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Federal Trade Commission Consent Order Does Not Preempt New York Lemon Law

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Recent Cases

FEDERAL TRADE COMMISSION CONSENT ORDER DOES NOT PREEMPT NEW YORK LEMON LAW

In *General Motors Corporation v. Robert Abrams, Attorney General of the State of New York,* 897 F.2d 34 (2d Cir. 1990), the United States Court of Appeals for the Second Circuit held that a consent order between General Motors Corporation ("GM") and the Federal Trade Commission ("FTC") that provided for arbitration of warranty disputes did not insulate GM from the additional requirements of the New York New Car Lemon Law ("Lemon Law"). N.Y. Gen. Bus. Law § 198-a. The court held that a consent order, like any other federal law, has the authority to preempt state laws if the federal agency intended the consent order to bar state regulation in that particular area. The court concluded, however, that because the FTC did not intend its Consent Order with GM to bar additional state regulation in the area of automobile warranties and related arbitration procedures, the Order did not preempt the Lemon Law requirements.

Background

In 1980, the FTC issued a complaint against GM for failing to notify its customers that certain GM cars and light trucks had defective engines and transmissions. The FTC entered a Consent Order with GM in 1983 after extensive negotiations and public comment. The Consent Order required GM to implement a nationwide arbitration program, administered by the Better Business Bureau, for customers who believed they had purchased defective automobiles. The program was voluntary for the customer and the arbitrator's decision bound only GM. Thus, the consumer could choose between arbitration and going directly to court without arbitration. If the consumer chose arbitration and was unhappy with the results, the consumer still could bring the case to court. On the other hand, if GM was unhappy with the arbitrator's decision, it was bound by the result. The Consent Order also required that the arbitrators be untrained in arbitration procedures, be drawn from all segments of the community, and base their decisions on common sense assesssments of what is fair and equitable given the facts of the case. However, the arbitrator's decision could never contradict state law.

In 1983, the New York legislature enacted the Lemon Law. The Lemon Law required automobile manufacturers to repair items covered by express warranties, free of charge, for a period of two years or 18,000 miles. If the new car was not repaired after four attempts or if the car was out for service for a cumulative total of thirty or more days, it was considered a "lemon" and the owner was entitled to a full refund or a replacement vehicle. However, if the manufacturer had an arbitration program, the consumer was required to participate in that program in order to qualify for Lemon Law protection. In 1986, the Lemon Law was amended to require that arbitrators be trained in arbitration procedures, be familiar with the Lemon Law provisions, and that the arbitrators apply Lemon Law standards and remedies when arbitrating under the manufacturer's program. The amendment also created an alternative arbitration program administered by the New York Attorney General and staffed with professional arbitrators. The arbitrators in this alternative program were to apply the Lemon Law standards and remedies.

GM sued the New York Attorney General in the United States District Court for the Southern District of New York, seeking a declaratory judgment that certain provisions of the Lemon Law were preempted by the GM-FTC Consent Order. GM contended that the FTC would not have negotiated a detailed settlement after taking public comment if the FTC had intended to permit additional state regulation. GM also argued that it was impossible to comply with both the Consent Order and the Lemon Law, and that the state Lemon Law frustrated the FTC's efforts to create a uniform nationwide arbitration program for GM's customers. Therefore, GM contended, the Consent Order preempted New York's Lemon Law.

The New York Attorney General countered that only a federal agency's regulations and not its settlement agreements should preempt state law because settlements did not have the administrative safeguards of regulations. Alternatively, even if a consent order could preempt state law, the FTC did not intend that the Consent Order preempt the New York Lemon Law.

The district court granted GM's motion for summary judgment and held that the GM-FTC Consent Order preempted the Lemon Law. The New York Attorney General appealed to the United States Court of Appeals for the Second Circuit.

Federal Consent Orders May Preempt State Laws

Whether a federal agency's consent order had the preemptive authority of other federal laws was an issue of first impression for the Second Circuit. Under the Supremacy Clause of the U. S. Constitution, federal laws preempt state laws where the two are in conflict. U.S. Const. art. VI, cl. 2. The United States Supreme Court held in *Louisiana Public Service Commission v. F.C.C.,* 476 U.S. 355, 369 (1986), that federal agencies acting within the scope of their congressionally-delegated authority may preempt state laws. Federal courts will uphold agency action intended to preempt state law if the agency was acting reasonably and within its congressionally delegated authority.

The court held that the FTC had the congressional authority to settle cases through consent orders. The court further held that the FTC-GM Consent Order was reasonable both because it avoided risky and expensive litigation and because it resulted from extensive negotiations and public comment. The court concluded that such a consent order may preempt state laws. However, the court noted that although a consent order may preempt state law, it will do so only if the consent order was intended to bar state regulation.

Intent to Preempt

The court next turned to the issue of whether the FTC intended its Consent Order with GM to preempt additional state regulation in this area. Absent an express intent to preempt state regulation, intent may be implied in two ways: (1) if federal regulation of a particular field is so comprehensive that it is reasonable to infer that the federal authority intended to exclude state regulation; and (2) if a conflict exists between the federal and state laws such that it is impossible to comply with both laws, or if complying with the state law frustrates the objectives of the federal law.

The court rejected GM's argument that the Consent Order was so comprehensive that the FTC intended to occupy the field of GM's warranty disputes to the exclusion of state regulations. The court stated that because states traditionally have regulated consumer protection, GM had to show compelling evidence that the FTC intended to preempt state regulation. The FTC-GM Consent Order alone did not show a clear purpose to exclude state regulation of automobile warranties. The Consent Order itself contained references to state law. Also, if GM was not bound by state law, it would have an unfair advantage over its competitors, who would have to follow the state law. The court concluded that the FTC Consent Order should not insulate GM from the New York Lemon Law.

Voluntary Participation in Arbitration

The court next considered GM's argument that the Consent Order and the Lemon Law conflicted. GM argued that, unless the Consent Order preempted the Lemon Law, the Lemon Law provision requiring participation in the manufacturer's arbitration program prior to court action would eliminate the voluntary arbitration created by the Consent Order. The court interpreted the Lemon Law differently. Rather than requiring that the consumer arbitrate, the Lemon Law restricted Lemon Law suits to those consumers who first had attempted to arbitrate the dispute. Consumers could bypass arbitration, but they could only sue on a cause of action other than the Lemon Law. Thus, the court concluded that the Lemon Law's exhaustion requirement did not conflict with the voluntary aspect of the Consent Order arbitration.

Other State and Federal Requirements Not In Conflict

GM contended that a conflict existed in that whereas the Consent Order directed arbitrators to decide cases according to a common sense assessment of what was fair and equitable, the Lemon Law required arbitrators to apply the specific standards and remedies of the Lemon Law. The court recognized that an arbitrator using a "fair and equitable" standard might not decide a case the same way as an arbitrator applying the Lemon Law standards. The court concluded, however, that the possible difference in results did not make the two laws incompatible. Moreover, the Lemon Law's specific standards and remedies applied only to cars that were considered "lemons." Where a vehicle did not meet the statuary definition of "lemon," an arbitrator was free to apply the "fair and equitable standard" under both the Lemon Law and the Consent Order. Therefore, the Lemon Law standards did not conflict with the Consent Order standards.

The court also rejected GM's argument that the New York law's requirement of trained arbitrators familiar with the Lemon Law made the two laws incompatible. The court reasoned that the Consent Order directed that the arbitrators be non-professional arbitrators. Nothing in the Lemon Law required professional arbitrators.

Finally, GM argued that the Lemon Law was preempted because it disrupted the goal of the Consent Order to provide nationwide uniformity. The court held that although the Consent Order was intended to create a nationwide system of arbitration between GM and its disgruntled customers, the Order did not require national uniformity. Nor was national uniformity necessary to achieve the goals of the Consent Order. For all these reasons, the court held that

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the Consent Order did not preempt New York's Lemon Law.

Dissenting Opinion

The dissent noted that under the Lemon Law the consumer was required to participate in the manufacturer's arbitration procedure, if any existed. Thus, the Lemon Law conflicted with the Consent Order because the Lemon Law made mandatory the arbitration established as voluntary under the Order. Moreover, according to the dissent, the Better Business Bureau not only trained its arbitrators to reach a common sense decision, but also specifically directed them not to apply the substantive law of any particular jurisdiction. Because New York's Lemon Law required arbitrators to apply Lemon Law standards, it was in conflict with the FTC-GM Consent Order. The dissent concluded that this conflict required a holding that the Order preempted the Lemon Law.

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HEALTH CARE INDUSTRY'S COMPARATIVE ADVERTISING CAMPAIGN NOT ENTITLED TO HEIGHTENED CONSTITUTIONAL PROTECTION

In ***U.S. Healthcare v. Blue Cross-Blue Shield of Greater Philadelphia***, 898 F. 2d 914 (3d Cir. 1990), the United States Court of Appeals for the Third Circuit held that allegedly defamatory, scare-tactic, multimedia health care advertising was commercial speech and therefore was not entitled to heightened protection under the first amendment to the United States Constitution. Moreover, although both parties had invited controversy and had the means to respond to the other's advertising, neither was considered a "public figure" and therefore the advertising did not warrant heightened constitutional protection.

Background: A Comparative Advertising War

For many years, Blue Cross of Greater Philadelphia and Pennsylvania's Blue Shield ("Blue Cross-Blue Shield") dominated the health insurance industry in southeastern Pennsylvania; the company offered "traditional" medical insurance coverage that allowed the consumer to choose among hospitals and physicians. A competitor, U.S. Healthcare, offered as an alternative a health maintenance organization ("HMO"), both as an insurer and as a direct provider of medical services. An HMO offers more comprehensive services than traditional insurance, but a primary health care provider must determine when treatment is necessary and from whom it may be obtained. In just over ten years, U.S. Healthcare grew to 600,000 members; Blue Cross-Blue Shield membership dropped by over 1% each year. A majority of those leaving Blue Cross-Blue Shield opted for U.S. Healthcare.

Faced with this loss of enrollment, Blue Cross-Blue Shield engaged in an aggressive, $2.175 million multi-media advertising campaign. In print, radio, television, and direct mail advertisements, Blue Cross-Blue Shield touted its Personal Choice program and attempted to make less attractive the HMO option. For example, several printed advertisements emphasized that a Personal Choice patient may see a specialist upon demand, but that an HMO physician has a disincentive to make such referrals because "it could take money directly out of his pocket."

Most of the Blue Cross-Blue Shield advertisements contrasted the features of Personal Choice and the HMO plan and emphasized that HMO patients had fewer choices with regard to physicians and hospitals. The majority of the advertisements were innocuous. One television spot, however, seemed to suggest that HMO membership was an invitation to disaster. The advertisement depicted a grief-stricken woman stating, "The hospital my HMO sent me to just wasn't enough. It's my fault."

U.S. Healthcare responded quickly by instituting its own aggressive $1.25 million multi-media advertisement campaign. The advertisements took aim at the Blue Cross-Blue Shield message that HMOs sacrificed quality care for greater profits and highlighted the fact that Personal Choice doctors had fewer admitting privileges than HMO doctors. Two of the printed advertisements contained the following headlines, emphasizing that fewer hospitals were available to Personal Choice subscribers: "When It Comes To Being Admitted To A Hospital, There's Something Personal Choice May Not Be Willing To Admit" and "If You Really Look Into 'Personal Choice,' You Might Have A Better Name For It." One of the television commercials played funeral music while showing a patient's anguished family members standing around a hospital bed. While a voice discussed Personal Choice's various shortcomings, a pair of hands pulled a sheet up over a Personal Choice brochure resting on the pillow of the hospital bed. U.S. Healthcare called the advertisement "Critical Condition."

Within a week after Blue Cross-Blue Shield initiated its advertising campaign, U.S. Healthcare filed in a Pennsylvania state court a lawsuit for commercial disparagement, defamation and tortious interference with contractual relations. At a later date, U.S. Healthcare re-filed its state claims in the United States District Court for the Eastern District of Pennsylvania. In the district court, the health care organization added a claim under section 43 (a) of the Lanham Act, 15 U.S.C. § 1125 (a) (1982), which creates a cause of action for any false or misleading representations of a product. Blue Cross-Blue Shield filed a counterclaim on essentially the same theories of liability stated in U.S. Healthcare's complaint.

After a fourteen day trial, the jury was deadlocked on all issues of liability and damages. The judge declared a mistrial and, before