Sills Cummis & Gross P.C.

COVID-19 Legal Resources

Client Alert

Sellers Beware – The COVID-19 Pandemic Has Opened the "Price Gouging" Pandora's Box

As the COVID-19 emergency goes on, both federal and New Jersey authorities have begun to enforce anti-price gouging and anti-hoarding provisions of federal and state law. A wide range of businesses, including but going beyond the sellers of medical equipment, should be aware of the limits imposed by these statutes and the dangers posed by enforcement.

A. The New Jersey Consumer Fraud Act

As has been widely reported in the media, the State of New Jersey is aggressively enforcing the anti-price gouging provisions of the Consumer Fraud Act, N.J.S.A. 56:8-107 through 109, during the current coronavirus emergency. Enforcement of the statute by the Division of Consumer Affairs or by private civil action under the Consumer Fraud Act poses a risk to the sellers of a broad variety of goods. However, it also poses a potential remedy for business purchasers for end use whose ordinary supply chain has been disrupted by the emergency.

During a state of emergency declared by the Governor, N.J.S.A. 56:8-109 makes it an "unlawful commercial practice" for any person to sell or offer for sale "any merchandise which is consumed or used as a direct result of an emergency or which is consumed or used to preserve, protect, or sustain the life, health, safety or comfort of persons or their property for a price that constitutes an excessive price increase." In turn N.J.S.A. 56:8-108 defines an "excessive price increase" as more than 10 percent greater than the seller's price in the usual course of business immediately before the declaration of emergency, unless the price increase is attributable either to the seller passing through increased prices from its supplier or costs imposed by the emergency. In that case, the statute defines an excess price increase as an increase of more than 10 percent beyond the seller's customary pre-emergency markup.

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The statutory language sweeps broadly and may be applied to price increases of almost any product where demand has increased or the supply chain has been disrupted by the coronavirus emergency. A recent news story reports that more than 3,600 complaints of alleged price-gouging have been made to the Attorney General's Division of Consumer Affairs, against more than 2,100 business, involving not only medical supplies but food and commodities in short supply like toilet paper and disinfectants. The Division is urging the public to remain "vigilant" and is actively soliciting complaints on its website. As it investigates complaints, the Division is issuing subpoenas for the seller's pre-emergency and current cost, price and markup information. The defense of passing through increased costs requires the seller to document both higher charges from suppliers and other costs, such as hazard pay for employees, imposed by the emergency.

Penalties for violation of the Consumer Fraud Act include civil penalties of up to $10,000 for a first offense. There are additional penalties if the violation was directed against senior citizens or persons with disabilities. In addition, the Attorney General may obtain an injunction against future violations. The courts may order restitution to consumers of money obtained in violation of the Act, and twice the amount obtained in the case of senior citizens. Failure to make restitution as ordered is punishable as contempt of court.

In addition to the enforcement powers of the Attorney General, N.J.S.A. 56:8-19 gives any person who has suffered an "ascertainable loss of moneys or property . . . as a result of any practice declared unlawful" under the Consumer Fraud Act as amended or supplemented a private right of action to recover treble damages and attorneys' fees, either directly or as a counterclaim in a suit by the seller. No reported decision decides whether this private right of action would apply to a violation of the Act's anti-price gouging provisions, but it is reasonable to anticipate that creative counsel are contemplating private class actions on behalf of retail purchasers.

The private right of action under the Consumer Fraud Act extends not only to individual consumers but to businesses that purchase supplies or equipment for use in the business. Hospitals, medical practices and other large scale purchasers of supplies and equipment affected by the coronavirus emergency may wish to explore that possibility.

B. The Federal Defense Production Act

The Korean War vintage Defense Production Act ("DPA") gives the President broad powers to direct the production of essential goods and to prioritize their distribution during periods of declared national emergency. Section 101 of the DPA, 50 U.S.C. § 4511, authorizes the President or his delegate to designate goods as scarce materials critical to the national defense. Section 102 of the Act, 50 U.S.C.§ 4512, the anti-hoarding provision, prohibits any person from accumulating "1) in excess of the reasonable demands of business, personal, or home consumption, or (2) for the purpose of resale at prices in excess of prevailing market prices, materials which have been designated by the President as scarce materials or materials the supply of which would be threatened by such accumulation." Designations are required to be published in the Federal Register. Section 103 of the DPA, 50 U.S.C. § 4513 makes the violation of § 102

a federal crime subject to a $10,000 fine and one year imprisonment. In addition § 706, 50 U.S.C. § 4556, authorizes the federal courts to enjoin violations of the DPA at the suit of the government. Other provisions, not relevant here, authorize the government to provide incentives and subsidies to increase production of essential goods.

The DPA is based on the War Powers Acts of World War II. It is designed to authorize the kind of command economy in place during that war, in which the armed forces were the sole end user, the government controlled production by placing contracts, fixing priorities and allocating raw materials, and the government directly controlled prices in the civilian market. It empowers the federal government to become the sole buyer and allocator of materials critical to the national defense. However, the President has chosen not to take the responsibility for centralized purchasing and allocation of critical medical supplies. Instead, the federal government has decided to allow states and other end users to compete for limited resources while using the DPA's criminal provisions to try to curb the more egregious examples of exploitation.

On March 23, 2020, the President issued Executive Orders 13909 and 13910, which invoke his authority under DPA § 101 to declare ventilators and medical personal protective equipment as scarce materials critical to the national defense. Under authority designated by the Executive Orders, on March 25, 2020 the Secretary of Health and Human Services designated a variety of masks, gloves, gowns, face shields and other personal protective equipment, as well as respirators, sterilization materials, and ventilators as scarce materials subject to the anti-hoarding section of the DPA. The designation was published in the Federal Register at 85 FR 17592 (Mar. 30, 2020). It enumerates the types of short-supply equipment but does not provide guidance as to what constitutes accumulation in excess of reasonable demand for consumption or what prices are considered in excess of the prevailing market price.

The Department of Justice has created a joint federal-state anti-hoarding task force under the leadership of the United States Attorney for the District of New Jersey, and several criminal prosecutions of alleged hoarders have been instituted. However, the prohibitions in DPA § 102 of accumulation "in excess of reasonable demands" for the holder's consumption or for resale at a price "in excess of prevailing market prices" appear to impose a rather vague standard of criminal liability, and there do not appear to be any reported decisions interpreting them. Unlike the New Jersey statute, there is no definite markup that would be allowed.

DPA § 104, 50 U.S.C. §4514, prohibits the President from imposing wage or price controls without Congressional authorization. Perhaps for that reason, the government has not set permissible prices for short-supply equipment at any time since the HHS designation. Instead, the government is taking the position that prevailing prices are either prices in effect in January and February of 2020, before the coronavirus crisis began in the United States, or that they are "benchmark" prices of a major private manufacturer. Whether either of those standards provides fair advance notice sufficient to support criminal liability is, to say the least, contestable.

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In addition, the government's position appears to criminalize what may be entirely legitimate economic activity. Experience has shown that there were large amounts of masks and other designated short-supply medical equipment scattered in pockets of inventory around the United States and abroad. Middlemen perform the valuable service of finding these supplies, marshaling them and making them available to end users. That takes effort, which will not be undertaken without the prospect of compensation. Unlike the New Jersey statute, the DPA does not on its face recognize the costs incurred by accumulators to obtain otherwise unavailable goods, either those passed through from upstream sellers, the expenses of search, or reasonable compensation for the effort involved.

In conclusion, the government has not used the DPA to set prices directly. Its criminal anti-hoarding provisions are a very blunt instrument for regulating economic activity in a time of shortage, especially because the federal government is not acting as the sole buyer or allocator of goods or fixing prices but is instead requiring end users of short-supply equipment to compete against each other. These criminal provisions have never been tested in court, and they leave open the possibility of vigorous defense based on the lack of a clear standard of criminal liability, on the need to attract scarce goods into the market, and on the pass-through of legitimate costs incurred to do so, including a reasonable profit. At this time, the permissible range of prices under the DPA is unclear and has not been tested in court. Clients are advised to retain records of sales and underlying costs, including both cost of goods sold and related expenses, and to be aware that the federal authorities are keeping a vigilant eye on the sale of designated scarce-supply medical equipment.

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