

How \$10 Billion Disappeared: *Price v. Philip Morris* and How the FTC Specifically Authorizes Cigarette Companies to Advertise in Illinois

Tim Cox

Student Fellow, Institute for Consumer Antitrust Studies
Loyola University Chicago School of Law

Introduction

The states and the federal government have been dealing with tobacco lawsuits for decades.¹ Moreover, the Federal Trade Commission (“FTC”) has significantly monitored, reported on, and regulated the tobacco industry since 1964.² While many of the early civil tobacco lawsuits related to health injuries, including cancer and sometimes death, more recent cases focus on deceptive advertising or similar state law claims. These claims rely on studies indicating that “light” and “low-tar” cigarettes are no less toxic, and in some cases may be more toxic, than their “full-flavored” counterparts. Moreover, a steadily rising level of evidence suggests that the tobacco companies had knowledge of this toxicity, but nonetheless continued advertising with the “light” and “low tar” terms. The plaintiffs in the Illinois class action case of *Price v. Philip Morris* (“*Price*”) sought to recover compensatory damages for this type of advertising under Illinois’ consumer protection statutes, but the Illinois Supreme Court remanded with instructions to dismiss the suit based on section 10b(1) of the Illinois Consumer Fraud Act (“CFA”).

The Illinois Consumer Fraud Act Purpose and FTC Rulemaking

Illinois enacted the CFA in part to protect consumers against fraud, unfair methods of advertising, and deceptive practices in trade.³ However, section 10b(1) of the CFA states that “[n]othing in this act shall apply to...[a]ctions or transactions *specifically authorized* by laws administered by any regulatory body or officer acting under statutory authority of this State or the United States.”⁴ Section 10b(1) therefore gives deference to federal and state regulatory authority by acknowledging that companies must be able to rely on the rules those authorities promote. In *Lanier v. Associates Financing, Inc.* and

¹ See generally Robert L. Rabin, *A Sociolegal History of the Tobacco Tort Litigation*, 44 STAN. L. REV. 853 (1992) (noting that the first lawsuit of *Lowe v. R.J. Reynolds Tobacco Co.*, although it was subsequently dropped, was filed in 1954 shortly after two public announcements, one by Readers Digest and the other on a popular television show, were released discussing the hazards of smoking, and thus the long-standing policy of tobacco companies proceeding to trial in lieu of settling began).

² The FTC decided at this time that the tobacco companies had a duty to inform the public of the health hazards of tobacco products and found that current advertising was deceptive after a scientific report plainly stated that cigarette smoking was a health hazard. These findings resulted in a trade regulation act requiring disclosure of the health dangers by the FTC that was ultimately preempted by the 1965 Federal Cigarette Labeling and Advertising Act.

³ *Price v. Philip Morris*, No. 96326, 2005 WL 3434368, at *28 (Ill. Dec. 15, 2005)(citing *Robinson v. Toyota Motor Credit Corp.*, 775 N.E.2d 951 (Ill. 2002)).

⁴ 815 ILL. COMP. STAT. 505/10b(1) (West 2005)(emphasis added).

Jackson v. South Holland, for example, the Illinois Supreme Court held that 10b(1) barred lawsuits seeking to require additional disclosures that exceeded the existing Truth in Lending disclosure requirements.⁵

The FTC, in addition to formal rulemaking and other methods of regulating the tobacco industry, at times enters into consent orders with individual tobacco companies.⁶ The FTC issued two of these consent orders discussing terms like “low” and “low-tar.” A 1971 consent order issued to American Brands provided that terms like “low” could be used in advertising as long as the package also disclosed the actual amount of tar and nicotine as measured in milligrams, and a 1995 consent order issued to American Tobacco Company provided that comparing tar and nicotine levels of competing cigarettes, with or without using terms like “low,” shall not violate a previous ban on numerical comparisons.⁷

Tobacco Loses in Round One

Plaintiffs filed the class action lawsuit in 2000 asserting violations of Illinois’ Consumer Fraud Act and Deceptive Practices Act.⁸ The certified class included all consumers who purchased either Marlboro Lights or Cambridge Lights since the inception of those brands into the tobacco market.⁹ The plaintiffs’ suit alleged that Philip Morris (“PMUSA”) designed both Marlboro Lights and Cambridge Lights to test low on the FTC’s tar and nicotine testing machine, even though it had knowledge that the testing was inaccurate and the cigarettes were actually more harmful than normal cigarettes. The *Price* plaintiffs claimed that they relied on the “fraudulent, deceptive, and unfair” assertions of “light” and “low-tar” by PMUSA in purchasing cigarettes over several decades. This resulted, the plaintiffs alleged, in deceived consumers who purchased these brands based on the contention that the cigarettes were less dangerous.¹⁰ Therefore, the plaintiffs sought compensatory damages for cigarette purchases over those respective time frames.¹¹

⁵ See generally *Lanier v. Associates Financing, Inc.*, 499 N.E.2d 440 (1986); *Jackson v. South Holland*, 755 N.E.2d 462 (2001).

⁶ *Price*, 2005 WL 3434368, at *40 (finding that consent orders to individual tobacco companies is one method of rulemaking the FTC employs).

⁷ *Id.* (stating the numerical comparison ban was in response to Carlton cigarette advertising showing multiple packs of Carlton cigarettes next to one pack of a competitor and claiming that Carlton’s had less tar/nicotine. The ban allowed actual comparison of the FTC milligram measurements).

⁸ *Id.* at *17.

⁹ *Id.* (noting that the class certification and therefore the economic damages dated to the inception of each brand of cigarettes in the claim: Marlboro Lights introduced 1971 and Cambridge Lights introduced in 1986).

¹⁰ See *id.* at *15-6 (listing several of the allegations in the second amended complaint).

¹¹ *Id.* (noting the actual damage calculation was based on an internet survey from that questioned 2,701 persons whose demographics consisted of being current or recent smokers, smoked in the last year, smoked Marlboro Lights, Cambridge Lights, or other light cigarettes. After a series of questions, an expert determined that consumers would demand a 92% discount off the price of the cigarettes. Taking this discount factor for all relevant purchases of cigarettes, the plaintiffs calculated the damages at \$7.1b after a five percent interest rate).

PMUSA answered plaintiffs' allegations with several affirmative defenses, including the statutory exemption contained in section 10b(1) of the CFA.¹² It argued that the 1971 and 1995 consent decrees provided it with the necessary regulatory authority to use the "light" and "low tar" terms. By complying with those consent decrees, PMUSA argued, the CFA statutory exemption applied. The circuit court, finding no affirmative defenses plausible and that the plaintiffs had proven violation of the CFA, entered a judgment against PMUSA for \$10.1b.¹³ In the judgment order, the circuit court held that use of the disputed terms was never "specifically authorized by law." However, the Court did not explicitly refer to the exemption in section 10b(1) of the Consumer Fraud Act. The case was appealed directly to the Supreme Court of Illinois.¹⁴

Illinois Supreme Court Broadly Defines Specifically Authorized Exemption

The Illinois Supreme Court first set out the CFA 10b(1) exemption's two necessary components: the regulatory agency must operate under statutory authority and the laws administered by the agency must specifically authorize the conduct in question.¹⁵ The court then dismissed PMUSA's contention that merely complying with tobacco regulation would trigger this exemption.¹⁶ Rather, the regulatory body must have affirmatively acted or specifically authorized the use of the terms "low tar" and "light". The court distinguished the previous Illinois cases of *Lanier* and *Jackson* noting that the *Price* plaintiffs were not alleging lack of disclosure; they were alleging fraud.¹⁷ Consequently, the appropriate question was whether the actions of the FTC specifically authorized the use of "lights" and "low-tar" on cigarette packages via its rulemaking, not merely whether PMUSA complied with current FTC regulations.¹⁸

The court concluded that neither formal rulemaking nor express statements were required to trigger the 10b(1) exemption, but rather staff interpretations or implied authorization could activate it. Pursuant to FTC internal documents and expert testimony by a PMUSA witness, the court found that agreeing to consent orders with individual tobacco companies was one way in which the FTC regulated the tobacco industry; that is, the FTC expected other tobacco companies to comply with the statements set out in individual consent orders. The Court then reviewed the two consent orders promulgated by the FTC to American Brands in 1971 and American Tobacco Company in 1995.¹⁹

¹² *Price*, 2005 WL 3434368, at *15 (stating PMUSA answered with twenty-seven affirmative defenses "including laches, waiver, the statute of limitations, federal preemption, and the statutory exemption contained in section 10b(1) of the Consumer Fraud Act" and that PMUSA filed a motion to decertify the class based on the argument that deception was an individual question rather than a broad class question).

¹³ *Id.* at *27 (noting that the damages consisted of \$7b compensatory and \$3b in punitive).

¹⁴ *Id.* at *1 (the Supreme Court of Illinois itself specifically ordered that the case be appealed directly to it under Supreme Court Rule 302(b)).

¹⁵ *Id.* at *32.

¹⁶ *Id.* at *32 (finding also that conduct is not specifically authorized merely because conduct is not prohibited or was passively allowed in the past).

¹⁷ *Id.* at *36 (accepting the fraud allegation in this case to be analogous to a hypothetical case where a cigarette company promised a pack of twenty cigarettes but only delivered nineteen).

¹⁸ *Price*, 2005 WL 3434368, at *37.

¹⁹ *Id.* at *38.

FTC Consent Orders Bar Cause of Action

The court accepted PMUSA's argument that the two consent orders constituted specific authorization from the FTC to use the terms "light" and "low tar" on cigarette packages and found that no evidence existed that PMUSA used those terms inconsistently with the consent orders. Therefore, the Court held that section 10b(1) of the Illinois Consumer Fraud Act prohibited suit because a United States regulatory agency had specifically authorized the use of those terms. In adding credence to this holding, the court discussed without relying on the Court of Appeals for the Seventh Circuit's decision in *Bober v. Glaxo Wellcome PLC*, 246 F.3d 934 (2001), where the court found the 10b(1) exemption applicable in a pharmaceutical consumer fraud case. The court quoted the Seventh Circuit's language that "specifically authorized...encompass[es] the making of statements that fall within the boundaries established by federal law in a highly regulated industry." In short order, the Court then held that the fact that section 10b(1) barred suit under the Consumer Fraud Act, the alleged Deceptive Practices Act violation was also barred, since that statute had a similar exemption clause.²⁰

Lastly, the court noted that even if the FTC had specifically authorized the use of the terms "light" and "low tar," an additional question remained: whether the fact that the cigarettes were more toxic, or mutagenic, would violate the Consumer Fraud Act by deceiving the public. The court answered in the negative, noting that the claim of toxicity is inherently linked with the base claim of deception and therefore barred by the finding that PMUSA was specifically authorized to use those terms.²¹

Although not part of the official holding, the Court made two significant additional declarations about issues related to the case. First, it questioned the class certification, stating that the circuit court may have misapplied the required cause-in-fact requirement of Consumer Fraud cases. Specifically, the Court was adamant that the cause element must be "but for" causation not, as the circuit court stated, "one of the proximate causes." The question therefore is whether the purchases would have occurred absent PMUSA's conduct. Second, the Court stated that it had "grave reservations" about the calculation of damages that the circuit court relied upon.²² Both of these statements give future plaintiffs something to consider.

Correct Interpretation?

This important Illinois case likely bars not only future tobacco Consumer Fraud claims that rely upon the words "light" or "low tar," but also makes other Consumer Fraud cases in a highly regulated industry unlikely to be successful. In finding that formal rulemaking was not required to constitute specific authorization, as well as approving the Seventh Circuit's language, the Court gave wide latitude to the term "specifically authorize." This ruling will severely impact consumer protection litigation.

²⁰ *Id.* at *41-3, 49-50.

²¹ *Id.* at *45-6.

²² *Id.* at *47-8.

In creating wide application for the exemption, it is highly unlikely that any highly regulated industry could be subject to an Illinois CFA lawsuit, thus limiting the efficacy of the consumer protection statutes.²³

The Court also clarified the causation element of class actions suits, indicating that the Illinois Supreme Court may have more stringent requirements before a class can be certified. Finally, the Court noted the highly speculative method of damage calculation applied by the circuit court, signifying that future plaintiffs will need a more detailed analysis of actual damages—likely leading to a lower damage amount.

²³ *See also* Law Professor Letter in *Price v. Philip Morris*, available at http://www.luc.edu/law/academics/special/center/antitrust/price_vs_philip_morris.pdf (urging the Illinois Supreme Court to request the FTC's views of the consent orders and noting that holding FTC consent orders sufficient in triggering exemptions could have detrimental implications on a variety of states' consumer protection statutes).