How Much Is Too Much? Price-Gouging Under the Defense Production Act

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The escalation of the COVID-19 crisis throughout the country has brought stories of front-line health workers and everyday people assisting one another in extraordinary ways. Unfortunately, it has also provided examples of others trying to take unfair advantage of the circumstances for their own economic gain. Federal and state authorities have responded by stepping up efforts to enforce criminal laws targeting hoarding and price-gouging. To that end, on March 24, Attorney General William Barr issued a memorandum to all federal law enforcement agencies making clear that the U.S. government "will not tolerate bad actors who treat the crisis as an opportunity to get rich quick," and directed the creation of a task force dedicated to addressing pandemic-related "market manipulation, hoarding, and price-gouging" (the "March 24 Memorandum").[1] This article will examine the due process concerns raised by the government's use of the Defense Production Act of 1950 (DPA) to criminally prosecute alleged price-gouging activity.

Background

Price-gouging involves a supplier of a product or service taking wrongful advantage of a national or local emergency by charging excessive prices. In the absence of a specific federal price-gouging statute, the Department of Justice (DOJ) has relied on the DPA, together with other general fraud statutes, in bringing charges during the pandemic caused by COVID-19. Section 102 of the DPA is an anti-hoarding statute, providing that

> no person shall accumulate (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 (emphasis added).[2]

Section 103 makes willful violations of the statute a misdemeanor with maximum penalties of one-year incarceration and a $10,000 fine.[3]

The DOJ's newly-established task force was directed to "develop effective enforcement measures" and "coordinate nationwide investigation and prosecution" of conduct in violation of the DPA. As part of the initiative, each United States Attorney's office has been told to designate an "experienced" prosecutor as part of the task force.[4] In conjunction with the March 24 Memorandum, President Trump issued an Executive Order, pursuant to Section 102 of the DPA, aimed at ensuring the availability of items "such as personal protective equipment and sanitizing and disinfecting products," and authorizing the Secretary of Health and Human Services to designate such materials as protected by the DPA.[5]

While the DOJ is dedicating significant resources to the enforcement of the federal statute, there remains little guidance upon which a potential supplier can rely to stay within the bounds of the law. For example, the DPA nowhere provides a definition or further gloss on the meaning of "in excess of prevailing market prices." Nor have the federal courts provided a clear interpretation of the phrase. Under these circumstances, there is scant notice available to those sellers during the pandemic who want to avoid triggering price-gouging scrutiny. While the DPA's applicability may be clear in extreme cases of price inflation (*i.e.,* "you know it when you see it"), there remains no objective guidance for those situations that fall at the margins.

The Due Process Clause requires that "no individual be forced to speculate, at peril of indictment, whether his [or her] conduct is prohibited."[6] The absence of any clear direction as to what constitutes price-gouging under the DPA implicates those Constitutional concerns. If a responsible seller of personal protective equipment wants to raise prices—perhaps because his or her suppliers have already done so, or because of increased delivery expenses in today's increasingly contactless environment, or maybe because the seller needs the additional income to pay furloughed employees—where is the line that the responsible seller should not cross? Can that seller make a better return on the goods than it would have before the pandemic because it had the foresight (or luck) to have developed a large inventory even before the emergence of the novel coronavirus? In other words, how much is too much?

Recent Federal Enforcement Efforts

These issues are likely to be addressed in the context of recent federal prosecutions. For example, two criminal complaints filed in the Eastern District of New York charge violations of the DPA: Complaint, *United States v. Singh*, (E.D.N.Y. Apr. 24, 2020) (No. 20-MJ-326) and Complaint, *United States v. Kent Bulloch, et al.*, (E.D.N.Y. Apr. 27, 2020) (No. 20-MJ-327). In the *Singh* complaint, the government alleges that a Long Island business owner resold N-95 respirators, facemasks, and clinical-grade disinfectants through his retail company "at prices in excess of prevailing market prices."[7] The investigation described in the complaint determined that the defendant had sold these essential products at markups ranging between 59% and 1,328% above his per-unit cost, although most of the markups were in the 100-200% range. In *Bulloch*, the defendants are alleged to have taken part in a scheme that included, among other things, inducing customers to purchase large numbers of non-existent respirators and face masks, along with selling personal protective equipment, respirators and surgical masks at over 200% of prevailing prices.[8]

Tracking the language of the DPA, both complaints allege that materials were being resold or attempted to be resold at "prices in excess of prevailing market prices" (*e.g.*, the phrase that remains further undefined by the federal statute). For example, the DPA offers no guidance as to how (if at all) a seller, in complying with the statute, should factor in additional costs that the seller may have incurred from distributors and/or manufacturers—a more than likely circumstance during a period of national crisis and potentially limited availability of supplies.

In *Singh*, the DOJ asserts that the DPA applies because the defendant resold essential materials at "huge markups."[9] But that vague phrase again offers no real help to the lack-of-notice concern. The complaint also analyzes the defendant's pricing as a percentage above his cost, while not actually discussing "prevailing market prices." While there is presumably some relationship between a given seller's cost and the prevailing market price, nothing in the statute addresses that relationship sufficient to guide sellers in setting prices during a national crisis. Presumably, 1,328% would qualify as a "huge markup" that should not be allowable under almost any circumstance, but is a price 59% above unit cost excessive at all, let alone so obviously excessive that it overcomes any constitutional notice concerns?[10]

The *Bulloch* Complaint, on the other hand, addresses the issue primarily by examining the defendants' price of items "compared to their price in the market prior to the COVID-19 pandemic."[11] In one instance, masks were allegedly sold at prices 300-400% greater than their prices prior to the pandemic.[12] This analysis seems to address more closely the language found

in the DPA. Nevertheless, it does not answer what percentage above previous pricing qualifies as being "excess[ive]," how to factor in increased costs, or the appropriate means of determining prevailing market pricing (*e.g.*, is it the average market price pre-crisis, or just the highest price that was on the market at the time?). Along the same lines, the DPA does not account for the fact that pre-pandemic pricing may differ greatly among geographic markets. Should a seller face potential criminal prosecution if his or her pricing exceeds the market price prior to a national emergency by under 5% or 10%? How about 20%?

While the recent prosecutions under the DPA arguably reflect alleged conduct at the egregious end of the spectrum, the foregoing suggests that in less obvious cases, worthy challenges to the vagueness of the statute will be brought under the Due Process Clause.[13] Similarly, under the rule of lenity, courts may wrestle with motions seeking dismissal of charges in circumstances where reasonable doubt exists that a given defendant's pricing fell within conduct prohibited by the DPA. *See Ladner v. United States*, 358 U.S. 169, 178 (1958) ("lenity means that the Court will not interpret a federal criminal statute so as to increase the penalty that it places on an individual when such an interpretation [is] no more than a guess as to what Congress intended."); *Lockhart v. United States*, 136 S. Ct. 958, 968 (2016) (ambiguity should be resolved in favor of the defendant only "when the ordinary canons of statutory construction have revealed no satisfactory construction.").

State Anti-Price-Gouging Laws

In the absence of an established federal anti-price-gouging statute, states have enacted their own laws prohibiting excessive price hikes during times of crisis. These statutes primarily provide state attorneys general with civil remedies, although in some instances criminal prosecution is available as well. While the specific statutory language defining wrongful conduct varies from state to state, the statutes primarily fall into two categories, both of which seemingly offer better guidance to sellers than the federal statute. For example, some states, such as California and New Jersey, along with the District of Columbia, have set a specific percentage above market rates that sellers cannot exceed when setting prices for consumer goods or services during an emergency. Other states, including New York, Florida, and Texas, do not rely on specific percentages but rather a more subjective "gross disparity" from the market standard. These state statutes will generally identify the scope of goods and services covered by the law, as well as the exceptions or defenses that apply to mitigate the general standard. A review of several of these state provisions will both highlight the constitutional notice prob-

lem presented by the DPA and inform potentially useful modifications to the federal statute.

California (one of the few states that provides for a criminal remedy) prohibits selling or offering to sell items or services for more than 10% above the price charged by that seller for those goods and services immediately prior to the proclamation or declaration of an emergency. The prohibition applies to items such as food, goods, or services used for emergency cleanup, emergency supplies, and medical supplies. Price increases are not actionable if the increase is directly attributable to additional costs imposed by a supplier or for labor or materials used to provide the service. Also, if a business was offering an item for sale at a reduced price immediately before the emergency, it may nevertheless use the price at which it normally sold the item to calculate the statute's limit on the price increase. Violations of the provision are misdemeanors.[14]

Similarly, District of Columbia Code 28-4102 prohibits charging greater than the "normal average retail price" for merchandise or services, which is defined as "not more than 10% more than the price at which similar services were sold or offered" in the area in the 90 days preceding the emergency. In the case of merchandise, it is the price reflecting the same percentage mark-up over the wholesale cost for similar merchandise prior to the emergency.[15]

New Jersey's price-gouging statute also prohibits selling covered items at more than 10% of the price that was offered in the usual course of business just prior to the emergency. The statute allows for an exception when the seller's costs have increased due to supplier or other increases attributable to the state of emergency.[16]

Florida prohibits selling essential commodities at an "unconscionable price," further defined as a gross disparity with the average price the seller charged in the usual course of business (or was readily obtainable in the area) during the 30-day period immediately prior to the state of emergency. A price is not unconscionable if the price increase is attributable to additional costs incurred in providing the commodity. Approval of the price by an appropriate government agency is another exception to the law.[17]

New York's statutory prohibition covers items sold at an "unconscionably excessive price," which—similar to Florida—is defined as a gross disparity between the price of the goods or services and the price at which they were sold by the defendant in the usual course of business (or readily obtainable in the area) immediately prior to the market disruption.[18] The prohibition broadly applies to "consumer goods and services used, bought or rendered primarily for personal, family, or household purposes."[19] Evidence of additional costs offers a defense.[20]

Finally, Texas prohibits selling "at an exorbitant or excessive price" and identifies no specific exceptions or defenses, largely echoing the federal statute.[21]

As noted above, these state statutes primarily provide for civil, not criminal, penalties. And while there have been vagueness/due-process challenges to certain of these state statutes, they not surprisingly arise in the context of civil enforcement of a statute. For example, in *People v. Two Wheel Corp.*, an intermediate appellate court upheld New York's price-gouging statute against an argument of unconstitutional vagueness.[22] The New York Attorney General had charged the defendant with selling generators at "unconscionably excessive" prices during a widespread power outage.[23] While the court recognized that "no fixed rate or percentage of permissible price increase [was] supplied" in the statute, the standards set forth nevertheless were determined "sufficient to apprise the [sellers] that their gross price increases of as much as 67 percent during the power outage were prohibited unless they were attributable to additional costs imposed by the suppliers of the generators."[24] *See also State ex rel. Hood v. Louisville Tire Ctr., Inc.*, 55 So. 3d 1068, 1073 (Miss. 2011) (Mississippi statute's language referring to pricing in the "same market area" and "at or immediately before" an emergency was not impermissibly vague and thus did not violate the Due Process Clause).

Again, these state decisions were in cases concerning *civil* enforcement of price-gouging statutes. Thus, the courts did not have to address the possibility—and more detrimental consequence—that a defendant could be incarcerated for running afoul of an unconstitutionally vague statute. Moreover, decisions like these seemingly offer little help to those responsible sellers who want to increase pricing at a time of national emergency while avoiding potential prosecution under the DPA.

Conclusion

There is no debate that the DPA and other state statutes aimed at curbing price gouging serve an important purpose, particularly during times of national crisis. Nevertheless, the lack of guidance offered by the DPA as to when a seller (and potential defendant) has marked up a good or service "in excess of prevailing market prices" raises a significant due-process concern. Some state statutes address this concern by providing specific percentages, above which price increases are deemed in violation of the law, while often allowing for the possibility that higher increases can be justified if supply costs have gone up as well. A fair enforcement regime under the DPA would seem to demand similar, more specific guidelines.[25] This concern is even more acute given the recent step-up in criminal prosecutions under the

statute during the COVID-19 crisis.

Deciding what specific parameters should apply is, of course, another issue. For example, those states that have set a definite limit often use a standard that bars any increase over 10% from what the seller charged (or was available in the market) immediately prior to an emergency's onset. Whether that 10% standard or a different one is appropriate under the DPA should be the subject of an analysis that carefully balances the need to root out wrongful market behavior with the interest in sufficiently incentivizing sellers to remain as market providers of what may often be vital goods or services during a time of crisis. Currently, with no real standard to guide them, those sellers remain in the dark as to "how much is too much," and face the very real risk of criminal prosecution without constitutionally fair notice.

Endnotes

1 Office of the Attorney General, *Memorandum for All Heads of Department Components and Law Enforcement Agencies* (Mar. 24, 2020), https://www.justice.gov/file/1262776/download, at 1.

2 50 U.S.C. § 4512.

3 *Id.* § 4513.

4 March 24 Memorandum, *supra*.

5 Exec. Order No. 13,910, 85 Fed. Reg. 17,001 (Mar. 23, 2020), https://www.federalregister.gov/documents/2020/03/26/2020-06478/preventing-hoarding-of-health-and-medical-resources-to-respond-to-the-spread-of-covid-19.

6 *Dunn v. United States*, 442 U.S. 100, 112 (1979) (citing *Grayned v. City of Rockford*, 408 U.S. 104, 108 [1972]).

7 *Singh*, No. 20-MJ-326, ECF Dkt. No. 1 at 1.

8 *See Bulloch*, No. 20-MJ-327, ECF Dkt. No. 1 ("*Bulloch* Complaint").

9 Department of Justice, U.S. Attorney's Office, E.D.N.Y., *Long Island Man Charged Under Defense Production Act with Hoarding and Price-Gouging of Scarce Personal Protective Equipment* (Apr. 24, 2020), https://www.justice.gov/usao-edny/pr/long-island-man-charged-under-defense-production-act-hoarding-and-price-gouging-scarc-0.

10 Of course, if unconstitutionally vague, the DPA would be unenforceable under any circumstances, no matter the size of a seller's markup.

11 *Bulloch* Complaint at 23.

12 *Id.*

13 For example, in *United States v. L. Cohen Grocery Co.,* 255 U.S. 81, (1921), the Supreme Court upheld a lower court's voiding of the Lever Act, a federal statute criminalizing under certain circumstances the willful making of "any unjust or unreasonable rate or charge." The Court found the language of the statute lacked "an ascertainable standard of guilt" adequate to inform persons charged under the

statute of the "nature and cause of the accusation against them." *Id.* at 89. *See also, United States v. National Dairy Products,* 372 U.S. 29, 37 (1963) (Black, J., dissenting) ("The rule established by [*L. Cohen Grocery Co.*] has been often followed.")

14 Cal. Penal Code § 396(b)-(h).

15 D.C. Code § 28-4101(2).

16 N.J. Stat. Ann. § 56:8-108.

17 Fla. Stat. Ann. § 501.160.

18 N.Y. Gen. Bus. Law § 396-r(2), (3).

19 *Id.* § 396-r(2).

20 *Id.* § 396-r(3)(c).

21 Tex. Bus. & Com. Code. Ann. § 17.46(b)(27).

22 128 A.D.2d 507, 510 (N.Y. App. Div. 1987). The vagueness argument was not further appealed, and the Appellate Division decision was affirmed on other grounds. *See* 71 N.Y.2d 693, 697-700 (1988).

23 *Id.* at 508-09.

24 *Id.* at 510.

25 Since the March 24 Memorandum, several bills have been introduced in Congress aimed at price-gouging that vary in their language. *See, e.g.,* H.R. 6472 (a bill entitled the "COVID-19 Price Gouging Prevention Act" would give additional enforcement powers to the FTC and state attorneys general to prevent the sale of a "good or service" at an "unconscionably excessive" price for the duration of a public health emergency due to COVID-19) and H.R. 6450 (prohibiting price increases on consumer goods and services of more than 10% during a declared emergency). Ballard Spahr LLP, *Congress Considering New Federal Price Gouging Laws* (Apr. 10, 2020), https://www.ballardspahr.com/alertspublications/legalalerts/2020-04-10-congress-considering-new-federal-price-gouging-laws.

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