

Episode 10: Pandemic Price Gouging

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Audio Transcript

Today's guest is Jeff Amato. And Jeff, I believe this is actually a return visit for you to our podcast. You've been on at least once before. Jeff is a partner in Winston & Strawn's New York office, and Jeff focuses on antitrust and complex commercial litigation. So hi, Jeff. Thanks for coming.

Jeff Amato: Thank you for having me back again to talk about this riveting subject.

Right? So today we're talking about a topic that's been grabbing headlines in recent months, and it's of particular importance in today's pandemic environment, and that's price gouging. So Jeff is going to walk us through the basics of price gouging and share some practical compliance advice for minimizing the exposure risks as the pandemic goes on.

So, Jeff, we didn't hear much—or anything, I think—about price gouging litigation until the pandemic. Can you explain to us why that is?

Jeff Amato: So, as a legal principle of price gouging is generally defined as raising prices beyond a fair or reasonable level for goods and or services that are deemed to be “essentials” or “necessities” during or immediately after a disaster or emergency declaration. At the beginning of the COVID-19 pandemic last winter, both federal and state governments declared states of emergency, which meant, among other things, that various laws prohibiting price gouging took effect.

Now almost a year later, we are still in a state of emergency, and price gouging is proving to be a very real threat to businesses that sell all sorts of different products. Investigations and prosecutions are on the rise, and prosecutors are casting wider nets in terms of the products and businesses they are going after. Because the state of

emergency is likely to continue for the foreseeable future, businesses that sell retail products need to continue being vigilant about how they operate, regardless of the products they sell or who they sell them to.

Okay. So, can you sort of just outline the basics or the elements, you know? What is price gouging?

Jeff Amato: Sure. So, although people frequently use the phrase “price gouging” to complain about unreasonably high prices, there isn’t typically a lot of price gouging litigation because, as I said, these laws only apply during government-declared states of emergencies like a hurricane or a pandemic.

And, at the moment, there are no federal laws that expressly prohibit price gouging. Having said that, the former President issued an executive order at the end of March 2020 invoking Section 102 of the Defense Production Act, which allows the President to designate certain materials as “scarce” and prevent hoarding those materials for resale at excessive prices.^[1] In the order, the former President delegated the authority to designate “scarce” products to the Secretary of Health and Human Services. So far, the DOJ has filed only a few cases under the Defense Production Act. Additionally, since the beginning of the pandemic, several bills have been introduced in the House and the Senate that would explicitly prohibit price gouging on the federal level, but none of these bills have been signed into law.

So, with no explicit federal prohibition on the books, price gouging violations are typically prosecuted under state law. Currently, almost all states have some sort of statute that addresses price gouging. It typically falls within the state consumer protection laws. While there can be a lot of variation among states’ laws, they all generally check the same four basic elements, and these are (1) the sale or offer for sale (2) of essential goods or services (3) at an unfair or unreasonably unconscionable price (4) following some emergency or other shock to supply or demand.

Okay. And let me just stop you there. Do those state laws typically apply to anyone who sells the essential goods or services directly to consumers, or are they broader than that?

Jeff Amato: So virtually all of the states prohibit price gouging by merchants who sell to the ultimate consumers. Some states, like New York and California, prohibit price gouging by any merchant, regardless of whether they sell to end consumers or to other merchants for distribution and resale. And a few states only prohibit price gouging in retail sales or sales to the ultimate consumer.

In terms of goods or services that qualify, I think you used the word “essential.” What does that mean?

Jeff Amato: Most states’ price gouging laws cover the sale of goods that are “necessary” in relation to the crisis. So for example, PPE would be necessary to the current crisis. But keep in mind that some states cover a wider range of products or are otherwise broad in their terms. For instance, Delaware has expansive price gouging prohibitions that cover any goods or services offered for sale. In contrast, some states’ laws are very narrow. For example, Vermont only prohibits price gouging of petroleum and heating products.

Okay. So you really have to look at that one on a state-by-state basis. Is there a sort of a general definition of what constitutes an unfair or illegal price increase?

Jeff Amato: This is also going to vary by state. However, most states have statutory metrics that are used to determine whether a price is “unreasonable” or “unconscionable” and therefore illegal. Generally, the first step is to look to the average price of a particular good during the period of time immediately before the state of emergency. The period of time used to determine the average varies among the states. Some states look at the average price 30 days before the crisis, while others can be as long as 90.

Another nuance here among the states is whether the average price is based on the market price of the product or the specific seller’s price in the time before the crisis. This distinction could be meaningful depending on how a seller’s prices compared to the competition going into the emergency. For instance, if the average market price is used, it might not matter if the seller’s prices were previously well below competition.

Once we’ve determined the average price, the next step in the analysis is to determine whether a price increase is unreasonably large. Most states define this threshold in terms of a percentage, and it is typical for a price increase above 10% to qualify as “unreasonable.” But some other states cap price increases at a 25% threshold.

Some state statutes don't include pre-defined thresholds, and instead leave the determination to be made on a case-by-case basis. For example, Texas prohibits "exorbitant or excessive," which is for the court to determine based on the facts. Other states prohibit price increases that create a "gross disparity" or are "unreasonably excessive under the circumstances."

And what about defenses or exceptions to price gouging violations in various states?

Jeff Amato: Yeah, there are defenses. Generally speaking, states will not hold a seller liable for passing on increased costs of goods from higher in the distribution chains to consumers. This is basically the standard defense available in all states that prohibit price gouging. But it's important to note that while sellers are generally allowed to raise their prices to compensate for certain increased costs, many states put caps on how much of a markup can be added on top of those costs. For example, in California, prices can only be increased to a maximum of 10% more than "the total of the cost to the seller plus the markup customarily applied by the seller for that good or service in the usual course of business immediately prior to the onset of the state of emergency."

There are additional exemptions and defenses to price gouging claims, but these are going to vary state by state. For instance, some states have carve-outs for specific industries and products that would be exempt.

Okay, understood. Let's move on, if we can, to the risks. Who can sue for price gouging? And what are the potential claims?

Jeff Amato: So, most states classify price gouging as a consumer protection violation and allow the attorney general of the state to seek some combination of injunctive relief and civil penalties, as well as restitution in certain states. In some states, such as California, price gouging violations can also qualify as misdemeanors or felonies. And individuals may also be subject to criminal fines of up to \$10,000 and potentially incarceration. Additionally, some states provide an express private cause of action, and plaintiffs have alleged that price gouging violations constitute a predicate offense for the basis of class action lawsuits, which can carry a significant civil exposure.

Well, in light of those serious risks, let's turn now to some practical suggestions that I know you wanted to cover for compliance with price gouging laws.

Jeff Amato: Sure. I think there are a number of steps businesses of all sizes can take to minimize their risk. First, while price gouging laws generally cover a broad array of products and services, enforcement during the pandemic is likely to focus much more on products and services tied to preventing the spread of COVID-19 such as PPE—personal protective equipment, hand sanitizer, and disinfecting services. A number of state AG cases and private class actions have already come up concerning these products. Merchants dealing in these goods and services should be particularly attuned to the possibility that price increases might trigger scrutiny and even potential private actions. That said, enforcers and private litigants might later revisit potential instances of price gouging during the pandemic in other industries.

So, retailers should be mindful of their profit margins and how they have changed with the pandemic. Although it might be tempting to raise prices for products that are seeing increased demand, like toilet paper or paper towels, sellers should be very careful about raising their prices too far above pre-pandemic levels, especially if costs to acquire and sell the goods haven't increased as much.

Relatedly, businesses should also be very diligent in recording any increases in their costs for acquiring merchandise. The pandemic has caused disruption in a wide range of industries, and many companies may be facing legitimate cost increases as a result. It's likely that upstream costs for production and shipping have increased as a result of the pandemic. For example, these cost increases could take the form of:

- Suppliers increasing prices of inputs that needs to be passed on;
- The need to find a new supplier when a prior one runs out of inventory or goes out of business;
- Increased labor costs as a result of extended hours with overtime pay;
- Loss of economies of scale as a result of reopening at lower capacity or with partial staff;

- The need to redesign a workspace so employees can stay six feet apart;
- The need to supply masks, PPE, or other supplies to the workforce; and
- The need to increase expenses or services like cleaning or testing employees for COVID-19.

If price increases are due in whole or part to legitimate cost increases—such as some of the ones I just mentioned—those cost changes should be documented, and any price increases should be commensurate with cost increases to minimize exposure. Businesses that sell essential products should also maintain records of their pricing from at least 30 days before the declaration of emergency, depending on applicable state laws. This is especially so if the sales are online. Companies may be able to use automated tools and artificial intelligence to help record prices to ensure the company is prepared if a state attorney general comes knocking, or to use in response to being frozen or kicked off as a digital platform.

This documentation should be maintained in easily accessible—ideally central—business records, as opposed to on one person’s private or personal computer. This will allow multiple people within the organization to be aware of the legitimate reasons for the price increases during emergencies and to further document other potential instances that might arise. If these issues become litigated down the road, this will also ensure that the records can be located, collected, and reviewed easily without exposing unrelated personal files to the same treatment or otherwise risk loss, destruction, or spoliation if that employee leaves the organization.

Okay. Thanks. And one last question, Jeff, that did come to mind. Do price gouging claims need to be filed now, during the declared emergency? What, in other words, what is the statute of limitations?

Jeff Amato: That’s a great question. Uh, while price gouging prohibitions are generally enforced only during states of emergency, the eventual end of the pandemic does not mean businesses will be out of the woods. Most states have statutes of limitations that allow claims to be brought for up to two years after the violation took place. Some states have longer limitations periods that run for up to six or even 10 years. This means that price gouging prosecutions can—and likely will—continue long after the pandemic is finally behind us.

All right. Whenever that may be. Jeff, thank you so much for joining me again on our podcast. You have a lot of information that I hope our listeners will be able to use as this crisis goes on.

Jeff Amato: It’s been my pleasure, and I hope this crisis comes to an end soon.

[1] The Defense Production Act of 1950, [50 U.S.C. § 4512](#).

Speaker

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