

Retail Tracking Cos. Now Face Emboldened FTC

By **Allison Grande**

Law360, New York (April 27, 2015, 7:51 PM ET) -- In bringing its first action against a retail tracking company Thursday, a divided Federal Trade Commission sent a warning that it expects companies to live up to privacy promises regardless of the size of their business or the novelty of their technology.

The settlement between Nomi Technologies Inc. and the FTC stems from the regulator's assertions that the company — which develops technology that allows retailers to track customers in their stores — misled consumers with promises that it would provide a mechanism for consumers to opt-out of tracking and that consumers would be informed when locations were using Nomi's tracking services.

While the enforcement action marks the first time that the commission has brought a complaint against a company in the emerging mobile device tracking industry, the case hinged on the well-established premise that companies must live up to their privacy promises. This is a standard to which the commission has repeatedly held companies in a wide range of industries under Section 5 of the FTC Act.

“The action reinforces the notion, which is an important one, that if you promise something, the FTC is going to hold you to it,” Foley Hoag LLP privacy and data security practice co-chair Colin Zick said. “It's sending a message to the rest of the marketplace to go back and look at their policies and make sure that they match what their activities are, because if they don't, that's a problem.”

The settlement is based on a fairly garden-variety deception claim, which should not be surprising to businesses that have been kept track of the commission's privacy enforcement activities. The application of the principle to the mobile tracking industry, however, is significant due to the relative lack of standards and guidance governing the collection and retention of tracking data.

In October 2013, a group of data analytics companies including Euclid Inc. and Mexia Interactive Inc. published a first-of-its-kind code of conduct for tracking retail customers' in-store movements, but industry members are not bound to follow it, attorneys noted.

“The rules of the road are not entirely clear for the industry at the moment,” said Yaron Dori, the co-chair of Covington & Burling LLP's communications and media practice group.

Although the commission's action against Nomi didn't go so far as to set notice and consent requirements for retail trackers, it did help to provide some insight into what the industry needs to do to avoid the regulator's ire.

“This case demonstrates the continued interest of the FTC in addressing cutting-edge technology issues to protect consumers, as well as the potential concerns to innovation from these efforts,” Wiley Rein LLP privacy group chair Kirk Nahra said. “Every start-up thinking about any kind of tracking technology must understand how the FTC looks at these cases and be prepared to either address these concerns or face a legal fight.”

One well-established privacy principle that the commission seems to be suggesting through its action that the mobile device tracking ecosystem adopt is privacy by design, or the concept that privacy be considered and built into products and services at the outset of their life cycle, attorneys say.

"Here, the FTC is mandating an actual systems architecture change, rather than mandating disclosures or other communications that leave it to consumers to choose whether they shop where the system is used or not," said Craig Cardon, co-chair of Sheppard Mullin Richter & Hampton LLP's privacy and data security group. “Emotionally, this was not a terribly difficult factual scenario in which to wade into mandating privacy by design, but we’ll have to watch how far into the waves the FTC decides to venture here.”

The FTC first signaled its interest in mobile device tracking last February, when it held a seminar that explored the interplay between the importance of allowing the emerging industry to grow and innovate and the potential risks to consumers of allowing tracking practices to expand organically without regulation.

The tension between the need for innovation and possible privacy risks significantly factored into the settlement announced Thursday.

While three of the FTC commissioners believed that requiring a start-up like Nomi to overhaul the way that it communicates with consumers was reasonable, not all of their colleagues agreed with this approach. The pair of dissents from the commission could give companies some footing to push back against the regulator's aggressive enforcement of emerging technologies.

Commissioners Maureen Ohlhausen and Joshua Wright penned separate dissents voicing concerns with both the potential impact that such a requirement could have on smaller companies' ability to innovate, as well as the majority's assertion that the alleged violation was worth pursuing.

Specifically, the commissioners argued that Nomi's express promise to provide an in-store opt-out was not material because consumers were able to opt out online as promised in the privacy policy, and that, in any event, the commission should not have brought the action because it would deter the industry from adopting business practices that benefit consumers.

Both dissents also noted that even though Nomi's privacy policy may have been partially inaccurate, the failure of the company to provide an in-store opt-out “harmed no consumers,” and the commission should have refrained from bringing the case because its limited resources should be focused on cases that involve actual consumer harm.

“We should not apply a de facto strict liability approach to a young company that attempted to go above and beyond its legal obligation to protect consumers but, in doing so, erred without benefiting itself,” Ohlhausen wrote. “I fear the majority’s decision in this case encourages companies to do only the bare minimum on privacy, ultimately leaving consumers worse off.”

The argument that start-ups shouldn't be held to as strict of a standard as more established businesses may have trouble gaining widespread traction, due to the potential that the approach would create a loophole that could be exploited by larger companies that outsource their practices to smaller companies. Businesses may find more success in latching onto the commissioners' assertion that actions should not be brought unless actual consumer harm can be demonstrated.

The lack of harm argument is regularly used by businesses — usually with a fair amount of success — to fend off class actions where consumers allege a data privacy violation but can't show a monetary or other tangible loss or injury, and the endorsement of the argument by the two commissioners could prove useful in combating not only consumers' claims, but also FTC allegations that may be perceived as overly broad.

“If the FTC cracks down too hard, the industry might fight back and argue that the commission is being completely unreasonable in using its very broad mandate under the FTC Act to regulate this space,” Zick said. “A trade association could use the dissents to show that this practice of prosecuting companies instead of dealing with the issue administratively when consumers are not hurt is a problem that is going to stifle innovation.”

In finding the right balance between showing that it is serious about enforcement and sending the message that it doesn't want to stifle innovation, the FTC could potentially look at how other state and federal agencies have handled such issues, including the approach taken by the U.S. Department of Health and Human Services' Office of Civil Rights when it first began enforcing the Health Insurance Portability and Accountability Act, Zick added.

“When HIPAA was first passed, OCR waited a long time before bringing enforcement actions and instead sent out notices about problems first because it realized that compliance would be difficult and that if it brought down a very aggressive enforcement regime, there would be calls to revoke HIPAA,” he said. “That approach seems to work out quite well, and there is certainly no one today that is accusing OCR of being soft on enforcement and penalties.”

While it is uncertain what step the FTC will take next in its nascent regulation of the budding mobile tracking industry, attorneys agree that the commission will not be able to escape having to grapple with the competing interests of protecting consumer privacy while giving businesses room to grow.

“What we can expect to see is a continuing debate between the benefits of technology, for both businesses and consumers, as well as the risk to innovation and the potential consumer confusion (and, sometimes) harm from these activities,” Nahra said.

Nomi is represented by Lydia B. Parnes of Wilson Sonsini Goodrich & Rosati PC.

The FTC is represented by its attorneys Amanda Koulousias and Jacqueline Connor.

The case is In the Matter of Nomi Technologies Inc., file number 132-3251, before the Federal Trade Commission.

--Editing by Sarah Golin and Philip Shea.