Unfair Competition and Consumer Fraud Statutes:
Recipe for Consumer Fraud Prevention or Fraud on the Consumer?
The Center for Legal Policy at the Manhattan Institute
The Federation of Defense and Corporate Counsel
The Harvard Club - New York City

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California's Notorious "17200" –
Written by Lewis Carroll, Adapted by Stephen King?

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Background

This law – Business and Professions Code Sec. 17200, the California Unfair Competition Law – is an offshoot of federal fair trade laws designed to protect businesses from unfair business practices engaged in by competitors. It began as a government enforcement tool. At the federal level and in most states it remains essentially so. In California it long served as a tool for the attorney general and district attorneys – permitting them to protect both firms and consumers by stopping a fraudulent, illegal, unfair business practice and get restitution for people who lost money because of it.

Legislative amendments and court decisions gradually made a fundamental change in this law. Private attorneys can use it to file a suit accusing a business of an unfair business practice:

- without a client;
- without evidence of anyone suffering a loss or even being deceived – simply accusing that an activity "tends to deceive" will keep a case in court;
- without any evidence of an intent to deceive;
- even if a district attorney or another private lawyer has already investigated and resolved a complaint related to the same activity.

Observations

An Atlanta lawyer with a California client called our office for a nutshell description our Unfair Competition Law. We finished, and there was silence, then a question: "Do y'all have gravity out there?"

A private attorney suing solely under 17200 cannot win ordinary tort damages, cannot get punitive damages, and there's often no client to agree to pay contingency fees. The dominant remedies are injunction and restitution. As a business activity for the lawyer, "17200" works in two basic ways:

> First, a separate "private attorney general" code section lets a judge order a defendant to pay attorney fees to lawyer winning a lawsuit in the public interest.
>
> Second, adding an unfair competition allegation to an existing lawsuit based on product defect, fraud, or almost anything else often raises the stakes and leads to bigger settlements.

While these 17200 benefits don't result in the multimillion dollar verdicts and huge contingency fee wins that make the papers, they do address a serious problem for segments of the plaintiffs' bar – the chronic client shortage. At a time when the ever-growing number of attorneys compete for clients on TV, the Yellow Pages, and the Internet, the ability to make money without a client is a blessing indeed.

As though confirming this, the state plaintiffs' lawyers' association announced a conference last spring with a seminar entitled: "Developing a New Practice – 17200."

California Supreme Court Justice Janice Brown cast this in different light in a dissenting opinion a couple of years ago, calling 17200 "a means of generating attorney fees without any corresponding benefit."

A federal judge on the Ninth Circuit recently wrote an opinion referring to 17200 as a "notoriously broad statute."

A California Law Revision Commission official has said he believes "there is a huge underground economy in 17200 claims."

An investigation of 17200 by the California Law Revision Commission found that:

> "The Unfair Competition Law provides unusually broad, and perhaps unique, standing for private parties . . . Those suing on behalf of the general public can range from plaintiffs having a narrow dispute with a defendant in a business context, who tack on the representative claim for discovery and settlement advantages, to plaintiffs serving a true private attorney general function...The Unfair Competition Law does not provide any mechanism to distinguish between these types of plaintiffs. There is a potential for abuse where a claim on behalf of the general public is added to a complaint for tactical advantage."

Note an agenda item at California plaintiffs' lawyers' annual Hawaii conference: “How Business and Professions Code Section 17200 Can be a 'Value Added' Component of Your Litigation."

University of San Diego Law School Professor Robert C. Fellmeth studied 17200 and wrote that "The survey of cases and practitioners involved in Unfair Competition Law litigation indicates that the statute's dilemma is no longer theoretical, it is currently functioning in a number of cases to frustrate the just and expeditious resolution of disputes."

Last month Mealey Publishing launched a new monthly publication dedicated solely to California’s 17200 law.

Awareness

Outside the legal community, awareness of this law has been slow in coming. There are several reasons.

Section 17200 doesn’t spawn big cases. Most never go to trial. In 17200 cases, no one tries to depose the CEO. I've never heard of 17200 cases, singly or cumulatively, being included in a corporation's 10-K report. Until recently, these suits seldom made the news – 17200 lawyers prefer to take their attorney fees from defendants who choose to pay them off rather than spend more money litigating. Neither side talks to the press – the company because it doesn’t want to attract copycat lawsuits and the lawyer because he doesn’t want copycat attorneys moving onto his turf.

Cases

In the mid-90s some lawyers tried to extract settlements by accusing software companies up and down the state of putting their product into boxes that were “too large,” therefore tending to deceive consumers into thinking they were getting maybe a dozen disks instead of one or two. (No such consumer ever stepped forward.)

These kind of cases abound: Several movie studios were sued under 17200 for using blurbs in their newspaper ads from movie reviewers they’d given freebies to.

Right now we know that 1,600 largely family-owned auto shops, mostly in Southern California so far, are being worked over by lawyers filing 17200 lawsuits based on two and three year old State Bureau of Automotive Repair investigations and citations. The lawyers find these by clicking on the Bureau’s web site and scanning dispositions of complaints, such as failing to give a customer a copy of an estimate. The lawyers tell each victim shop owner that if he or she mails them a certified check for $2,000 with a note promising never to do this again (a do-it-yourself injunction) they can consider the lawsuit dropped.

This is not only a small business scam; it has been used against oil companies by attorneys researching past air pollution investigations by the South Coast Air Quality Management District.

The California Building Industry Association tells us 17200 claims are now being added to some suits challenging development projects.

The law has furnished a new springboard for junk science. One lawyer has sued both the California and national dental associations, claiming a 17200 violation in their failure to state that amalgam filling material contains mercury. So far, the case has skated past the issue of whether mercury in fillings is harmful.

The California Supreme Court has ruled that Nike can be subject to a 17200 lawsuit accusing it of inaccurate statements in letters and press releases about labor conditions in overseas plants making its shoes. A petition was filed with the U.S. Supreme Court last week, asking for a review on freedom of speech grounds. Our association has been asked to file a brief on the 17200 issue.

Kaiser Foundation Health Plan has been sued under 17200 for ads praising its doctor-patient relationships.

On the other hand, a court of appeal has upheld a 17200 lawsuit against Massachusetts Mutual Life Insurance for failing to disclose internal background information on its policies.

There certainly are instances where companies should be liable for false statements, for fraud, for concealing information critical to investors or consumers, for anti-competitive activity. But remember, under 17200 we aren't talking about normal standards required to find fraud and determine liability. Standards requiring reliance, intent, damages, and so on don't apply to 17200. "Unfair" can be whatever a lawyer says it is.

Class Actions?

The issue of 17200's low or barely-existing standards for 17200 "liability" is under a new spotlight because of an appellate court ruling last summer against Bank of America. The court upheld the ability to use a 17200 violation claim as the basis for certifying a class action lawsuit over auto loans.

Until the state Supreme Court's Year 2000 *Kraus v. Trinity Management* decision, attorneys with few or no plaintiffs were able to guide restitution money into "fluid recovery funds" under the cy pres doctrine. These funds could propel the attorney on to the next case, etc. The court in *Kraus* said state law doesn't provide for such a spill-over of money from a defendant. So a 17200 violator cannot be ordered to disgorge ill-gotten gains beyond the amount which can be restored legitimately to a real life plaintiff or plaintiffs.

Because 17200 procedures do not require anything like a class notification, the projected (or hypothetical) number of persons incurring a loss might be large while the identified group of people who can actually receive restitution is small. This lack-of-notice problem has attracted some appellate concern but no solution other than coining the phrase "representative action" to distinguish a private attorney 17200 "class action" from an ordinary class action and to say (in *Kraus)* that maybe a judge can order a defendant to locate and notify customers who might be entitled to restitution.

On the other hand, class certification of a claim with plausible legitimacy can be more attractive to a defendant who would like finality to the litigation – something never certain under a 17200 lawsuit.

While Kraus appeared to restrict the 17200 largesse formerly available, 17200 plaintiffs' lawyers have not been "overly dismayed," as they say in the news business. One wrote on his web site that while you no longer can get a judge to order a defendant to contribute to your personal "corporation" or favorite cause, nothing prevents you from squeezing extra money in that direction in settlement negotiations.

A cleaner solution to plaintiffs' lawyers' *Kraus* problem was delivered by the majority in the afore-alluded-to *Corbett v. Superior Court (Bank of America*). Coupling the almost summary judgment-proof allegations of a 17200 claim with the threat of a class action certification raises the 17200 dollars-without-clients prospect to glorious heights.

Appellate Justice Paul Haerle, who wrote a stunningly clear dissent in *Corbett v. Bank of America* case, said that if this class action-17200 coupling is allow to stand, a future class action plaintiff could be "literally anyone [that the] class counsel dragoons off the street."

The lesson in all of this for judges and legislatures outside California is simple: Don't go there!

Attempts at Change

Our association has closely watched 17200 in the courts since the mid-90s, filing numerous amicus briefs in unfair competition-related appeals. Some decisions have acknowledged problems but have said it's the Legislature's role to fix them.

In the California Legislature, bills dealing with 17200 have to survive the judiciary committees, which are practically subsidiaries of the organized plaintiffs' bar.

On the ballot initiative front, late last year our association's Board of Directors voted to research an initiative for the 2004 statewide elections to cure abuses of Business and Professions Code Sec. 17200. Since then we have examined reform options and conducted focus groups with likely voters around the state. Surprisingly, we find good support for closing the private lawyer loophole in the Unfair Competition Act. People do not like lawyers without real clients doing what they are doing to victim companies. When we asked, "What about Enron?" people made a distinction. They understand prosecuting real wrongs versus settlement-leveraging and fee-inspired lawsuits. Personal injury lawyers dedicated to maintaining the status quo on 17200 remain incredibly low on the credibility scale.

In some of the most outrageous cases – like the auto shop shakedown I mentioned – the names of lawyers involved have been sent to the State Bar for investigation. Based on the Bar's action on a similar complaint a few years ago, I don't expect any strong action.

California Attorney General Bill Lockyer brought his office to bear on private attorneys using the state's Proposition 65 (which requires cancer warnings on almost everything) to extract

settlements from companies, sometimes using that law in conjunction with 17200. He worked with business and some environmental groups to enact changes that hold promise for ending some of the worst attorney fee-driven litigation.

I wrote Attorney General Lockyer last summer to urge him to put 17200 on his agenda for similar treatment. He had used the term “legal shakedowns” to describe some Proposition 65 violation claims and that precisely fits abuses going on under 17200.

He responded to the CJAC letter, acknowledging the problem and offering to work on it with us. We’ll be holding the first meeting next month. The first thing we learned is that there isn’t a conference room in the Attorney General's offices large enough for representatives of all the affected businesses whom we expect to attend the initial meeting.

As we proceed on this part of the project, I recall an observation the *Economist* made about the U.S. legal system a few years back: “Ideally, societies want lawyers to strike the right balance between being businessmen and being professionals. Wherever that 'right' balance is, lawyers have too often failed to find it on their own – especially where great wads of cash are there to be made.”

What Is Needed

Closing the loopholes of abuse in 17200 is not going to be a simple task.

Any solution should not diminish the ability of the attorney general and district attorneys to use 17200. Generally, the low threshold of violations and proof do not cause a problem when administered by a public official as opposed to a law business. We don’t want to eliminate private attorney use of 17200 altogether. Companies need to be able to use it. Some consumer protection uses are legitimate.

We need to focus on private attorneys who use the law claiming to be representing the public. We want to end:

o legal shakedowns;

o the use of 17200 as a add-on claim to enable discovery fishing expeditions to increase the burden on defendants as a way to leverage higher settlements;

o the ability to bring a 17200 lawsuit over an issue that a government agency, public prosecutor, or another private attorney has already settled.

If private lawyers are going to file lawsuits “in the public interest” using a law designed for public agencies, then they should be subject to much more public oversight.

Perhaps before launching a 17200 lawsuit, a private lawyer should have to convince a judge that the subject of the proposed suit is of genuine importance to the public and not largely a fee-generating scheme, and that public prosecutors have not already dealt with the matter. It may be that all settlements of a 17200 claim should be approved by the court. Perhaps we need

new rules on attorney fees that requires a judge to weigh real public benefit – or rule that there is none – when considering approving the attorney fee part of a settlement or judgment under 17200.

Some will argue that we must fully quantify the problem before beginning to solve it – that legal horror stories are not enough. An artful way of stating this is that: "Evidence is not the plural of anecdote." That is true, but it is not an absolute guideline. The California Legislature did not have data on numbers and kinds of lawsuits when it amended packaging law to stop the software shakedown suits I mentioned earlier.

Last session the plaintiffs' bar in California sponsored a bill to virtually eliminate the use of summary judgments. When questioned in a committee hearing about the number of summary judgments granted or the percent the sponsors objected to, the trial lawyer witnesses admitted they had no data. Nevertheless the Legislature went on to pass and the Governor signed a milder bill still designed to frustrate the granting of summary judgments.

Abuse of 17200 must end.

It has created a legal embarrassment, something that belongs in a story by Lewis Carroll or even Stephen King.

It is a cement shoe on California's business image nationally.

The loophole in 17200 is being used against small shop owners, many of them new Americans, many of them people who came to this country to escape lawlessness and arbitrary oppressive governments. What a shock it must be to discovery California's own brand of predatory oppression, all carried out with the silent consent of the state's Legislature and judiciary and encouraged by a large number of powerful officers of the court.

The total economic cost of 17200 abuse to larger businesses eludes us. But enough companies are feeling its effect that I believe we now are moving ever faster now toward the critical mass essential to bringing change.

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* The Civil Justice Association of California is a non-profit, membership supported coalition of citizens, taxpayers, businesses, local governments, professionals, manufacturers, financial institutions, insurers, and medical organizations.

Founded in 1979, CJAC is the only California statewide association dedicated solely to improving California's civil liability system. It is active in both the Legislature and the courts, working to reduce the excessive and unwarranted litigation that increases business and government expenses, discourages innovation, and drives up the costs of goods and services for all consumers.

Information on the association, membership, and more on 17200 is at the the CJAC web site www.cjac.org. The association's phone number is 916.443.4900.