9/8/75

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

BROWN & WILLIAMSON TOBACCO CORPORATION, Plaintiff, -against- LEWIS A. ENGMAN, Chairman, Federal Trade Commission, et al., Defendants.	:	75 Civ. 4047 (CHT) and the following consolidated actions: 75 Civ. 4048 (KTD) 75 Civ. 4049 (KTD) 75 Civ. 4050 (CBM) 75 Civ. 4051 (CLB) 75 Civ. 4052 (CLB)

PLAINTIFFS' BRIEF IN OPPOSITION
TO DEFENDANTS' MOTION TO DISMISS

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Plaintiffs submit this brief in opposition to defendants' motion to dismiss the complaints in these consolidated actions pursuant to Rule 12(c) of the Federal Rules of Civil Procedure.*

Preliminary Statement

By taking the extraordinary and unwarranted action of formally "determining" that six cigarette manufacturers are in

* Defendants' motion is not properly made under Rule 12(c), which governs motions for judgment on the pleadings and provides that a party may move for judgment on the pleadings "[a]fter the pleadings are closed . . ." Since none of the defendants has answered the complaint, the motion is improper. Hence, defendants' motion is in substance a motion to dismiss under Rules 12(b)(1) and 12(b)(6) and will be so treated in this brief.

violation of consent orders regulating cigarette advertising and announcing its determination to sue them for civil penalties, the Federal Trade Commission has put plaintiffs to a classical Hobson's choice, barring a prompt decision on the merits by this Court.

Now that plaintiffs are on notice that the full Commission deems their cigarette advertising to violate the consent orders, plaintiffs -- unless this Court promptly resolves this dispute -- have only two alternatives:

1. They can immediately change their advertising in an attempt to comply with the FTC's determination, with no assurance that the changes would satisfy the Commission's ill-defined demands, or

2. They can continue with their advertising.

If they choose the first option, they do so at substantial cost without first having an opportunity to test the legality of the FTC's position in court. If they choose the second alternative, knowing that the FTC regards their advertising as unlawful and that it intends to seek civil penalties, they run a serious risk of judgments potentially amounting to tens of thousands of dollars a day -- with the clock running until the FTC commences its action and then throughout the enforcement proceedings.

Defendants maintain that the federal courts lack jurisdiction in a declaratory judgment proceeding to rule on the correctness of the FTC's determinations that certain of plaintiffs' advertising does not comply with the consent orders, although defendants themselves have proposed that this issue ultimately will be decided by a federal court in an enforcement proceeding -- that is, unless the enormous risks deter plaintiffs from seeking review at all.

Defendants rest their position chiefly on two grounds. First, they assert that defense of an enforcement proceeding -- whenever it may be commenced -- is an adequate remedy for the situation in which plaintiffs find themselves and that accordingly there is no need for judicial review at this time. Second, defendants argue that the Court should infer that Congress intended to preclude judicial review at this juncture.

Defendants' principal claim is that pre-enforcement judicial review should be precluded because it would hinder the voluntary settlement of trade regulation disputes. But the availability of pre-enforcement review cannot possibly impair settlement; plaintiffs and the FTC obviously can settle disputes about the meaning of the consent orders at any time, whether or not pre-enforcement review is available. Hence, the FTC's real complaint must be that the availability of pre-enforcement review would deprive the FTC of its trump card in the settlement context --

the extortive "bargaining power" that it would enjoy if plaintiffs must risk enormous civil penalties to challenge the FTC's interpretation of the consent orders. And it is precisely that leverage -- the fact that plaintiffs must knuckle under or run grave risks -- that makes plaintiffs' position intolerable and defense of an enforcement proceeding an inadequate remedy.

Defendants also suggest that granting pre-enforcement review in this case would create a precedent that could flood the courts with disputes over compliance with FTC orders. But that contention overlooks entirely the extraordinary nature of the FTC's August 1, 1975 determination. Such a formal and public determination by the full Commission that one subject to an FTC order has violated that order is most unusual and perhaps unprecedented. And since we seek review of this unusual formal action by the Commission, not some informal expression of opinion by the staff, defendants' fears are groundless.

The Commission's extraordinary action has put plaintiffs in a serious dilemma.

The Constitution, the Administrative Procedure Act, the Declaratory Judgment Act, and venerable principles of equity bar subjecting plaintiffs to such a dilemma and, we submit, require this Court to retain jurisdiction and to decide this case on the merits as promptly as possible.

The Facts*

The material facts relevant to this motion to dismiss are few.

Background

In 1965, Congress enacted legislation which, inter alia, required a warning statement with respect to smoking and health on each cigarette package.** The statute, amended in 1969, does not require the inclusion of a warning statement in cigarette advertising or promotional materials. However, beginning about April 15, 1971, plaintiffs -- cigarette manufacturers -- voluntarily included the warning statement in their advertising.

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* Since this is a motion to dismiss, the well-pleaded allegations of the complaint are deemed admitted for the purposes of this motion. Jenkins v. McKeithen, 395 U.S. 411, 421-22 (1969). The same rule applies to motions for judgment on the pleadings. 5 Wright & Miller, Federal Practice and Procedure § 1368, at 691 (1969).

We note that the defendants' motion does not rest on the affidavit submitted by them in opposition to plaintiffs' motions for a stay of the accumulation of penalties. The notice of motion states that the motion to dismiss is made only "upon the accompanying memorandum of law. . . ." Paragraph 1 of the affidavit states that it is submitted only "in opposition to plaintiffs' application for a stay . . ." Hence, it would be inappropriate to treat the motion as one for summary judgment. (Cf. Rule 12(b), Fed. R. Civ. P.) We nevertheless have submitted affidavits refuting defendants' contentions. In the event the Court elects to consider the affidavits, any material disputes of fact would require denial of defendants' motion under Rule 56, Fed. R. Civ. P.

** The Federal Cigarette Labeling and Advertising Act, 79 Stat. 282. The phrasing of the required warning statement was amended by the Public Health Cigarette Smoking Act of 1969, 15 U.S.C. § 1333.

In July 1971, the Commission sent plaintiffs a proposed complaint, which alleged that the warning statement in advertising was not sufficiently clear and conspicuous, and was therefore a deceptive practice in violation of Section 5 of the FTC Act, 15 U.S.C. § 45. The Commission simultaneously offered to negotiate a settlement of the proposed complaints by consent orders.

Plaintiffs thereupon jointly entered into intensive negotiations with the Commission's staff. The discussions continued over many months and culminated in six agreements and consent orders, identical as to each company, issued by the Commission on March 30, 1972.* The orders prescribe in minute detail the format of the warning statement to be included in newspaper, magazine and billboard advertising, transit cards, leaflets, direct mail circulars, programs, paperback book inserts, and point of sale ("POS") promotional materials.

Plaintiffs revised their advertising and promotional materials to conform with the requirements of the orders, and the warning statement has appeared in conformity with the orders in thousands of newspaper and magazine advertisements, on billboards, and in POS materials.

The consent orders required the submission of compliance reports. In August and September 1972, such reports were submitted to the Commission by all six plaintiffs. The reports included copies of representative advertisements and promotional materials containing the warning statement required

* Copies of the consent orders are attached as exhibits to the complaints.

by the consent orders. The Commission did not communicate any objection to plaintiffs with respect to the compliance reports; rather, in December 1972, the FTC informed plaintiffs that "no compliance action by the Commission is indicated at this time."

Section 8(b) of the Public Health Cigarette Smoking Act of 1969, 15 U.S.C. § 1337(b), requires the Commission to submit an annual report to Congress concerning, among other matters, "current practices and methods of cigarette advertising and promotion." In its report dated December 31, 1972, the Commission advised Congress:

> "Advertisements containing the disclosure statement in the format required by these [consent] orders began to appear in May of 1972, and by the end of October, all cigarette advertisements observed by the Commission staff were being published in accordance with the terms of these orders." (Federal Trade Commission Report to Congress, December 31, 1972, p. 4.) (Emphasis supplied.)

In its next annual report to Congress, dated December 31, 1973, but actually issued on January 23, 1974, the Commission publicly and officially repeated that "by October of 1972, almost all cigarette advertising published in this country was in compliance with the terms" of the consent orders. (Federal Trade Commission Report to Congress, December 31, 1973, p. 1)

Plaintiffs relied on the Commission's acceptance of its compliance reports and on the Commission's official reports to Congress. They believed that the Commission deemed the depiction of the warning statement in its advertising and promotion to be in conformity with the order.

The Present Controversy

Plaintiffs have complied diligently with the provisions of the consent orders. Nevertheless, in May 1974, the staff of the Commission commenced an inquiry into the manner of all of the plaintiffs' compliance with the orders. Plaintiffs cooperated in the staff's inquiry. But in response to plaintiffs requests that there be discussions as to what would avoid future controversy with respect to plaintiffs' advertising and promotional materials, the staff repeatedly informed plaintiffs' counsel that as a pre-condition to such discussions plaintiffs would have to agree to join in a lump-sum payment of about $6 million as penalties for alleged violations of the orders.*

On August 1, 1975, the Commission sent similar letters to each of the plaintiffs. The letter to Brown & Williamson -- which is representative -- stated in pertinent part:

> "The Federal Trade Commission has determined that Brown & Williamson Tobacco Corporation has violated the above-captioned order by failing in certain cigarette advertisements to disclose the required health warning and by failing in other

* While the allegations of the complaint are deemed true for purposes of this motion, we note that defendants' affidavit does not deny that the staff advanced the $6 million figure in connection with a discussion of penalties. It denies only that a $6 million payment was a pre-condition to discussions. (Rubin affidavit ¶¶ 16-17).

cigarette advertisements to disclose the health warning in the clear and conspicuous manner that is required by the order.

"The Commission will, therefore, pursuant to the provisions of 15 U.S.C. 56(a)(1), notify the Attorney General of its intention to commence for these violations an action for civil penalties and other relief. . . .

"By direction of the Commission Charles A. Tobin, Secretary" (Brown & Williamson Cpt. exh. B) (emphasis supplied)

The letter also mentioned four ill-defined alleged forms of violations of the order relating principally to alleged failures to display the warning on vending machine display panels and counter racks, alleged failures to display the warning in the proper type style or size, and an allegedly inaccurate translation of the health warning in foreign language advertising. (Brown & Williamson Cpt. exh. B)

It is undisputed, however, that the warning statement has appeared on every package of cigarettes and in thousands of newspaper, magazine and other advertisements, as well as a broad range of promotional material. Indeed, the Court properly may notice that the warning statement has become a ubiquitous feature on American life and that virtually every literate citizen is fully aware of its message.

Plaintiffs submit that the determinations in the Commission's letter are based on erroneous and unwarranted

interpretations of the express terms of the consent order. The Commission manifestly has taken a contrary position. Thus, there is an immediate and concrete controversy between plaintiffs and the FTC, and plaintiffs are in urgent need of a prompt judicial resolution of that conflict in order to guide their future conduct.

I

PLAINTIFFS ARE ENTITLED TO PRE-ENFORCEMENT REVIEW OF THE FTC's DETERMINATION

Plaintiffs need immediate judicial review because the Federal Trade Commission has taken extraordinary action in the context of a dispute over the interpretation of six 1972 consent orders dealing with the depiction of a health warning in certain cigarette advertising. The Commission has formally and publicly determined that certain of plaintiffs' advertising violates the orders, and the Commission has notified the companies that the Commission will institute an action against plaintiffs for civil penalties -- penalties which mount for each day of noncompliance. 15 U.S.C. § 45(l). Thus, the Commission necessarily has served notice not only of its determination that plaintiffs' past advertising has violated the order, but that it regards the future use of such advertising as unlawful and subject to heavy penalties. Plaintiffs firmly believe their advertising complies with the consent orders, and they require a judicial determination to resolve this controversy and guide their future conduct.

It is clear that this dispute between plaintiffs and the Commission will have to be resolved by a federal court. Defendants have conceded that apart from the question of a stay of penalties, "there is no appreciable difference between this action and the enforcement action." (Defendants' Memo., p. 23). The only question then is whether jurisdiction should be accepted now, rather than later.

We believe that jurisdiction should be accepted now because there is an immediate and serious controversy between the parties. Contrary to defendants' contentions:

- The FTC Act does not preclude the Court from accepting jurisdiction now. Defendants contrary argument is based entirely on a seriously misleading treatment of the legislative history.

- The FTC's August 1 determination is final, reviewable agency action. It has immediate practical and legal consequences for plaintiffs -- consequences that are present whatever the FTC's subjective motivations may have been.

- Plaintiffs have no other adequate remedy but this proceeding. There is no other vehicle by which plaintiffs can obtain review of the FTC's determination without running the risk of serious penalties which may be accumulating from day-to-day.

A. The Federal Trade Commission Act Does Not Preclude Review.

The FTC argues strenuously that this action should be dismissed because the Federal Trade Commission Act evidences a

Congressional intention to preclude judicial review of the FTC's August 1, 1975 determination.* It asserts that pre-enforcement review would conflict with an alleged legislative purpose to foster voluntary settlement of trade regulations disputes without resort to the courts. But the government's position is based upon a misleading discussion of the legislative history.

The sources cited by the government plainly do not stand for the proposition that Congress intended that disputes over the meaning of FTC orders be resolved in the FTC, without resort to the courts. The government's authorities instead show that Congress intended that the FTC rather than the courts have jurisdiction in the first instance over claims of unfair or deceptive trade practices under Section 5(a) of the Act, 15 U.S.C. § 5(a), in order to utilize its expertise in defining such practices.** Indeed, the notion that the interpretation of FTC orders was intended to be a matter for the Commission and not the courts is inconsistent with the structure of the Act.

The Federal Trade Commission Act provides for no enforcement procedure within the Commission after an order is entered. It provides instead that enforcement proceedings are

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* See Administrative Procedure Act, § 10, 5 U.S.C. § 701(a)(1), which provides for judicial review "[e]xcept so far as (1) statutes preclude judicial review . . ."

** Thus, the D.C. Circuit (and others) has declined to imply a private cause of action under Section 5(a). Holloway v. Bristol-Myers Corp., 485 F.2d 986 (D.C. Cir. 1973).

to be instituted in the first instance in the federal district courts. 15 U.S.C. §§ 45(l), 45(m). And since -- as the government concedes -- the defendant in an enforcement proceeding can contest the FTC's interpretation of its order, there can be no doubt that the courts inevitably review FTC determinations that its orders have been violated. Thus, the only issue is when -- not whether -- judicial review is to take place.

The Federal Trade Commission Act is silent on the question whether one subject to an FTC order may obtain pre-enforcement review of the FTC's determination of a violation. And since Congress knows how to express explicitly an intention that judicial review be precluded,* the fairest conclusion is that Congress did not intend that pre-enforcement review be precluded. Moreover, the structure of the Act is such that there is no reason to infer an intention to preclude review.

As we have seen, the need for judicial review of the Commission's August 1, 1975 determination arises from its interrelationship with the cumulative penalty provisions of Section 5(l) of the Act. Since Congress gave scant attention to the penalty provisions of Section 5(l)** and doubtless never foresaw that the Commission would take the extraordinary step of making a formal public determination of a violation of its order, a function it committed to the courts, it can hardly be said that Congress intended to preclude pre-enforcement judicial review in

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* See Jaffe, Judicial Control of Administrative Action 353-57 (1965).

** United States v. St. Regis Paper Co., 355 F.2d 688, 692 and n.5 (2d Cir. 1966).

such circumstances.* The facts are simply so unusual that we can have no idea what Congress would have done had it considered the matter.

The Supreme Court repeatedly has said "that only upon a showing of 'clear and convincing evidence' of a contrary legislative intent should the courts restrict access to judicial review." Abbott Laboratories v. Gardner, 387 U.S. 136, 141 (1967). Accord, e.g., Barlow v. Collins, 397 U.S. 159, 166-67 (1970); Kingsbrook Jewish Medical Center v. Richardson, 486 F.2d 663, 667 n.11 (2d Cir. 1973); Citizens Committee for the Hudson Valley, 425 F.2d 97, 101-02 (2d Cir.), cert. denied, Parker v. Citizens Committee for the Hudson Valley, 400 U.S. 949 (1970).

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* Defendants' contention that pre-enforcement review would frustrate an alleged Congressional purpose that a decision to bring an enforcement proceeding be made only after consultation between the FTC and the Attorney General cannot withstand analysis. (Defendants' Memo., pp. 30-33)

For one thing, plaintiffs should not be denied review of FTC action that has an immediate impact on its business merely because the FTC acted improperly by failing to consult with the Attorney General. For another, it appears that the FTC's improper action may have eliminated prospectively the consultation requirement -- as anomalous as that may seem.

The FTC maintains that it need not consult with the Attorney General prior to instituting enforcement proceedings with respect to violations "committed with actual knowledge of their unlawfulness . . ." (see id. at 30). Thus, the FTC's position may well be that the August 1 determination put plaintiffs on formal notice, that any future advertising that fails to conform to the FTC's interpretation would be "with actual knowledge of [its] unlawfulness" (infra, pp.20-21), and that it therefore may institute enforcement proceedings relating to the post-August 1 period without consultation with the Attorney General.

Indeed, the Court's most recent pronouncement is even stronger. In dealing with the reviewability of action taken by the Department of Transportation, the Court stated:

> "A threshold question -- whether petitioners are entitled to any judicial review -- is easily answered. Section 701 of the Administrative Procedure Act . . . provides that the action of 'each authority of the Government of the United States,' . . . is subject to judicial review except where there is a statutory prohibition on review or where 'agency action is committed to agency discretion by law.'" Citizens to Preserve Overton Park v. Volpe, 401 U.S. 402, 410 (1971) (Emphasis supplied)

Not only is there no reason to infer that Congress intended to preclude review of action such as that taken by the Commission here, but there is most certainly no "statutory prohibition on review." Accordingly, judicial review is not precluded by statute within the meaning of Section 10 of the Administrative Procedure Act. Indeed, if it were, the statute would be unconstitutional under the rule announced by Justice Brandeis in Oklahoma Operating Co. v. Love, 252 U.S. 331 (1920). Infra, pp. 29-30

B. The FTC's Determination is Final and Authoritative.

The government has argued that the FTC's August 1 letter was intended merely to "encourage" plaintiffs to make a "settlement offer." (E.g., Transcript, August 25, 1975, at 45-46). Thus, the government seems to be suggesting that review is inappropriate either because there remain further administrative proceedings or because the FTC's determination was not final. Both of these contentions should be rejected, as they fail to appreciate the full significance of the FTC's action.*

To begin, it should be clearly understood that the statutory scheme for enforcement of FTC orders does not contemplate any administrative proceeding in the sense that we normally understand that term. There is no established adversary procedure within the FTC for determining whether

* Indeed, the Court should not even consider defendants' attempt to undercut the Commission's August 1 letter. Not only does the suggestion that the letter was merely a negotiating gambit ignore the plain language of the document, there is no evidence that the representations made to the Court were authorized by the full Commission, and plaintiffs have had no opportunity to conduct discovery to determine whether the staff's characterization of the Commission's action was authorized. Rules 12(b), 12(c), 56(f), Fed. R. Civ. P.

a prospective defendant is in compliance with an order prior to the institution of enforcement proceedings in a federal court. The normal course of events is that the FTC staff determines that there is reason to believe an order is being violated and a recommendation for prosecution is made to the Commission. If the Commission elects to prosecute, an action for civil penalties is commenced.* The FTC does not necessarily give a prospective defendant notice that it deems it to be in violation of an order, and our Circuit has held that it need not do so. United States v. J. B. Williams Co., 498 F.2d 414, 434-35 (2d Cir. 1974). Thus, the Commission's action in formally and publicly "determining" that plaintiffs were in violation of the consent orders was an unusual event not contemplated by normal FTC procedures -- and there is no means of securing further consideration of that determination

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* With certain limitations, the FTC can now prosecute its own penalty actions. 15 U.S.C. §§ 45(l), 45(m)(1), 56. The Attorney General no longer has a veto power over the institution of enforcement proceedings.

within the Commission.* The Commission's sole role is that of prosecutor in an action brought in a United States district court. See 15 U.S.C. §§ 45(l), 45(m).

The FTC's unusual action has immediate consequences for plaintiffs' business. Plaintiffs are no longer faced merely with a disagreement with members of the FTC staff; they are confronted with an authoritative ruling by the full Commission and a determination to prosecute. As the August 1

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* The government has stated that "[t]he FTC's disclosure of its intent to commence an enforcement action in this matter was done pursuant to long-standing procedures, described with approval by the 2nd Circuit . . . U.S. v. St. Regis Paper Co., supra, 355 F.2d at 696." (Defendant's Memo p. 21) That statement is highly misleading.

The reference in St. Regis is to an FTC rule, now 16 C.F.R. § 3.61(a) (1975), which relates to the Commission's handling of compliance reports. Commission rule 3.61(a) indicates that one filing a compliance report "may" be advised "whether the actions set forth therein evidence compliance . . ." But the government fails to mention either that the Commission has delegated that authority to the staff (36 Fed. Reg. 7082 [1971], 3 Trade Reg. Rep. ¶ 9840.07) or that the rule makes no mention of informing respondents of intended enforcement proceedings.

In view of the delegation to the staff of authority over compliance reports, one given notice of noncompliance under rule 3.61(a) -- and there is no requirement that such notice be given -- still has the possibility that the full Commission may not accept a staff interpretation of an order or may decline to seek enforcement. The Commission's August 1, 1975 determination, however, leaves neither possibility open here.

letter states, it was sent to plaintiffs "By direction of the Commission." The prospective effect of that determination is dramatic. Not only are plaintiffs faced with the virtual certainty of enforcement proceedings for post-August 1 advertising (unless the comply with the FTC's ill-specified position) and the possibility of further accrual of day-to-day penalties, but they must live with the likelihood that the government will contend that any future advertising that fails to comply with the FTC's determination is willful violation of the consent order, a contention which, if accepted, could greatly increase any eventual liability.* See United States v. J. B. Williams Co., 354 F.2d 521, 552 (S.D.N.Y. 1973) rev'd without consideration of the point, 498 F.2d 414 (2d Cir. 1974) (disregard of FTC staff's interpretation of order evidence

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* The unusual nature and consequences of the FTC's August 1 action also give the lie to the Commission's claim that a decision to entertain this action will open the federal courts to a flood of litigation concerning compliance with FTC orders. The fact is that this determination by the full Commission, as opposed to informal expressions of opinion by FTC staff members, is -- as far as we are aware -- unprecedented. Since pre-enforcement review here need not compel pre-enforcement review whenever an FTC respondent has a compliance dispute with the staff, the Court plainly is faced with a unique situation -- not the proverbial camel's nose under the tent.

of bad faith or reckless disregard). Thus, the Commission's August 1, 1975 determination, which "purport[s] to give an authoritative interpretation of a[n] order that has a direct effect on [plaintiffs'] day-to-day business[es],"* "has the characteristic of securing 'expected compliance . . ."**

In comparable circumstances other courts have held that administrative interpretations of applicable law are subject to pre-enforcement review for precisely these reasons.

In National Automatic Laundry and Cleaners Council v. Shultz, 443 F.2d 689 (D.C. Cir. 1971) the Court of Appeals held that the plaintiff trade association was entitled to pre-enforcement judicial review of an interpretation of the 1966 amendments to the Fair Labor Standards Act rendered in a letter by the Wage and Hour Administrator of the Department of Labor. It held that the Administrator's interpretation was final agency action subject to review because the interpretation by the head of the agency was presumptively final and not

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* Abbott Laboratories v. Gardner, 387 U.S. 136, 152 (1967).

** National Automatic Laundry and Cleaning Council v. Shultz, 443 F.2d 689, 697 (D.C. Cir. 1971).

subject to reconsideration, because it "has the characteristic . . . of securing 'expected compliance' [Abbott Laboratories, supra] 387 U.S. at 152 . . .)," and because it almost surely would influence the interpretation of the amendments by an enforcement court. 443 F.2d at 697-702.

To similar effect is a recent decision by Judge Gesell in the District of Columbia. Potomac Federal Corp. v. SEC, [1974-75 Transfer Binder] Fed. Sec. L. Rep. ¶ 94,704 (D. D.C. 1974). There the plaintiff requested an opinion from the SEC staff as to whether it could engage in certain activities without registering as an investment adviser under the Investment Advisers Act of 1940. 15 U.S.C. § 80b-1 et seq. Following receipt of an adverse opinion from the staff, plaintiff requested the Commission to reconsider the staff's position. The Commission thereupon authorized a letter determining that the plaintiff was not exempt from registration under the Investment Advisers Act and the plaintiff instituted an action for a declaratory judgment to review the SEC's ruling.

The SEC moved to dismiss, making much the same argument as does the FTC here. But Judge Gesell held that the SEC's determination was reviewable, stating:

> "The Commission could have refused to consider plaintiff's petition altogether, thereby letting stand the staff's opinion letter, which would not have been subject to judicial review. Kixmiller v. S.E.C. 492 F.2d 641 (D.C. Cir. 1974). See 17 C.F.R. § 202.1 (1973). Having chosen instead to examine the staff's findings and to order them reconfirmed, even under an informal procedure without oral argument, the Commission took final agency action which may be reviewed by the court if the issues are ripe and the balance of interests favors prompt adjudication. Medical Comm. for Human Rights v. S.E.C., 432 F.2d 659 (D.C. Cir. 1970), vacated as moot, 404 U.S. 403 (1972). Since the court will have before it plaintiff's detailed summary of the contested activities, which the Commission and its staff evidently deemed adequate for the issuance of a statutory interpretation, see National Automatic Laundry & Cleaning Council v. Shultz, 443 F.2d at 689 (D.C. Cir. 1971) and since judicial review at this stage would extract plaintiff from a serious legal dilemma without impairing the Commission's ability to give informal advice confined to the staff level, the court concludes that such review is appropriate." Potomac Federal Corp., supra.

The only case cited by defendants in support of the suggestion that the FTC's determination is not final agency action is Ewing v. Mytinger & Casselberry, Inc., 339 U.S. 594 (1950). There the Administrator of the Food Drug Administration found that there was "probable cause" to believe that an allegedly misbranded article being distributed by the plaintiff

was dangerous to health or fraudulently labeled and the Attorney General subsequently instituted multiple seizure proceedings under Section 304(a) of the Federal Food, Drug and Cosmetic Act, 21 U.S.C. § 334(a). The plaintiff brought an action seeking a declaration that the multiple seizure provision was unconstitutional and attacking the Administrator's finding of probable cause.

The Supreme Court sustained the multiple seizure provision and held that the probable cause finding was unreviewable. But the probable cause finding in Ewing had a far different effect than the FTC's determination here. As the Court stated, the probable cause finding:

> "has no effect in and of itself. All proceedings for the enforcement of the Act or to restrain violations of it must be brought by and in the name of the United States [citation omitted]. Whether a suit will be instituted depends on the Attorney General, not on the administrative agency. He may or may not accept the agency's recommendation." 339 U.S. at 598-99.

Indeed, the Supreme Court relied heavily on this point in distinguishing Ewing in Abbott Laboratories. 387 U.S. at 147.

Unlike the statute involved in Ewing, the Federal Trade Commission Act recently has been amended to give the

Commission the power to commence its own enforcement proceedings; the Attorney General no longer has veto power over the Commission. Thus, the Commission's determination -- unlike that of the Administrator in Ewing -- is final.

Since plaintiffs have no recourse within the FTC and are faced with action having a serious immediate impact on their business, the FTC's action is final agency action subject to review.

C. The FTC's Determination Puts Plaintiffs in an Impossible Dilemma Unless This Action is Entertained.

Unless plaintiffs obtain prompt judicial review, they must either acquiesce in the Commission's ill-defined interpretations of the order by changing their advertising -- even though plaintiffs believe in good faith that their advertising does not violate the consent orders -- or await and defend the Commission's threatened penalty action and thereby risk a judgment that also could amount to millions of dollars, even for the period from the announcement of the Commission's determination to final judgment.

We respectfully submit that neither the Constitution nor the Administrative Procedure Act permits the FTC to force

plaintiffs to run such a risk as the price of having a court determine whether the advertising they will run from this day forward complies with the order.*

The significance of the accumulating civil penalties for violation of FTC orders has already been dealt with to some extent on plaintiffs' motion for a stay. We will not repeat at length what has already been said. We submit that, even if plaintiffs are not entitled to a stay because penalties are discretionary, this Court clearly is vested with jurisdiction to decide the controversy presented by the Commission's determination. The Supreme Court's decisions in St. Regis Paper Co. v. United States, 368 U.S. 208 (1961), and in Abbott Laboratories v. Gardner, 387 U.S. 136 (1967), establish that plaintiffs are entitled to pre-enforcement review of the Commission's determination.

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* Section 10(c) of the Administrative Procedure Act, 5 U.S.C. § 704, provides in pertinent part that: "Every agency action made reviewable by statute and every final agency action for which there is no other adequate remedy in any court shall be subject to judicial review." As will appear, we submit that the risk of ever-mounting civil penalties which plaintiffs must run if they are to test the Commission's interpretation of the order as applied to their future advertising makes defense of an enforcement proceeding brought by the Commission at some time in the future an inadequate remedy.

St. Regis is merely illustrative of a time-honored principle of administrative law: One who is the object of administrative action is entitled to an opportunity to test the validity of that action in a court. In consequence, he may not be subjected, in the event his challenge fails, to the risk or threat of serious cumulative penalties for conduct prior to a judicial review. E.g., Oklahoma Operating Co. v. Love, 252 U.S. 331, 336-37 (1920) (Brandeis, J.); Ex parte Young, 209 U.S. 123, 147-48 (1908). As the Supreme Court stated in Abbott Laboratories v. Gardner, supra, 387 U.S. at 153:

> "Where the legal issue presented is fit for judicial resolution, and where a regulation [in the present case, a determination] requires an immediate and significant change in the plaintiffs' conduct of their affairs with serious penalties attached to noncompliance, access to the courts under the Administrative Procedure Act and the Declaratory Judgment Act must be permitted, absent a statutory bar or some other unusual circumstance, neither of which appears here."

Thus, St. Regis recognized that a company directed to file a report by the Federal Trade Commission must have an opportunity to contest the validity of that order. And it recognized that a penalty of $100 a day for noncompliance that would begin to

run before any opportunity for judicial review and continue to accumulate while review was sought would violate due process because it would impermissibly deter judicial review. St. Regis Paper Co., supra, 368 U.S. at 225-27.

The practical effect of the potentially large, albeit discretionary, penalties involved here is to discourage plaintiffs in seeking review in the enforcement proceeding even more emphatically than the mandatory penalties involved in St. Regis. The fact that a judge in an enforcement proceeding may consider that a defendant found to have violated an FTC order did so in good faith belief in the legality of his action is of little comfort to plaintiffs in determining whether they should comply with the FTC's determination or await an enforcement proceeding to test it. Plaintiffs have no way of knowing whether or to what extent the Court may find the presence of mitigating factors. The critical point is that, absent a stay, plaintiffs are under the threat of large penalties and that threat has a coercive effect.*

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* The fact that serious risks are present in enforcement proceedings even where any penalties may be tempered by a consideration of the defendant's good faith is well illustrated by the Second Circuit's recent decision in United State v. Ancorp National Services, Inc., 516 F.2d 198 (1975). There the court sustained imposition of civil penalties of $204,200 and a permanent injunction for violation of an FTC cease and desist order. It did so despite the fact that the defendant claimed that its conduct was not barred by the order and, in any event, was in good faith.

The courts repeatedly have recognized that the potential imposition of serious penalties improperly deters judicial review even where the amount of the penalties is discretionary. They have done so in holding unconstitutional statutes that made administrative action reviewable only in proceedings where one challenging that action was subject to discretionary penalties if unsuccessful. And they have done so in concluding that pre-enforcement review is appropriate because defense of enforcement proceedings is not an adequate remedy under the Administrative Procedure Act.

Illustrative of the former category of decisions is Oklahoma Operating Co. v. Love, 252 U.S. 331 (1920). There a state administrative body had the power to promulgate rates for laundry services. The only means of reviewing the validity of a rate order was by defending a contempt proceeding for disobedience in which the respondent, if unsuccessful, was subject to exactly the sort of discretionary sanctions involved here, although the amounts involved were far smaller -- "a penalty . . . not exceeding $500 a day" for each day of disobedience. 252 U.S. at 336-37.

The Supreme Court, speaking through Mr. Justice Brandeis, held the statute unconstitutional, stating:

> "[T]he penalties, which may possibly be imposed, if he pursues this course [review by defense of a contempt proceeding] without success, are such as might well deter even the boldest and most confident. The penalty for refusal to obey an order may be $500; and each day's continuance of the refusal after service of the order it is declared 'shall be a separate offense.' The penalty may apparently be imposed for each instance of violation of the order. * * * Obviously a judicial review beset by such deterrents does not satisfy the constitutional requirements, even if otherwise adequate, and therefore, the provisions of the acts relating to the enforcement of the rates by penalties are unconstitutional without regard to the question of the insufficiency of those rates." 252 U.S. at 336-37.

Hence, even though the amount of any penalty for contempt in Oklahoma Operating Co. was discretionary, the Supreme Court nevertheless struck down the statutory scheme on the ground that it impermissibly deterred judicial review. Accord, Ex parte Young, supra, 209 U.S. at 147-49

Illustrative of cases holding that the risk of serious discretionary penalties in an enforcement proceeding justifies pre-enforcement review is National Automatic Laundry and Cleaning Council v. Schultz, supra, 443 F.2d 689, which is directly in point here.

As we have seen, the plaintiff in that case was granted pre-enforcement review of a ruling by the Wage and Hour Administrator that coin-operated laundries were -- in the opinion of the Administrator -- subjected to the Fair Labor Standards Act by virtue of the 1966 FLSA amendments. In reaching that conclusion, the Court of Appeals for the D.C. Circuit held that the defense of enforcement proceedings -- even where good faith could be considered not merely in mitigation of penalties, but as a defense -- was not an adequate remedy under the Administrative Procedure Act.

The Court stated:

> "The granting of prompt court consideration on the basis of hardship is obviously supported by the APA's provision for review of final agency action for which there is no adequate remedy in a court. Plaintiff . . . says its members are confronted with adverse financial consequences if they comply with the Administrator's view and with consequences of serious litigation if they do not. The Government brief says the coin-operated laundries are not faced with a 'Hobson's choice' . . .
>
> "If the Administrator is correct in his interpretation of the 1966 law, the owners of coin-operated laundries who are paying their employees at rates which are in violation of the Act are subject not only to injunctive enforcement proceedings under § 17 of the Act, 29 U.S.C. § 217; and in extreme cases to criminal liability under § 16(a), 29 U.S.C. § 216(a); but also to actions for double

> damages, denominated 'liquidated damages,' brought by affected employees under §16(b), 29 U.S.C. § 216(b). The provision inserted by Congress as a meaningful penalty and deterrent cannot be passed off by Governmental lawyers as a prospect of no substantial legal consequence." 443 F.2d at 696.

The Court noted that good faith is a defense to, or is at least considered in mitigation of damages in, an action for liquidated damages, citing Section 11 of the Portal-to-Portal Pay Act of 1947, 29 U.S.C. § 260.* 443 F.2d at 697. It doubtless was aware that the employer's good faith may be considered in awarding relief in an injunctive action under 29 U.S.C. § 217. E.g., Shultz, v. Morris, 315 F. Supp. 558 567 (M. D. Ala. 1970), aff'd, 437 F.2d 896 (5th Cir. 1971); see Walling v. Nashville, Chattanooga and St. Louis Ry. Co., 330 U.S. 158 (1947). And it observed that criminal penalties are available only in "extreme cases" -- the statute speaks of willful violations -- and therefore not where the employer acts in good faith. 443 F.2d at 696.

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* 29 U.S.C. § 260 provides:

> "In any action commenced prior to or on or after May 14, 1947, to recover unpaid minimum wages, unpaid overtime compensation, or liquidated damages, under the Fair Labor Standards Act of 1938, as amended, if the employer shows to the satisfaction of the court that the act or omission giving rise to such action was in good faith and that he had reasonable grounds for believing that his act or omission was not a violation of the Fair Labor Standards Act of 1938, as amended, the court may, in its sound discretion, award no liquidated damages or award any amount thereof not to exceed the amount specified in section 216 of this title." (Emphasis added.)

Thus, National Automatic Laundry is directly applicable here. Both cases involve pre-enforcement challenges to administrative interpretations of applicable law. In both cases, unless pre-enforcement review is granted, the party seeking review must either acquiesce in the administrative interpretation at great cost, or decline to comply and run the risk of serious penalties in a subsequent enforcement proceeding. And National Automatic Laundry demonstrates that the risk of even discretionary penalties -- penalties that may be avoided or tempered if the party subject to the administrative interpretation acts in good faith -- makes defense of an enforcement proceeding in which such penalties may be imposed an inadequate remedy.

The Second Circuit appears to have recognized these principles. In Rettinger v. FTC, 392 F.2d 454 (2d Cir. 1968), the petitioner claimed that the FTC had changed its interpretation of an FTC consent order to its great disadvantage. It unsuccessfully moved in the FTC for reopening of the consent order proceeding and a modification of the order. Subsequently it filed a petition in the Court of Appeals for review of the FTC's denial of its motion, arguing that the FTC's interpretation of the consent order was incorrect and that unless review

were available, it would improperly be subjected to the risk of substantial civil penalties under Section 5(l), the same penalty statute involved here, or be forced to submit to the FTC's position.

While the Second Circuit held that it lacked jurisdiction over the petition for review,* it stated that "Rettinger offers appealing arguments" and suggested that Rettinger's remedy was to sue in the district court under the Administrative Procedure Act to obtain review of the FTC's action. 392 F.2d at 456-58. Accord, United States v. J. B. Williams Co., 354 F. Supp. 521, 552 (S.D.N.Y. 1973), rev'd without consideration of the point, 498 F.2d 414 (2d Cir. 1974). Hence, the only Second Circuit authority on this point strongly suggests that this Court has jurisdiction here.

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* It held that Section 5(b) of the Federal Trade Commission Act, 15 U.S.C. 45(b), gives the courts of appeals jurisdiction only where a reopening is granted and that review under the Administrative Procedure Act was available only in the district courts, not in the court of appeals. 392 F.2d at 456-57.

The cases relied upon by the government in support of its claim that an enforcement proceeding under Section 5(l) of the Federal Trade Commission Act is an adequate remedy are entirely inapposite.

Floersheim v. Weinburger, 346 F. Supp. 950 (D. D.C. 1972), rev'd sub nom. Floersheim v. Engman, 494 F.2d 949 (D.C. Cir. 1973), although it involved an attempt to obtain pre-enforcement review of an interpretation of a cease and desist order, differs from this case in at least one critical respect. Floersheim involved a litigated cease and desist order which had been reviewed and sustained by the United States Court of Appeals for the Ninth Circuit. Since a federal court of appeals has an "inherent authority to construe its mandate," the plaintiff in Floersheim could have petitioned the Ninth Circuit for an interpretation of the cease and desist order without incurring any risk of civil penalties for future conduct. 494 F.2d at 953-54. Thus, Floersheim had a means of obtaining review of the FTC's action without awaiting an enforcement proceeding -- and therefore had an adequate remedy precluding the action in the district court.* The present case, on the other hand,

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* Floersheim also involved an interpretation of the order by the staff, not the Commission. Hence, Floersheim had the possibility that the Commission would reject the staff's position, which is not true here.

involves a consent order, the order has not been reviewed by a Court of Appeals, and plaintiffs have no other forum to which they can turn.

The other case relied upon by the government involves the civil penalty provisions of the National Traffic and Motor Vehicle Safety Act of 1966, 15 U.S.C. § 1381 et seq., which provide that a recipient of an administrative order requiring notification of a vehicle defect is subject to a civil penalty if it does not comply. General Motors Corp. v. Volpe, 321 F. Supp. 1112 (D. Del. 1970), aff'd, 457 F.2d 922 (3d Cir. 1972).

In that case, General Motors filed suit challenging the administrative order in the district court in Delaware on November 4, 1970, and two days later, on November 6, 1970, the Attorney General filed an enforcement action in the District of Columbia. 321 F. Supp. at 1118. It was in these circumstances that the district court concluded it had jurisdiction but it should not exercise it because GM could adequately present its defense without penalty in the enforcement action. As the Court of Appeals stated, the district court "concluded that 'based on the facts before it' the enforcement action pending as of the date of its order provided GM with an adequate judicial remedy." See 457 F.2d at 923. Moreover, the

Court of Appeals pointed out "that the amount of penalties, if any, to be assessed was 'frozen' before GM filed its complaint . . ." Ibid. By contrast, in the present case, more than a month has elapsed since the August 1 determination and the government has not filed any action; further, penalties here are not "frozen" but continue to accumulate from day to day.

II

THIS COURT HAS JURISDICTION OVER THE SUBJECT MATTER

Defendants' motion is purportedly to dismiss for "lack of jurisdiction." But this Court plainly has jurisdiction over the subject matter of this action.

Plaintiffs here seek judgment declaring that the FTC's determination that plaintiffs' advertising violates the consent orders is inconsistent with the provisions of those orders and that plaintiffs are not liable to the United States for civil penalties under Section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45. There can be no serious doubt, therefore, that this is an action arising under the Federal Trade Commission Act and that this Court has subject matter jurisdiction under 28 U.S.C. §§ 1331* and 1337.** Hence it is unnecessary to consider alternative bases of jurisdiction alleged in the complaint.***

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* 28 U.S.C. § 1331(a) provides: "The district courts shall have original jurisdiction of all civil actions wherein the matter in controversy exceeds the sum or value of $10,000, exclusive of interest and costs, and arises under the Constitution, laws, or treaties of the United States."

** 28 U.S.C. § 1337 provides: "The district courts shall have original jurisdiction of any civil action or proceeding arising under any Act of Congress regulating commerce or protecting trade and commerce against restraints and monopolies."

*** The complaint further asserts that jurisdiction is founded on the Administrative Procedure Act, 5 U.S.C. §§ 702-06. There is some controversy concerning whether the APA provides an independent ground of jurisdiction to the district courts. Hart & Wechsler, The Federal Courts and The Federal System 1161 and n. 6 (2d ed. 1973).

An action for a declaratory judgment to the effect that the defendant does not have a right against the plaintiff under federal law is indisputably an action "arising under" the laws of the United States where, as here, a coercive action by the defendant on his federal claim could be brought in a federal court. Public Service Commission of Utah v. Wycoff Co., 344 U.S. 237, 248 (1952); Skelly Oil Co. v. Phillips Petroleum Co., 339 U.S. 667, 671-2 (1950). This is particularly so where the plaintiff seeks declaratory relief against action by a federal agency. As Judge Friendly has said in sustaining federal jurisdiction in an action seeking review of an NLRB determination:

> "[I]t could be said that what plaintiff is asserting is a right to be free from the Act, not a right allegedly conferred by it. But § 1337, like § 1331, speaks not of a claim created by, but of an action arising under, an act regulating commerce; it would run counter both to the language and to the policy underlying the statute to hold that the jurisdictional grant did not include an action whose sole purpose is to challenge an order of a Federal agency sought to be justified by a Federal statute. * * * [C]onsiderations of good sense support . . . permitting the sphere of application of Federal statutes to be determined by Federal courts." Empresa Hondurena de Vapores, S.A. v. McLeod, 300 F.2d 222, 226-27 (2d Cir. 1962), vacated on other grounds sub nom. McCulloch v. Sociedad Nacional de Marineros de Honduras, 372 U.S. 10 (1963) (footnote omitted).*

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* See also Dunlop v. Bachowski, 43 L.W. 4669, 4671 (U.S. June 2, 1975), Stark v. Wickard, 321 U.S. 288, 290 and n. 1 (1944); Safir v. Gibson, 417 F.2d 972, 975 (2d Cir. 1969), cert. denied, 400 U.S. 850 (1970); General Motors Corp. v. Volpe, 457 F.2d 922, 923 (3d Cir. 1972). (Stark involved 28 U.S.C.A. § 41(8) (1927), a forerunner of 28 U.S.C. § 1337, which granted jurisdiction over "all suits and proceedings arising under any law regulating commerce.")

Since the Federal Trade Commission Act is obviously both an "Act of Congress regulating commerce" and a "law . . . of the United States", jurisdiction properly rests both on 28 U.S.C. §§ 1337 and 1331.* As one court has recently held in sustaining federal jurisdiction in an action for a judgment declaring the FTC's line-of-business reporting program invalid:

> "Because this case arises under the Federal Trade Commission Act, September 26, 1914, 38 Stat. 717, as amended, 15 U.S.C.A. § 41 et seq., and the requisite amount appears to be in controversy as to each plaintiff, this Court has Federal Question Jurisdiction under 28 U.S.C.A. § 1331. Alternatively, jurisdiction under 28 U.S.C.A. § 1337 is obvious because the Federal Trade Commission Act falls clearly within the ambit of that statute. Because jurisdiction is so easily found, other bases of jurisdiction urged by plaintiffs as conferring jurisdiction will not be considered." A. O. Smith Corp. v. FTC, Civil Action No. 75-15 slip op. at 8 (D. Del. Feb. 19, 1975) (footnotes omitted).

Hence, defendants' contention that this Court lacks jurisdiction is clearly frivolous.

CONCLUSION

The FTC's authoritative and extraordinary determination that plaintiffs are in violation of the consent order creates an immediate controversy which cries out for prompt judicial resolution. Plaintiffs are entitled to have a court determine whether these determinations are correct. It is

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* The jurisdictional amount is satisfied here. See, e.g., Empresa Hondurena, supra, 300 F.2d at 226.

entitled to such a determination without being exposed to the risk of serious and evermounting penalties that may be running at this moment and -- barring prompt judicial intervention -- may continue to run for an indefinite period until the FTC eventually brings an enforcement proceeding. In short, the FTC's determination "puts [plaintiffs] in a position that it was the very purpose of the Declaratory Judgment Act to ameliorate." Abbott Laboratories v. Gardner, 387 U.S. 136, 152 (1967). This Court therefore should entertain this action.

Respectfully submitted,

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