cases, but it would no longer be the turbo-charged engine it now is. On the other hand, if these cases are affirmed, one would have ask why anyone would bother bringing a true consumer class action in California any longer.

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