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## LEARNING OBJECTIVES

- **LO1** To examine how advertising is regulated, including the role and function of various regulatory agencies.
- **LO2** To examine self-regulation of advertising and evaluate its effectiveness.
- **LO3** To consider how advertising is regulated by federal and state government agencies, including the Federal Trade Commission.
- **LO4** To examine rules and regulations that affect sales promotion, direct marketing, and marketing on the Internet.

# 22 Regulation of Advertising and Promotion

## PRODUCT PLACEMENTS MAY FACE REGULATION

Product placements are nearly as old as television itself as they date back to the early days of TV when the hosts of popular shows such as Milton Berle's *Texaco Star Theater* and Mutual of Omaha's *Wild Kingdom* would promote the sponsor's products. During his tenure as host of *General Electric Theater* from 1954 to 1962, future United States President Ronald Reagan would commonly plug the show's sponsor in introductions, segues, and closing comments by delivering a friendly message about the company that usually ended with the tagline "Progress is our most important product." The mentioning of these companies was never considered a problem because they sponsored the production of the program and were very aboveboard in promoting themselves. However, the number of product placements has increased dramatically over the years and the way brands are integrated into TV shows has also changed, which has led to concern over the practice by various consumer advocacy groups.

Unlike some countries, the United States does not prohibit product placements in the broadcast or motion picture industries. However, the use of undisclosed commercial messages in broadcasting has been regulated for more than 75 years as Section 317 of the Communications Act of 1934, which requires broadcasters to disclose "any money, service, or valuable consideration" that is paid to, or promised to, or charged by the broadcaster in exchange for product placements. However, broadcasters do not have to disclose product placements when they are offered without charge or for a nominal fee. The Federal Communications Commission (FCC) is the governmental agency that has the responsibility to prescribe the appropriate rules and regulations needed to carry out the sponsorship identification requirements. The FCC has basically interpreted the purpose of Section 317 of the Act to be that the viewers in the TV audience must be informed that what they are viewing has been paid for and that the entity paying for the broadcast must be clearly identifiable.

While there are a number of requirements and conditions associated with Section 317, broadcasters usually have been considered in compliance with the regulation by placing an announcement in the credits at the beginning or end of the program stating that "promotion consideration paid for by (name of sponsor)" which remains on the screen long enough to be read or heard by the average viewer. While this single disclosure has been the common practice in the industry, a number of consumer groups have argued that more stringent regulation is needed. They argue that product placements have become more prevalent and also more stealthy in nature as marketers work with producers of TV shows to integrate their brands into their programs. Product placements have definitely become more ubiquitous according to numbers from Nielsen IAG which tracks the number of show segments in which a brand placement appears. In 2009 the number of product placements in prime time increased by 8 percent over 2008. The television programs with the most product placements included *The Jay Leno Show* (1,015), *The Biggest Loser* (704), and *American Idol* (553) while the top brands with TV product placements were AT&T, Coca-Cola, Apple, and Ford.

Although the FCC has enforcement authority against certain forms of product placement, some consumer advocacy groups have argued that for more regulation of the practice is needed. Those expressing concern over product placements range from consumer advocacy groups to pediatricians who are seeking to protect children from the promotion of sugary cereals. One of the leading critics of product placement is Commercial Alert, a nonprofit organization cofounded by consumer activist Ralph Nader, which argues that product placements are inherently deceptive because so many viewers do not realize they are, in fact, advertisements. Another activist group that opposes product placements is Free Press. Corie Wright, an attorney and policy advisor for the group, argues that the practice is deceptive, stating that "Product placements don't allow us to have the usual veil of skepticism we have when we watch a standard commercial." Critics are concerned not just by the prevalence of products appearing in shows but also by the various forms of integration whereby brands are actually written into plotlines such as a *30 Rock* episode in which Alec Baldwin sang the praises of Cisco teleconferencing equipment, or Subway collaborating with producers of *Chuck* and *The Biggest Loser* to work the brand into show plots. The critics argue that the promotion of brands is no longer confined to the commercial breaks, and commercials and content are becoming one and the same, and difficult to distinguish from one another.

Critics are calling upon the FCC to require the TV networks to disclose product placements by using some form of onscreen notification system. Proposals range from requiring programs to run text along the bottom of the screen when a product appears in a scene, to using a flashing red light to alert viewers that a marketer is promoting a product. Some point to a system that is being proposed in the United Kingdom, which plans to begin allowing product placements for the first time in 2011. The European Union approved their use in 2009 but left it up to the individual countries to make their own rules. Regulators in the U.K. are calling for the use of an onscreen symbol, perhaps in the form of a large "P" at the beginning and end of programs to alert audiences to the paid messages embedded in the shows they are about to watch or have just seen.

In 2008 the FCC published a "Notice of Inquiry" and a "Notice of Proposed Rulemaking" to seek public comment on the call for more stringent regulations. The FCC is proposing more frequent and more obvious disclosures during programming with product placements, extension of product integration regulations to cable television, and additional restrictions for children's programming. While little has been done thus far, the television industry is already up in arms as are the marketers who use product placements. Tony Pace, Subway's chief marketing officer opposes disclosures except at the end of a program arguing that "We'd rather seem like a natural part of the show than punch the viewer in the nose with a message like, 'Hey, this is paid for." Producers of television programs as well as the major broadcast and cable networks are also concerned as paid product placements are an important source of revenue that help underwrite the costs of TV shows. Marketers also view product placements as a way to deliver branding messages to consumers who are becoming more difficult to reach during commercial breaks, particularly when they record a show on a DVR and fast-forward through the commercials when watching it.

Proponents of product placements also point to the fact that the Federal Trade Commission, which has broad jurisdiction over advertising practices, has declined to regulate their use. The FTC position has been that they have no basis for doing so since product placements rarely make objective, material claims about a product when used within a show. The FTC has also stated that it would be difficult to develop a "one-size-fits-all" rule or guide that could effectively regulate product placements. Proponents note that the FTC's position supports their argument that further restrictions on these placements are unnecessary since they are not causing any injury to consumers.

Ultimately, it may be consumers who decide the fate of product placements. The time may come when we yearn for a return to the traditional model of television programs whereby ads appear during commercial breaks and we can decide whether we want to watch them. However, until then, it is likely that marketers will continue to look for clever ways to integrate their brands into the TV shows and leave it up to the consumer to figure out why they are there.

Sources: Emma Hall, "U.K. Proposes Product Placement Alert," *Advertising Age*, June 30 2010, http://adage.com/print?article_id=144751; Brian Steinberg, "Don't Like Product Placement? Here's Why It's Your Fault," *Advertising Age*, February 11, 2010, http://adage.com/print?article_id=142069; Daniel Hertzberg, "Blasting Away at Product Placement, *BusinessWeek*, October 26, 2010, p. 60; Richard J. Wegener, "Product Placement & Government Regulation: FCC vs. FTC," paper presented at Promotional Marketing Association's 30th Annual Promotion Marketing Conference, November 20, 2008.

LO 22-1

Suppose you are the advertising manager for a consumer-products company and have just reviewed a new commercial your agency created. You are very excited about the ad. It presents new claims about your brand's superiority that should help differentiate it from the competition. However, before you approve the commercial you need answers. Are the claims verifiable? Did researchers use proper procedures to collect and analyze the data and present the findings? Do research results support the claims? Were the right people used in the study? Could any conditions have biased the results?

Before approving the commercial, you have it reviewed by your company's legal department and by your agency's attorneys. If both reviews are acceptable, you send the ad to the major networks, which have their censors examine it. They may ask for more information or send the ad back for modification. (No commercial can run without approval from a network's Standards and Practices Department.)

Even after approval and airing, your commercial is still subject to scrutiny from such state and federal regulatory agencies as the state attorney general's office and the Federal Trade Commission. Individual consumers or competitors who find the ad misleading or have other concerns may file a complaint with the National Advertising Division of the Council of Better Business Bureaus. Finally, disparaged competitors may sue if they believe your ad distorts the facts and misleads consumers. If you lose the litigation, your company may have to retract the claims and pay the competitor damages, sometimes running into millions of dollars.

After considering all these regulatory issues, you must ask yourself if the new ad can meet all these challenges and is worth the risk. Maybe you ought to continue with the old approach that made no specific claims and simply said your brand was great.

Regulatory concerns can play a major role in the advertising decision-making process. Advertisers operate in a complex environment of local, state, and federal rules and regulations. Additionally, a number of advertising and business-sponsored associations, consumer groups and organizations, and the media attempt to promote honest, truthful, and tasteful advertising through their own self-regulatory programs and guidelines. The legal and regulatory aspects of advertising are very complex. Many parties are concerned about the nature and content of advertising and its potential to offend, exploit, mislead, and/or deceive consumers.

Advertising has also become increasingly important in product liability litigation involving products that are associated with consumer injuries. In many of these cases the courts have been willing to consider the impact of advertising on behavior of consumers that leads to injury-causing situations. Thus advertisers must avoid certain practices and proactively engage in others to ensure that their ads are comprehended correctly and do not misrepresent their products or services.[1]

Numerous guidelines, rules, regulations, and laws constrain and restrict advertising. These regulations primarily influence individual advertisers, but they can also affect advertising for an entire industry. For example, cigarette advertising was banned from the broadcast media in 1970, and many groups are pushing for a total ban on the advertising of tobacco products.[2] Legislation now being considered would further restrict the advertising of alcoholic beverages, including beer and wine.[3] Advertising is controlled by internal self-regulation and by external state and federal regulatory agencies such as the Federal Trade Commission (FTC), the Federal Communications Commission (FCC), the Food and Drug Administration (FDA), and the U.S. Postal Service. And recently state attorneys general have become more active in advertising regulation. While only government agencies (federal, state, and local) have the force of law, most advertisers also abide by the guidelines and decisions of internal regulatory bodies. In fact, internal regulation from such groups as the media and the National Advertising Review Board probably has more influence on advertisers' day-to-day operations and decision making than government rules and regulations.

Decision makers on both the client and agency side must be knowledgeable about these regulatory groups, including the intent of their efforts, how they operate, and how they influence and affect advertising and other promotional mix elements. In this chapter, we examine the major sources of advertising regulation, including efforts by the industry at voluntary self-regulation and external regulation by government agencies. We also examine regulations involving sales promotion, direct marketing, and marketing on the Internet.

# SELF-REGULATION

LO 22-2

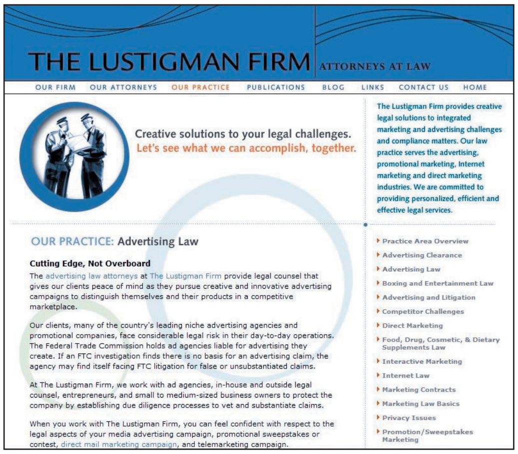
For many years, the advertising industry has practiced and promoted voluntary **self-regulation**. Most advertisers, their agencies, and the media recognize the importance of maintaining consumer trust and confidence. Advertisers also see self-regulation as a way to limit government interference, which, they believe, results in more stringent and troublesome regulations. Self-regulation and control of advertising emanate from all segments of the advertising industry, including individual advertisers and their agencies, business and advertising associations, and the media.

## Self-Regulation by Advertisers and Agencies

Self-regulation begins with the interaction of client and agency when creative ideas are generated and submitted for consideration. Most companies have specific guidelines, standards, and policies to which their ads must adhere. Recognizing that their ads reflect on the company, advertisers carefully scrutinize all messages to ensure they are consistent with the image the firm wishes to project. Companies also review their ads to be sure any claims made are reasonable and verifiable and do not mislead or deceive consumers. Ads are usually examined by corporate attorneys to avoid potential legal problems and their accompanying time, expense, negative publicity, and embarrassment.

Internal control and regulation also come from advertising agencies. Most have standards regarding the type of advertising they either want or are willing to produce, and they try to avoid ads that might be offensive or misleading. Most agencies will ask their clients to provide verification or support for claims the clients might want to make in their advertising and will make sure that adequate documentation or substantiation is available. However, agencies will also take formal steps to protect themselves from legal and ethical perils through agency-client contracts. For example, many liability issues are handled in these contracts. Agencies generally use information provided by clients for advertising claims, and in standard contracts the agency is protected from suits involving the accuracy of those claims. Contracts will also absolve the agency of responsibility if something goes wrong with the advertised product and consumers suffer damages or injury or other product liability claims arise.[4] However, agencies have been held legally responsible for fraudulent or deceptive claims and in some cases have been fined when their clients were found guilty of engaging in deceptive advertising.[5] Many agencies have a creative review board or panel composed of experienced personnel who examine ads for content and execution as well as for their potential to be perceived as offensive, misleading, and/or deceptive. Most agencies also employ or retain lawyers who review the ads for potential legal problems. Exhibit 22–1 shows an ad for a legal firm specializing in advertising and integrated marketing communications law.

**EXHIBIT 22–1**
The Lustigman firm specializes advertising and integrated marketing communications law




## Self-Regulation by Trade Associations

Like advertisers and their agencies, many industries have also developed self-regulatory programs. This is particularly true in industries whose advertising is prone to controversy, such as liquor and alcoholic beverages, drugs, and various products marketed to children. Many trade and industry associations develop their own advertising guidelines or codes that member companies are expected to abide by.

The Wine Institute, the U.S. Brewers Association, and the Distilled Spirits Council of the United States all have guidelines that member companies are supposed to follow in advertising alcoholic beverages.[6] No specific law prohibits the advertising of hard liquor on radio or television. However, such advertising was effectively

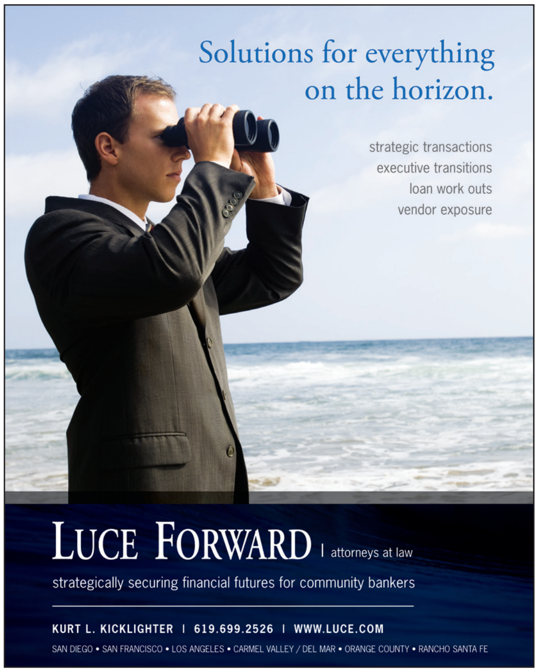



**EXHIBIT 22–2**
Advertising by lawyers has become common

banned for over five decades as a result of a code provision by the National Association of Broadcasters and by agreement of liquor manufacturers and their self-governing body, the Distilled Spirits Council (DISCUS). However, in November 1996, DISCUS amended its code of good practice and overturned its self-imposed ban on broadcast advertising.[7] IMC Perspective 22–1 on page 8 discusses the reasons why the council decided to overturn the ban, as well as the increase in TV advertising for distilled spirits that has resulted from its decision. Other industry trade associations with advertising codes and guidelines include the Toy Industry Association, the Motion Picture Association of America, and the Pharmaceutical Research and Manufacturers of America whose guidelines for prescription drug advertising are discussed later in the chapter.

Many professions also maintain advertising guidelines through local, state, and national organizations. For years professional associations like the American Medical Association (AMA) and the American Bar Association (ABA) restricted advertising by their members on the basis that such promotional activities lowered members' professional status and led to unethical and fraudulent claims. However, such restrictive codes have been attacked by both government regulatory agencies and consumer groups. They argue that the public has a right to be informed about a professional's services, qualifications, and background and that advertising will improve professional services as consumers become better informed and are better able to shop around.[8]

In 1977, the Supreme Court held that state bar associations' restrictions on advertising are unconstitutional and that attorneys have First Amendment freedom of speech rights to advertise.[9] Many professional associations subsequently removed their restrictions, and advertising by lawyers and other professionals is now common (Exhibit 22–2).[10] In 1982, the Supreme Court upheld an FTC order permitting advertising by dentists and physicians.[11]

Research shows that consumers generally favor increased use of professional advertising. However, professionals continue to have reservations. They worry that advertising has a negative impact on their image, credibility, and dignity and see benefits to consumers as unlikely.[12] Still, advertising by professionals is increasing, particularly among newcomers to medicine, dentistry, and law. Associations such as the AMA and the ABA developed guidelines for members' advertising to help maintain standards and guard against misleading, deceptive, or offensive ads.

The issue of professional advertising, particularly by attorneys, is still debated. Some traditional law firms resist using advertising, particularly on TV, due to concern that it might hurt the profession's image. Many in the legal profession worry that ads soliciting personal injury victims only worsen the public's perception of attorneys. A sizable faction within the American Bar Association (ABA) blames the legal profession's image problem on sleazy ads. The ABA's Commission on Advertising held a series of public hearings on what, if any, restrictive measures to recommend to state ethics panels. Some states restrict the content of attorney ads and the way they can be delivered and require a disclaimer urging consumers not to base their attorney selection on an advertisement. Many attorneys are incensed over efforts to restrict their rights to promote themselves because they use advertising to help build their practices. Several cases are currently being litigated, but ultimately the Supreme Court may have to decide just how far states can go in curtailing advertising.

Although industry associations are concerned with the impact and consequences of members' advertising, they have no legal way to enforce their guidelines. They can only rely on peer pressure from members or other nonbinding sanctions to get advertisers to comply.

# IMC Perspective 22–1 > > >

## Distilled Spirits Use TV Advertising to Boost Sales

For more than five decades, distilled spirits were not advertised on television or radio because of a self-imposed ban by members of the Distilled Spirits Council of the United States (DISCUS). Council members agreed in 1936 to avoid radio advertising and extended the ban to TV in 1948. But Seagram, the second-largest distiller in the world at the time, ended the U.S. spirits industry's long-standing ban on broadcast advertising in June 1996 by airing commercials for its Crown Royal Canadian Whiskey brand on an affiliate in Corpus Christi, Texas.

Seagram issued a statement that it was ending the liquor industry's decades-old practice of not advertising on TV because DISCUS's voluntary code of good practice placed spirits at a competitive disadvantage to beer and wine, which did not have any such restrictions. Seagram also argued that the ban had become outdated as radio and TV have become more targeted and they could pinpoint their advertising message to people of legal drinking age. A number of distillers, eager to turn around the long, slow decline in hard liquor sales, watched Seagram test the water with its TV ads before rolling out their own commercials. Some held discussions with TV stations but waited for a formal amendment to the DISCUS code of good practice before proceeding. The amendments came on November 7, 1996, when DISCUS members voted unanimously to overturn the self-imposed ban on broadcast ads. The DISCUS president noted that spirits makers wanted to break down the public perception that spirits are stronger or more dangerous than beer and wine and thus deserving of harsher social and political treatment.

After the DISCUS ban was lifted, the four major broadcast TV networks, as well as major cable networks such as ESPN and MTV, continued to refuse liquor ads prompting consumer and public interest groups to applaud their actions. In fact, it has been argued that it was really the refusal by TV stations and networks to accept liquor advertising that kept them off the air rather than the DISCUS code. However, the major networks cannot control the practices of affiliate stations they do not own and many of the affiliates began accepting liquor ads, as did local cable channels and independent broadcast stations—although most had restrictions that the ads had to air after 9 P.M.

In December 2001 NBC, which was owned by the General Electric Co. at the time, announced that it would become the first broadcast network to accept hard-liquor advertising. NBC planned to limit the liquor ads to programs where at least 85 percent of viewers are 21 or older, such as during late-night time slots. However, NBC was not joined by the three other major broadcast networks—ABC, CBS, and Fox—in its decision to accept liquor commercials. NBC's decision engendered criticism from members of Congress, federal regulators, the American Medical Association, and many public advocacy groups. Critics of NBC's decision expressed concern that airing liquor ads on TV would glamorize drinking and encourage children and teenagers to drink. Facing a widening backlash over its decision, in March 2002 NBC announced that it was dropping its plans to accept liquor advertising.

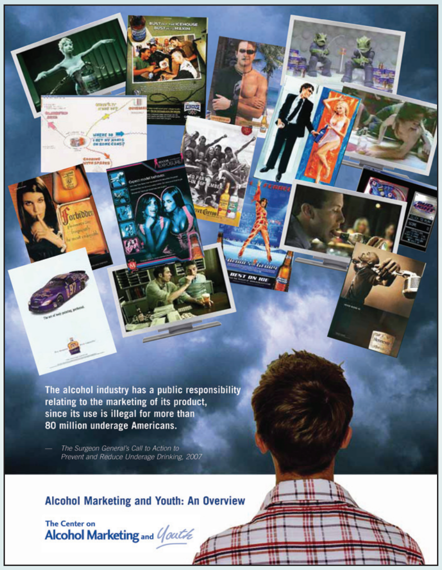
The national broadcast networks have continued their self-imposed ban although the amount of liquor advertising on television continues to increase as more than 600 local broadcast and cable stations now accept liquor advertising. Moreover, in 2009 Absolut, the Swedish vodka that has used aggressive advertising and marketing over the past three decades to become one of the world's leading spirit brands, took the bold step of breaking the voluntary ban of spirits advertising on network television by airing a prime-time commercial during the third hour of the *Grammy Awards.* The commercial ran on CBS owned-and-operated stations in 15 of the top markets reaching 31 percent of U.S. TV households and marked the first time a commercial for a distilled spirits product aired on any CBS-owned station. The 30-second spot was an emotion-laden soft sell commercial where the only reference to the brand was at the end when "In an Absolut World" and an understated product shot appeared. According to a CBS representative, local station managers are responsible for determining the suitability of the commercials they air and determined that the Absolut spot was tasteful and appropriate for their late-evening audiences.

Following the initial network airing on the *Grammy's,* Absolut ran the ad on network TV in a number of local markets and media experts, as well as individuals working in the alcohol industry expected other spirits brands to follow suit. Industry consultant Arthur Shapiro noted that: "The

## Self-Regulation by Businesses

LO 22-2

A number of self-regulatory mechanisms have been established by the business community in an effort to control advertising practices.[13] The largest and best known is the **Better Business Bureau (BBB)**, which promotes fair advertising and selling practices across all industries. The BBB was established in 1916 to handle consumer complaints about local business practices and particularly advertising. Local BBBs




world has changed since 2001. People are more accepting of spirits advertising. The industry draws the distinction between network, cable, or spot. The consumer doesn't care." The decision by the CBS affiliates to run the spot was also not surprising as the recession has taken its toll on advertising spending and local advertising has been particularly hard hit, making it difficult to turn away a new source of advertising revenue. NBC has also made some small moves back into the category by airing spots on its New York affiliate from Bacardi and Grey Goose.

The director of local broadcasting at the Universal McCann media agency has predicted that the spirits category is getting ready to break open, noting that network affiliates would not have considered these ads are now reviewing them as they look for new sources of revenue. However, as might be expected, this is not welcome news for various public advocacy groups. George Hacker, the director of the alcohol policies project at the Center for Science in the Public Interest (CSPI) predicted that brands that advertise on network TV would certainly be held up to scorn and noted that his group was less than delighted by the expansion of spirits advertising into network television. The former executive director of the Center on Alcohol Marketing and Youth at Georgetown University called the move a step backward and refuted the argument that it is acceptable to run the ads after 10 P.M., noting that many young people have TVs in their rooms and this is a heavy viewing time for the groups most at risk.

The liquor industry has also been able to break through several other promotional barriers recently. A major breakthrough occurred when NASCAR lifted its long-standing ban on liquor sponsorships in 2005. For many years, NASCAR officials were skeptical about lifting the ban. However, liquor giants Diageo, Jim Beam Brands, and Brown-Forman started lobbying the racing league in the late 1990s when they saw NASCAR sponsorship as a good fit with their target audience, as well as a symbolic step into mainstream marketing of their brands. Jack Daniels has become a NASCAR sponsor and is also the official sponsor of NASCAR.com's postrace show each week. All of the ads connected to NASCAR must have a strong responsible drinking component. For example, Jack Daniels' sponsorship initiatives include the slogan "Pace Yourself. Drink Responsibly."

In 2009, the distilled spirits industry made inroads into another sport when the National Basketball Association voted to rescind its longtime ban on courtside advertising of hard-liquor brands in an effort to increase revenue during the economic downturn. The NBA is also crafting policies that could allow teams to show ads for hard liquor on their websites, at point-of-sale retail locations, or in arena promotions. The new NBA policy followed moves by Major League Baseball, the National Hockey League, and NASCAR to allow spirits advertising within camera view. However, the National Football League still does not allow any hard liquor signage within camera view in their stadiums. CSPI's George Hacker called the NBA's decision an "act of desperation" and indicated that the advocacy group would not let it pass unnoticed and would be contacting the league.

Restrictions on advertising and other forms of promotion of hard liquor continue to loosen as DISCUS has made major inroads into putting liquor advertising more on par with advertising for beer and wine. DISCUS argues that it gets a high rate of compliance with its marketing code, which has helped the industry gain access to cable television and other channels that were traditionally closed to liquor advertisers. It appears that TV advertising for distilled spirits is here to stay.

Sources: Jeremy Mullman, "The Booze Tube: Spirits Marketers Put Big Bucks into TV," adage.com, July 17, 2006; David Kiley, "A Green Flag for Booze," *BusinessWeek*, March 7, 2005, p. 95; Stuart Elliott, "Facing Outcry, NBC Ends Plan to Run Liquor Ads," *The New York Times*, March 21, 2002, p. C1; Anthony Crupi and Kenneth Hein, "Absolut Takes a Shot at Network Television," *Brandweek*, February 9, 2009, p. 5; Rich Thomaselli, "NBA, MLB Rethink Liquor, Gaming Deals, *Advertising Age*, January 26, 2009, *http://adage.com/print?article_id=134071*.



are located in most large cities throughout the United States and supported entirely by dues of the more than 100,000 member firms.

Local BBBs receive and investigate complaints from consumers and other companies regarding the advertising and selling tactics of businesses in their area. Each local office has its own operating procedures for handling complaints; generally, the office contacts the violator and, if the complaint proves true, requests that the practice be stopped or changed. If the violator does not respond, negative publicity


**EXHIBIT 22–3**
The National Advertising Review Council partners with various advertising and marketing organizations to create an effective self-regulatory system

may be used against the firm or the case may be referred to appropriate government agencies for further action.

While BBBs provide effective control over advertising practices at the local level, the parent organization, the **Council of Better Business Bureaus**, plays a major role at the national level, as the third-party administrator of the advertising industry self-regulatory system. Policies and procedures for industry self-regulation are established by the National Advertising Review Council. The system includes three investigative units—the National Advertising Division of the Council of Better Business Bureaus (NAD), the Children's Advertising Review Unit (CARU), and the Electronic Retailing Self-Regulation Program (ERSP)—and an appellate unit, the **National Advertising Review Board (NARB)**. Staffed primarily by attorneys, NAD, CARU, and ERSP review advertising claims that are national in scope. CARU reviews advertising directed to children under the age of 12 and ERSP examines advertising claims in direct-response advertising, including infomercials and home-shopping channels.

## The National Advertising Review Council and the NAD/NARB

In 1971, four associations—the American Advertising Federation (AAF), the American Association of Advertising Agencies (AAAA), the Association of National Advertisers (ANA), and the Council of Better Business Bureaus—joined forces to establish the **National Advertising Review Council (NARC)**. In 2009, the CEOs of three other major marketing organizations—The Direct Marketing Association (DMA), Electronic Retailing Association (ERA), and the Interactive Advertising Bureau—joined the NARC Board of Directors (Exhibit 22–3).

NARC's mission is to sustain high standards of truth and accuracy in national advertising. NAD has examined advertising for truth and accuracy since 1971 and has published more than 5,000 decisions, focusing on areas that include product performance claims, superiority claims against competitive products, and all kinds of scientific and technical claims.

Federal law requires that advertisers possess substantiation for their advertising claims before the claims are published. After initiating or receiving a complaint, NAD requests the advertiser's substantiation, reviews the information, and reaches a determination. In cases where the substantiating evidence does not support the claim, NAD recommends that the advertiser modify or discontinue the claim. When an advertiser or a challenger disagrees with the NAD's findings, NAD's decision can be appealed to the NARB for additional review.

The NAD's advertising monitoring program is the source of many of the cases it reviews (Figure 22–1 on page 11). It also reviews complaints from consumers and consumer groups, trade associations, local BBBs, and competitors. For example, the NAD received a complaint from the Center for Science in the Public Interest, a consumer advocacy group, over an ad run by Campbell Soup for the company's V8 vegetable juice that suggested a link between the tomato-based product and a reduced risk of cancer. Though the NAD decided that Campbell provided competent and reliable evidence to support certain claims, it recommended that the company modify language stating "for prostate cancer, a lower risk is apparent when five or more servings (of tomato products) are consumed per week." Campbell agreed to change the wording of the ad.[14] During the 1970s and '80s, many of the complaints to the NAD came from consumers. However, with the increased use of comparative advertising, the majority of the complaints are now coming from marketers that are

| Sources | Number | Percent | Decisions | Number | Percent |
|---|---|---|---|---|---|
| Competitor challenges | 134 | 81% | Modified/discontinued | 42 | 30% |
| NAD monitoring | 32 | 19 | Substantiated/modified/discontinued | 42 | 30 |
| Local BBB challenges | 0 | 0 | Administratively closed | 15 | 11 |
| Consumer challenges | 0 | 0 | Compliance | 19 | 14 |
| Total | 166 | 100% | Substantiated | 5 | 4 |
| | | | Referred to government | 15 | 11 |
| | | | Total (28 cases pending) | 138 | 100% |

**FIGURE 22–1**

Sources of NAD Cases and Decisions, 2009

challenging competitors' comparisons with their brands.[15] For example, the online dating service eHarmony.com filed a complaint with the NAD over advertising used by competitor Chemistry.com, which claimed that it could use "the latest science of attraction to predict which single men and women one will have a relationship and dating chemistry."[16] Chemistry.com's matchmaking system was developed by an anthropologist who studies mate selection and uses responses to an extensive survey to determine people who might be attracted to one another.

In the Chemistry.com case, the NAD concluded that the dating service could not substantiate many of the advertising claims and ruled that the company should discontinue them. Chemistry's parent company, Match.com, issued a statement saying that it disagreed with some of the NAD's findings but would discontinue the claims at issue.[17]

Advertisers that disagree with NAD's findings have an automatic right to appeal NAD's decision to the National Advertising Review Board. NARB is composed of 70 advertising professionals and prominent public-interest/academia members.

In 2003, for example, Millennium Import Company, importers of Belvedere and Chopin vodka, filed a complaint with the NAD over advertising used by Sidney Frank Importing for its popular Grey Goose vodka brand that claimed it is the world's best-tasting vodka. Millennium argued that the claims were based on the results of a 1998 taste test and communicated a false message to consumers that Grey Goose currently ranked substantially higher than Belvedere in taste testing. After reviewing the case, the NAD ruled in favor of Millennium and Sidney Frank appealed the decision to the National Advertising Review Board, which concurred with the NAD's decision and found the advertising claim for Grey Goose inaccurate and misleading for consumers. Sidney Frank refused to comply with the NAD's and NARB's directive to discontinue or modify their ads and the self-regulatory agency referred the matter to the Federal Trade Commission. Millennium also filed a lawsuit against Sidney Frank in 2004 accusing the company of false advertising and was successful in gaining an injunction preventing Grey Goose from using the claim.[18]

Although the self-regulatory system has no power to order an advertiser to modify or stop running an ad and no sanctions it can impose, advertisers who participate in NAD/CARU/ERSP or NARB proceedings generally comply. When companies refuse to participate in a self-regulatory proceeding or do not comply with the terms of a decision, their disputed advertising may be referred to the most appropriate federal agency for further review.

In 2009, for example, of the 166 cases opened by NAD, 15 were referred to the government, 15 were administratively closed, 42 were modified or discontinued; 42 were substantiated, modified, or discontinued; 5 were substantiated; 15 cases were referred to the government; and 12 cases were appealed (Figure 22–1).[19]


**EXHIBIT 22–4**
Electronic Retailing Self-Regulation Program is a new area of self-regulation by the NARC

CARU's activities include the review and evaluation of child-directed advertising in all media, as well as online privacy issues that affect children. The CARU also provides a general advisory service for advertisers and agencies and has developed self-regulatory guidelines for children's advertising. CARU recognizes that the special nature and needs of a youthful audience require particular care and diligence on the part of advertisers. As such, CARU's Self-Regulatory Guidelines for Children's Advertising go beyond truthfulness and accuracy to address children's developing cognitive abilities.

In 2004, the NARC became involved in the self-regulation of electronic retailing when it initiated the Electronic Retailing Self-Regulation Program (ERSP). The program is sponsored by the Electronic Retailing Association (ERA), although it works independently of the ERA to create an unbiased self-regulatory system. The mission of the ERSP is to enhance consumer confidence in electronic retailing, to discourage advertising and marketing in the electronic retailing industry that contains unsubstantiated claims, and to demonstrate a commitment to meaningful and effective self-regulation (Exhibit 22–4). The majority of claims reviewed under the ERSP program are for direct-response TV ads including long- and short-form infomercials. Reviews apply to all aspects of a marketing campaign including radio and Internet marketing. SPAM e-mails along with Internet pop-up ads that lead to further e-commerce are in the ERSP's purview as well as advertising on TV shopping channels.[20]

The NAD also works with various industries to help them develop more effective self-regulatory programs. For example, in 2006 the National Advertising Review Council and the Council for Responsible Nutrition (CRN), a trade association representing dietary supplement manufacturers and ingredient suppliers, developed a dietary supplement advertising review program. The goal of the program was to increase consumer confidence in the truth and accuracy of advertising claims for dietary supplement products and to encourage fair competition within the industry. The year before the monitoring initiative began, the NAD opened less than 10 cases involving dietary supplement advertising. However, during the first three years of the program the NAD opened more than 75 cases, with almost all resulting in voluntary compliance. In 2009 the NAD received a $959,000 grant from the CRN Foundation to extend the program for an additional five years.[21]

The National Advertising Review Council, working through the NAD/CARU/ERSP and NARB is a valuable and effective self-regulatory body. Cases brought to it are handled at a fraction of the cost (and with much less publicity) than those brought to court and are expedited more quickly than those reviewed by a government agency such as the FTC. The system also works because judgments are made by the advertiser's peers, and most companies feel compelled to comply. Firms may prefer self-regulation rather than government intervention in part because they can challenge competitors' unsubstantiated claims and win a more rapid resolution.[22]

**Advertising Associations** Various groups in the advertising industry also favor self-regulation. The two major national organizations, the American Association of Advertising Agencies and the American Advertising Federation, actively monitor and police industrywide advertising practices. The AAAA, which is the major trade association of the ad agency business in the United States, has established standards

The Board of Directors of the American Association of Advertising Agencies recognizes that when used truthfully and fairly, comparative advertising provides the consumer with needed and useful information.

However, extreme caution should be exercised. The use of comparative advertising, by its very nature, can distort facts and, by implication, convey to the consumer information that misrepresents the truth.

Therefore, the Board believes that comparative advertising should follow certain guidelines:

1. The intent and connotation of the ad should be to inform and never to discredit or unfairly attack competitors, competing products, or services.
2. When a competitive product is named, it should be one that exists in the marketplace as significant competition.
3. The competition should be fairly and properly identified but never in a manner or tone of voice that degrades the competitive product or service.
4. The advertising should compare related or similar properties or ingredients of the product, dimension to dimension, feature to feature.
5. The identification should be for honest comparison purposes and not simply to upgrade by association.
6. If a competitive test is conducted, it should be done by an objective testing source, preferably an independent one, so that there will be no doubt as to the veracity of the test.
7. In all cases the test should be supportive of all claims made in the advertising that are based on the test.
8. The advertising should never use partial results or stress insignificant differences to cause the consumer to draw an improper conclusion.
9. The property being compared should be significant in terms of value or usefulness of the product to the consumer.
10. Comparatives delivered through the use of testimonials should not imply that the testimonial is more than one individual's thought unless that individual represents a sample of the majority viewpoint.

**FIGURE 22–2**

AAAA Policy Statement and Guidelines for Comparative Advertising

Source: Reprinted with permission.

of practice and its own creative code. It also issues guidelines for specific types of advertising such as comparative messages (Figure 22–2). The AAF consists of advertisers, agencies, media, and numerous advertising clubs. The association has standards for truthful and responsible advertising, is involved in advertising legislation, and actively influences agencies to abide by its code and principles.

LO 22-2

## Self-Regulation by Media

The media are another important self-regulatory mechanism in the advertising industry. Most media maintain some form of advertising review process and, except for political ads, may reject any they regard as objectionable. Some media exclude advertising for an entire product class; others ban individual ads they think offensive or objectionable. For example, *Reader's Digest* does not accept advertising for tobacco or liquor products. A number of magazines in the United States and other countries refused to run some of Benetton's shock ads on the grounds that their readers would find them offensive or disturbing (Exhibit 22–5).[23]

Newspapers and magazines have their own advertising requirements and restrictions, which often vary depending on the size and nature of the publication. Large, established publications, such as major newspapers or magazines, often have strict standards regarding the type of advertising they accept. Some magazines, such as *Parents* and *Good Housekeeping,* regularly test the products they advertise and offer a "seal of approval" and refunds if the products are later found to be defective. Such policies

**EXHIBIT 22–5**

A number of magazines refused to run this Benetton ad

are designed to enhance the credibility of the publication and increase the reader's confidence in the products it advertises.

Advertising on television and radio has been regulated for years through codes developed by the industry trade association, the National Association of Broadcasters (NAB). Both the radio code (established in 1937) and the television code (1952) provided standards for broadcast advertising for many years. Both codes prohibited the advertising of certain products, such as hard liquor. They also affected the manner in which products could be advertised. However, in 1982, the NAB suspended all of its code provisions after the courts found that portions (dealing with time standards and required length of commercials in the TV code) were in restraint of trade. While the NAB codes are no longer in force, many individual broadcasters, such as the major TV networks, have incorporated major portions of the code provisions into their own standards.[24]

The four major television networks have the most stringent review process of any media. All four networks maintain standards and practices divisions, which carefully review all commercials submitted to the network or individual affiliate stations. Advertisers must submit for review all commercials intended for airing on the network or an affiliate.

A commercial may be submitted for review in the form of a script, storyboard, animatic, or finished commercial (when the advertiser believes there is little chance of objection). A very frustrating, and often expensive, scenario for both an agency and its client occurs when a commercial is approved at the storyboard stage but then is rejected after it is produced. Commercials are rejected for a variety of reasons, including violence, morbid humor, sex, politics, and religion. Network reviewers also consider whether the proposed commercial meets acceptable standards and is appropriate for certain audiences. For example, different standards are used for ads designated for prime-time versus late-night spots or for children's versus adults' programs (see Figure 22–3). Although most of these guidelines remain in effect, ABC and NBC loosened their rules on celebrity endorsements.[25]

The four major networks receive nearly 50,000 commercials a year for review; nearly two-thirds are accepted, and only 3 percent are rejected. Most problems with

**FIGURE 22–3**

A Sampling of the TV Networks' Guidelines for Children's Advertising

Each of the major TV networks has its own set of guidelines for children's advertising, although the basics are very similar. A few rules, such as the requirement of a static "island" shot at the end, are written in stone; others, however, can sometimes be negotiated. Many of the rules below apply specifically to toys. The networks also have special guidelines for kids' food commercials and for kids' commercials that offer premiums.

- Must not overglamorize product
- No exhortative language, such as "Ask Mom to buy . . ."
- No realistic war settings
- Generally no celebrity endorsements
- Can't use "only" or "just" in regard to price
- Show only two toys per child or maximum of six per commercial
- Five-second "island" showing product against plain background at end of spot
- Animation restricted to one-third of a commercial
- Generally no comparative or superiority claims
- No costumes or props not available with the toy
- No child or toy can appear in animated segments
- Three-second establishing shot of toy in relation to child
- No shots under one second in length
- Must show distance a toy can travel before stopping on its own

**EXHIBIT 22–6**
This humorous "Got milk?" commercial had to be modified slightly to satisfy network censors

the remaining 30 percent are resolved through negotiation, and the ads are revised and resubmitted.[26] Most commercials run after changes are made. For example, censors initially rejected a humorous "Got milk?" spot that showed children watching an elderly neighbor push a wheelbarrow. Suddenly, the man's arms rip off, presumably because he doesn't drink milk. The spot was eventually approved after it was modified so that the man appears unhurt after losing his limbs and there was no expression of pain (Exhibit 22–6).[27]

Network standards regarding acceptable advertising change constantly. The networks first allowed lingerie advertisers to use live models rather than mannequins in 1987. Advertising for contraceptives is now appearing on some stations. The networks also loosened long-standing restrictions on endorsements and competitive advertising claims.[28] Network standards will continue to change as society's values and attitudes toward certain issues and products change. Also, many advertising people believe these changes are a response to competition from independent and cable stations, which tend to be much less stringent in their standards and practices. However, since television is probably the most carefully scrutinized and frequently criticized of all forms of advertising, the networks must be careful not to offend their viewers and detract from advertising's credibility.

For example, a number of advertisers such as Godaddy.com have had ads created for the Super Bowl rejected because the big game has a very large audience that ranges from children to older adults and the networks ruled that the sexually suggestive ads were inappropriate for the tenor of the event.[29] CBS rejected a commercial that ManCrunch .com, a gay dating website, wanted to air on the 2010 Super Bowl showing two young men watching a football game and rooting for their teams and then becoming passionate when their hands meet inside a bowl of chips (Exhibit 22–7). In its rejection letter CBS stated that the ad was not within the network's broadcast standards for Super Bowl Sunday and that it had difficulty verifying ManCrunch's credit status. While CBS indicated that it was open to working with the company on alternative submissions, some gay rights groups complained that the network was discriminating against the company as well as gays by not accepting the ad.[30]

**EXHIBIT 22–7**
CBS rejected a commercial that ManCrunch wanted to run on the Super Bowl

## Appraising Self-Regulation

The three major participants in the advertising process—advertisers, agencies, and the media—work individually and collectively to encourage truthful, ethical, and responsible advertising. The advertising industry views self-regulation as an effective mechanism for controlling advertising abuses and avoiding the use of

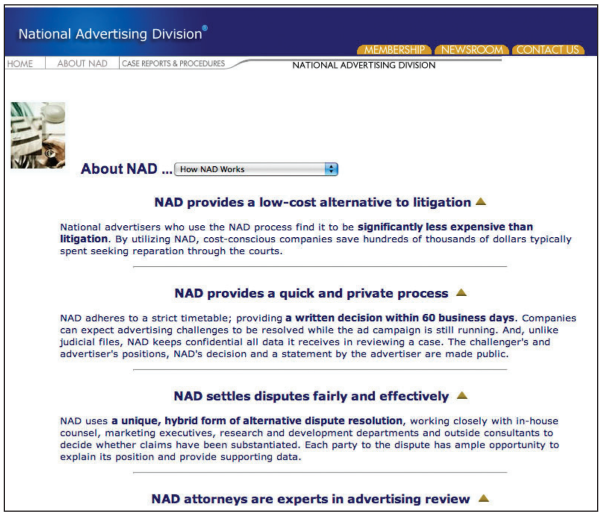



**EXHIBIT 22–8**
The NAD is an effective alternative to government intervention and/or litigation.

offensive, misleading, or deceptive practices, and it prefers this form of regulation to government intervention (Exhibit 22–8). Self-regulation of advertising has been effective and in many instances probably led to the development of more stringent standards and practices than those imposed by or beyond the scope of legislation.

A senior vice president and general counsel at Kraft Foods, while praising the NAD, summarized the feelings of many advertisers toward self-regulation. In his testimonial he stated: "NAD is superior to its competition, which is regulation by the government or regulation by the courts. Accurate, prompt, and inexpensive decisions year in and year out have earned NAD its well-deserved credibility with the industry and with regulators." Former Federal Trade Commission chairman Timothy Murris has described the NAD as a "model of self-regulation." Deborah Platt Majoras, who was the FTC chair from 2004 until 2008, also praised the National Advertising Review Council for running a model program covering national advertising as well as a number of other areas.

There are, however, limitations to self-regulation, and the process has been criticized in a number of areas. For example, the NAD may take six months to a year to resolve a complaint, during which time a company often stops using the commercial anyway. Budgeting and staffing constraints may limit the number of cases the NAD/NARB system investigates and the speed with which it resolves them.[31] And some critics believe that self-regulation is self-serving to the advertisers and advertising industry and lacks the power or authority to be a viable alternative to federal or state regulation.

Many do not believe advertising can or should be controlled solely by self-regulation. They argue that regulation by government agencies is necessary to ensure that consumers get accurate information and are not misled or deceived. Moreover, since advertisers do not have to comply with the decisions and recommendations of self-regulatory groups, it is sometimes necessary to turn to the federal and/or state government.

## FEDERAL REGULATION OF ADVERTISING

LO 22-3

Advertising is controlled and regulated through federal, state, and local laws and regulations enforced by various government agencies. The federal government is the most important source of external regulation since many advertising practices come under the jurisdiction of the **Federal Trade Commission**. In addition, depending on the advertiser's industry and product or service, other federal agencies such as the Federal Communications Commission, the Food and Drug Administration, the U.S. Postal Service, and the Bureau of Alcohol, Tobacco, and Firearms may have regulations that affect advertising. We will begin our discussion of federal regulation of advertising by considering the basic rights of marketers to advertise their products and services under the First Amendment.

### Advertising and the First Amendment

Freedom of speech or expression, as defined by the First Amendment to the U.S. Constitution, is the most basic federal law governing advertising in the United States. For many years, freedom of speech protection did not include advertising and other forms of speech that promote a commercial transaction. However, the courts have extended First Amendment protection to **commercial speech**, which is speech that promotes a commercial transaction. There have been a number of landmark cases over the past three decades where the federal courts have issued rulings supporting the coverage of commercial speech by the First Amendment.

In a 1976 case, *Virginia State Board of Pharmacy v. Virginia Citizens Consumer Council,* the U.S. Supreme Court ruled that states cannot prohibit pharmacists from advertising the prices of prescription drugs, because such advertising contains information that helps the consumer choose between products and because the free flow of information is indispensable.[32] As noted earlier, in 1977 the Supreme Court ruled that state bar associations' restrictions on advertising are unconstitutional and attorneys have a First Amendment right to advertise their services and prices.[33] In another landmark case in 1980, *Central Hudson Gas & Electric Corp. v. New York Public Service Commission,* the Supreme Court ruled that commercial speech was entitled to First Amendment protection in some cases. However, the Court ruled that the U.S. Constitution affords less protection to commercial speech than to other constitutionally guaranteed forms of expression. In this case the Court established a four-part test, known as the **Central Hudson Test**, for determining restrictions on commercial speech.[34] In a more recent case, the Supreme Court's 1996 decision in *44 Liquormart, Inc. v. Rhode Island* struck down two state statutes designed to support the state's interest in temperance. The first prohibited the advertising of alcoholic beverage prices in Rhode Island except on signs within a store, while the second prohibited the publication or broadcast of alcohol price ads. The Court ruled that the Rhode Island statutes were unlawful because they restricted the constitutional guarantee of freedom of speech, and the decision signaled strong protection for advertisers under the First Amendment.[35]

In the cases regarding advertising, the U.S. Supreme Court has ruled that freedom of expression must be balanced against competing interests. For example, the courts have upheld bans on the advertising of products that are considered harmful, such as tobacco. The Court has also ruled that only truthful commercial speech is protected, not advertising or other forms of promotion that are false, misleading, or deceptive.

In a recent and important case involving Nike, the California Supreme Court issued a ruling that is likely to impact the way companies engage in public debate regarding issues that affect them. Nike was sued for false advertising under California consumer protection laws for allegedly making misleading statements regarding labor practices and working conditions in its foreign factories. Nike argued that statements the company made to defend itself against the charges should be considered political speech, which is protected by the First Amendment, rather than commercial speech, which is subject to advertising regulations. However, the California high court ruled that statements made by the company to defend itself against the allegations were commercial in nature and thus subject to the state's consumer protection regulations. Nike appealed the case to the U.S. Supreme Court, which sent it back to California for trial to determine if the company's statements were deceptive and misleading. However, Nike settled the case rather than risking a long and costly court battle. While the ruling in this case only applies to California, it is important as the courts ruled that speech in the form of press releases or public statements by company representatives can be considered commercial and subject to consumer protection laws.[36]

The job of regulating advertising at the federal level and determining whether advertising is truthful or deceptive is a major focus of the Federal Trade Commission. We now turn our attention to federal regulation of advertising and the FTC.

## Background on Federal Regulation of Advertising

Federal regulation of advertising originated in 1914 with the passage of the **Federal Trade Commission Act** (FTC Act), which created the FTC, the agency that is today the most active in, and has primary responsibility for, controlling and regulating advertising. The FTC Act was originally intended to help enforce antitrust laws, such as the Sherman and Clayton acts, by helping to restrain unfair methods of competition. The main focus of the first five-member commission was to protect competitors from one another; the issue of false or misleading advertising was not even mentioned. In 1922, the Supreme Court upheld an FTC interpretation that false advertising was an unfair method of competition, but in the 1931 case *FTC v. Raladam Co.,* the Court ruled the commission could not prohibit false advertising unless there was evidence of injury to a competitor.[37] This ruling limited the power of the FTC to protect consumers from false or deceptive advertising and led to a consumer movement that resulted in an important amendment to the FTC Act.

In 1938, Congress passed the **Wheeler-Lea Amendment**. It amended section 5 of the FTC Act to read: "Unfair methods of competition in commerce and unfair or deceptive acts or practices in commerce are hereby declared to be unlawful." The amendment empowered the FTC to act if there was evidence of injury to the public; proof of injury to a competitor was not necessary. The Wheeler-Lea Amendment also gave the FTC the power to issue cease-and-desist orders and levy fines on violators. It extended the FTC's jurisdiction over false advertising of foods, drugs, cosmetics, and therapeutic devices. And it gave the FTC access to the injunctive power of the federal courts, initially only for food and drug products but expanded in 1972 to include all products in the event of a threat to the public's health and safety.

In addition to the FTC, numerous other federal agencies are responsible for, or involved in, advertising regulation. The authority of these agencies is limited, however, to a particular product area or service, and they often rely on the FTC to assist in handling false or deceptive advertising cases.

## The Federal Trade Commission

LO 22-3

The FTC is responsible for protecting both consumers and businesses from anti-competitive behavior and unfair and deceptive practices. The major divisions of the FTC include the bureaus of competition, economics, and consumer protection. The Bureau of Competition seeks to prevent business practices that restrain competition and is responsible for enforcing antitrust laws. The Bureau of Economics helps the FTC evaluate the impact of its actions and provides economic analysis and support to antitrust and consumer protection investigations and rule makings. It also analyzes the impact of government regulation on competition and consumers. The Bureau of Consumer Protection's mandate is to protect consumers against unfair, deceptive, or fraudulent practices. This bureau also investigates and litigates cases involving acts or practices alleged to be deceptive or unfair to consumers. The Division of Advertising Practices protects consumers from deceptive and unsubstantiated advertising and enforces the provisions of the FTC Act that forbid misrepresentation, unfairness, and deception in general advertising at the national and regional level (Exhibit 22–9). The Division of Marketing Practices engages in activities that are related to various marketing and warranty practices such as fraudulent telemarketing schemes, 900-number programs, and disclosures relating to franchise and business opportunities.

**EXHIBIT 22–9**
The Division of Advertising Practices protects consumers from deceptive and unsubstantiated advertising claims


The FTC has had the power to regulate advertising since passage of the Wheeler-Lea Amendment. However, not until the early 1970s—following criticism of the commission in a book by "Nader's Raiders" and a special report by the American Bar Association citing its lack of action against deceptive promotional practices—did the FTC become active in regulating advertising.[38] The authority of the FTC was increased considerably throughout the 1970s. The Magnuson-Moss Act of 1975, an important piece of legislation, dramatically broadened the FTC's powers and substantially increased its budget. The first section of the act dealt with consumers' rights regarding product warranties; it allowed the commission to require restitution for deceptively written warranties where the consumer lost more than $5. The second section, the FTC Improvements Act, empowered the FTC to establish **trade regulation rules (TRRs)**, industrywide rules that define unfair practices before they occur.

During the 1970s, the FTC made enforcement of laws regarding false and misleading advertising a top priority. Several new programs were instituted, budgets were increased, and the commission became a very powerful regulatory agency. However, many of these programs, as well as the expanded powers of the FTC to develop regulations on the basis of "unfairness," became controversial. At the root of this controversy is the fundamental issue of what constitutes unfair advertising.

## The Concept of Unfairness

Under section 5 of the FTC Act, the Federal Trade Commission has a mandate to act against unfair or deceptive advertising practices. However, this statute does not define the terms *unfair* and *deceptive,* and the FTC has been criticized for not doing so itself. While the FTC has taken steps to clarify the meaning of *deception,* people have been concerned for years about the vagueness of the term *unfair.*

Controversy over the FTC's authority to regulate unfair advertising practices began in 1978, when the agency relied on this mandate to formulate its controversial "kid vid" rule restricting advertising to children.[39] This interpretation caused widespread concern in the business community that the term *unfair* could be used to encompass anything FTC commissioners might find objectionable. For example, in a 1980 policy statement the FTC noted that "the precise concept of consumer unfairness is one whose precise meaning is not immediately obvious." Consequently, in 1980 Congress responded by suspending the children's advertising rule and banning the FTC from using unfairness as a legal basis for advertising rulemaking.

The FTC responded to these criticisms in December 1980 by sending Congress a statement containing an interpretation of unfairness. According to FTC policy, the basis for determining **unfairness** is that a trade practice (1) causes substantial physical or economic injury to consumers, (2) could not reasonably be avoided by consumers, and (3) must not be outweighed by countervailing benefits to consumers or competition. The agency also stated that a violation of public policy (such as of other government statutes) could, by itself, constitute an unfair practice or could be used to prove substantial consumer injury. Practices considered unfair are claims made without prior substantiation, claims that might exploit such vulnerable groups as children and the elderly, and instances where consumers cannot make a valid choice because the advertiser omits important information about the product or competing products mentioned in the ad.[40]

The FTC's statement was intended to clarify its interpretation of unfairness and reduce ambiguity over what might constitute unfair practices. However, efforts by the FTC to develop industrywide trade regulation rules that would define unfair practices and have the force and effect of law were limited by Congress in 1980 with the passage of the FTC Improvements Act. Amidst calls to end the stalemate over the FTC's regulation of unfair advertising by having the agency work with Congress to define its advertising authority, in 1994 Congress and the advertising industry agreed on a definition of unfair advertising that is very similar to the FTC's 1980 policy statement discussed earlier. However, the new agreement requires that before the FTC can initiate any industrywide rule, it has to have reason to believe that the unfair or deceptive acts or practices are prevalent.[41]

The FTC does have specific regulatory authority in cases involving deceptive, misleading, or untruthful advertising. The vast majority of advertising cases that the FTC handles concern deception and advertising fraud, which usually involve knowledge of a false claim.

## Deceptive Advertising

In most economies, advertising provides consumers with information they can use to make consumption decisions. However, if this information is untrue or misleads the consumer, advertising is not fulfilling its basic function. Moreover, a study by Peter Drake and Robin Ritchie found that deceptive advertising engenders mistrust, which negatively affects consumers' responses to subsequent advertising from the same source as well as second-party sources. They note that deceptive advertising can seriously undermine the effectiveness and credibility of advertising and marketing in general by making consumers defensive toward future advertising and should be of concern to all marketers.[42] But what constitutes an untruthful or deceptive ad? Deceptive advertising can take a number of forms, ranging from intentionally false or misleading claims to ads that, although true, leave some consumers with a false or misleading impression.

The issue of deception, including its definition and measurement, receives considerable attention from the FTC and other regulatory agencies. One of the problems regulatory agencies deal with in determining deception is distinguishing between false or misleading messages and those that, rather than relying on verifiable or substantiated objective information about a product, make subjective claims or statements, a practice known as puffery. **Puffery** has been legally defined as "advertising or other sales presentations which praise the item to be sold with subjective opinions, superlatives, or exaggerations, vaguely and generally, stating no specific facts."[43] The use of puffery in advertising is common. For example, Bayer aspirin calls itself the "wonder drug that works wonders," Nestlé claims "Nestlé makes the very best chocolate," Snapple advertises that its beverages are "made from the best stuff on Earth," and BMW uses the tagline "The Ultimate Driving Machine." Superlatives such as *greatest, best,* and *finest* are puffs that are often used.

Puffery has generally been viewed as a form of poetic license or allowable exaggeration. The FTC takes the position that because consumers expect exaggeration or inflated claims in advertising, they recognize puffery and don't believe it. But some studies show that consumers may believe puffery and perceive such claims as true.[44] One study found that consumers could not distinguish between a verifiable fact-based claim and puffery and were just as likely to believe both types of claims.[45] Ivan Preston argues that puffery has a detrimental effect on consumers' purchase decisions by burdening them with untrue beliefs and refers to it as "soft-core deception" that should be illegal.[46]

Advertisers' battle to retain the right to use puffery was supported in the latest revision of the Uniform Commercial Code in 1996. The revision switches the burden of proof to consumers from advertisers in cases pertaining to whether certain claims were meant to be taken as promises. The revision states that the buyer must prove that an affirmation of fact (as opposed to puffery) was made, that the buyer was aware of the advertisement, and that the affirmation of fact became part of the agreement with the seller.[47]

The use of puffery as a defense for advertising claims is periodically challenged in court. IMC Perspective 22–2 on page 22 discusses a legal battle involving Pizza Hut and Papa John's in which the U.S. Supreme Court issued a decision in support of the use of puffery as the basis for a comparative advertising claim, and how Domino's used the ruling as the basis for an ad campaign comparing the taste of their pizza to Papa John's.

A more recent ruling by an appellate court may set new precedents for the use of puffery and comparative advertising. The case was filed in 2006 by Time Warner Cable against its rival DirecTV over commercials the satellite television company was running to promote the superiority of its high definition service over that of cable. One of the spots featured actress Jessica Simpson portraying the Daisy Duke character she played in the movie *The Dukes of Hazzard*. In the spot Simpson says, "Hey 253 days at the gym to get this body and you're not gonna watch me on DirectTV HD? You're not gonna get the best picture out of some fancy big-screen TV without DirecTV. It's broadcast in 1080 dpi. I don't totally know what that means, but I want it." In the original spot a narrator added, "For picture quality that beats cable, you've got to get DirecTV." However, the spot was revised to say, "For an HD picture that can't be beat, get DirecTV." The campaign also included Internet banner ads featuring a very fuzzy picture identified as "other TV" next to a clear picture labeled "DirecTV."

Although Time Warner was not mentioned by name in the ads, it sued, challenging the campaign's accuracy despite the changes to the original slogan. DirecTV argued that the revised ads never said its picture was better than cable's and claimed the Internet ads were using puffery. A district court judge issued an order stopping DirecTV from running the TV spots and Internet banner ads. However, DirecTV appealed the ruling and in 2007 an appellate panel issued a ruling upholding the ban on the TV spots, but reversing the decision on the Internet ads, noting that no one would believe the fuzzy picture shown represented a real cable picture. The judges ruled that the license to use verbal puffery claims also apply to "grossly exaggerated" images that no consumer would take as fact. The two companies settled the dispute out of court and the case was dropped.[48]

Since unfair and deceptive acts or practices have never been precisely defined, the FTC is continually developing and refining a working definition in its attempts to regulate advertising. The traditional standard used to determine deception was whether a claim had the "tendency or capacity to deceive." However, this standard was criticized for being vague and all-encompassing.

In 1983, the FTC, under Chair James Miller III, put forth a new working definition of **deception**: "The commission will find deception if there is a misrepresentation, omission, or practice that is likely to mislead the consumer acting reasonably in the circumstances to the consumer's detriment."[49] There are three essential elements to this definition of deception.[50] The first element is that the representation, omission, or practice must be *likely to mislead* the consumer. The FTC defines *misrepresentation* as an express or implied statement contrary to fact, whereas a *misleading omission* occurs when qualifying information necessary to prevent a practice, claim, representation, or reasonable belief from being misleading is not disclosed.

The second element is that the act or practice must be considered from the perspective of *the reasonable consumer.* In determining reasonableness, the FTC considers the group to which the advertising is targeted and whether their interpretation of or reaction to the message is reasonable in light of the circumstances. The standard is flexible and allows the FTC to consider factors such as the age, education level, intellectual capacity, and frame of mind of the particular group to which the message or practice is targeted. For example, advertisements targeted to a particular group, such as children or the elderly, are evaluated with respect to their effect on a reasonable member of that group.

The third key element to the FTC's definition of deception is *materiality.* According to the FTC a "material" misrepresentation or practice is one that is likely to affect a consumer's choice or conduct with regard to a product or service. What this means is that the information, claim, or practice in question is important to consumers and, if acted upon, would be likely to influence their purchase decisions. In some cases the information or claims made in an ad may be false or misleading but would not be regarded as material since reasonable consumers would not make a purchase decision on the basis of this information.

Miller's goal was to help the commission determine which cases were worth pursuing and which were trivial. Miller argued that for an ad to be considered worthy of FTC challenge, it should be seen by a substantial number of consumers, it should lead to significant injury, and the problem should be one that market forces are not likely to remedy. However, the revised definition may put a greater burden on the FTC to prove that deception occurred and that the deception influenced the consumers' decision-making process in a detrimental way.

Determining what constitutes deception is still a gray area. Two of the factors the FTC considers in evaluating an ad for deception are (1) whether there are significant

# IMC Perspective 22–2 > > >

## Domino's Joins the Pizza Puffery War

The use of unsubstantiated superlatives such as good, better, and best has long been a staple of American advertising. The Federal Trade Commission views the use of these terms, as well as other forms of marketing bravado, as puffery and takes the position that consumers would not expect these claims to be documented or take them seriously. However, advertisers often see the use of these terms as tantamount to claims of superiority and the advertisers that use them as engaging in comparative advertising. Thus, they expect their competitors can substantiate their claims rather than try to hide behind a thin veil of puffery. In recent years, a number of well-known companies have taken legal action against competitors to stop them from using claims their rivals argue are based on puffery, and thus require no substantiation.

One of the most intense battles regarding the use of puffery was fought by Papa John's and Pizza Hut and went all the way to the United States Supreme Court. The problem began when Papa John's began running ads comparing its product to market leader Pizza Hut using the tagline "Better Ingredients. Better Pizza." Pizza Hut initially filed a complaint with the National Advertising Division of the Council of Better Business Bureaus, but after getting no sympathy from the NAD, the company filed a lawsuit against Papa John's, claiming that the latter's ads were false and misleading. After hearing several weeks of testimony, a jury sided with Pizza Hut, ruling that the slogan was false and misleading because Papa John's had failed to prove its sauce and dough were superior. The judge upheld the jury's decision and ruled that the slogan was acceptable puffery until Papa John's began running ads touting its tomato sauce and pizza dough as superior and issued an injunction against the entire "Better Ingredients. Better Pizza" integrated marketing campaign the company was using.

Papa John's appealed the decision arguing that the judge had misinterpreted the law and claimed the use of the slogan was legally acceptable puffery. The court of appeals handed down a complicated ruling that sided with Papa John's on the puffery issue and lifted the injunction. Pizza Hut petitioned to have the ruling heard by the U.S. Supreme Court on the grounds that the appellate court had required an unusually high standard of evidence from its research studies to prove that consumers had been misled by Papa John's. However, the high court denied the petition and the court of appeals ruling was allowed to stand. The advertising industry was relieved that the Supreme Court ruled in favor of Papa John's because a ruling against the puffery defense could have opened the door for other challenges and a redrawing of the blurry line between so-called puffery and outright false advertising.

Pizza Hut and Papa John's finally ended their battle after spending millions of dollars in legal fees and being criticized for frivolous appeals and wasting the Supreme Court's time by having the highest court in the land listen to how

omissions of important information and (2) whether advertisers can substantiate the claims made for the product or service. The FTC has developed several programs to address these issues.

**Affirmative Disclosure** An ad can be literally true yet leave the consumer with a false or misleading impression if the claim is true only under certain conditions or circumstances or if there are limitations to what the product can or cannot do. Thus, under its **affirmative disclosure** requirement, the FTC may require advertisers to include certain types of information in their ads so that consumers will be aware of all the consequences, conditions, and limitations associated with the use of a product or service. The goal of affirmative disclosure is to give consumers sufficient information to make an informed decision. An ad may be required to define the testing situation, conditions, or criteria used in making a claim. For example, fuel mileage claims in car ads are based on Environmental Protection Agency (EPA) ratings since they offer a uniform standard for making comparisons. Cigarette ads must contain a warning about the health risks associated with smoking.

An example of an affirmative disclosure ruling is the FTC's case against Campbell Soup for making deceptive and unsubstantiated claims. Campbell's ads, run as part of its "Soup is good food" campaign, linked the low-fat and low-cholesterol they make their pizzas. However, knowing that the legal battle was a disaster for both companies, Domino's (which is the second leading national pizza chain) decided to take advantage of the appellate court ruling that Papa John's "Better Ingredients. Better Pizza" slogan was considered puffery.

In early 2010, Domino's began running a TV commercial showing the company's head chef, Brandon Solano, standing outside of a Federal Court of Appeals building in New Orleans talking about Papa John's and its slogan. In the spot Solano says: "For years Papa John's has been telling us they have better ingredients and better pizza. But when challenged in this court, they stated their slogan is puffery." He then turns to a lawyer standing next to him and asks him: "What's puffery?" Reading from a law book the lawyer says: "Puffery. An exaggerated statement based on opinion. Not fact." Solano then says "Here's what's not puffery" and goes on to explain how Dominos beat Papa John's in a national taste test. The spot ends with Solano stating: "Our pizza tastes better and that's not puffery, that's proven."

The commercial was not the first time Domino's used a comparative taste-test commercial. In late 2008 the pizza chain launched a campaign claiming that consumers preferred its oven-baked sandwiches over Subway's by a two-to-one margin. However, Subway responded to Domino's comparative ads very quickly with a cease-and-desist letter citing concerns about the methodology used in the taste tests and the ability to make fair comparisons between the products. Domino's responded less than a month later with an ad showing its CEO declaring: "Everything's better when it's oven-baked, even a letter from Subway," as he tosses the letter into a pizza oven. Domino's also added a "Bake the letter" feature on its website where consumers could


click a button and watch an image of the letter burn, with a visible Subway logo.

Some experts note that Domino's may be setting itself up for a legal challenge with its comparative ads as both make specific fact claims regarding taste superiority over Papa John's and Subway. However, Domino's chief marketing officer has noted that the company is confident in its consumer research, and its aggressive marketing demonstrates its commitment to gaining a foothold in the sandwich business as well as increasing its share of the pizza market. At this point, the ball is in Papa John's as well as Subway's court and both must decide if they want to call in their lawyers and start the legal battle once again.

Sources: Emily Bryson York, "Domino's Claims Victory with Pizza Makeover Strategy," *Advertising Age,* May 10, 2010, http://adage.com/article_id=143764; Emily Bryson York, "Domino's Doesn't Back Down in Sandwich Skirmish," *Advertising Age,* January 23, 2009, http://adage.com/article_id=134070; Suzanne Vranica, "Pizza Maker's Ads Aims to Top Rival," *The Wall Street Journal,* April 4, 2005, p. B6.



content of its soup with a reduced risk of heart disease. However, the advertising failed to disclose that the soups are high in sodium, which may increase the risk of heart disease. In a consent agreement accepted in 1991, Campbell agreed that, for any soup containing more than 500 milligrams of sodium in an 8-ounce serving, it will disclose the sodium content in any advertising that directly or by implication mentions heart disease in connection with the soup. Campbell also agreed it would not imply a connection between soup and a reduction in heart disease in future advertising.[51]

Another area where the Federal Trade Commission is seeking more specificity from advertisers is in regard to country of origin claims. The FTC has been working with marketers and trade associations to develop a better definition of what the "Made in the USA" label means. The 50-year-old definition used until recently required full manufacturing in the United States, using U.S. labor and parts, with only raw materials from overseas.[52] Many companies argue that in an increasingly global economy, it is becoming very difficult to have 100 percent U.S. content and remain price-competitive. However, the FTC argues that advertising or labeling a product as "Made in the USA" can provide a company with a competitive advantage. For many products some consumers do respond to the claim, as they trust the quality of domestic-made products and/or feel patriotic when they buy American. For example, athletic-shoe maker

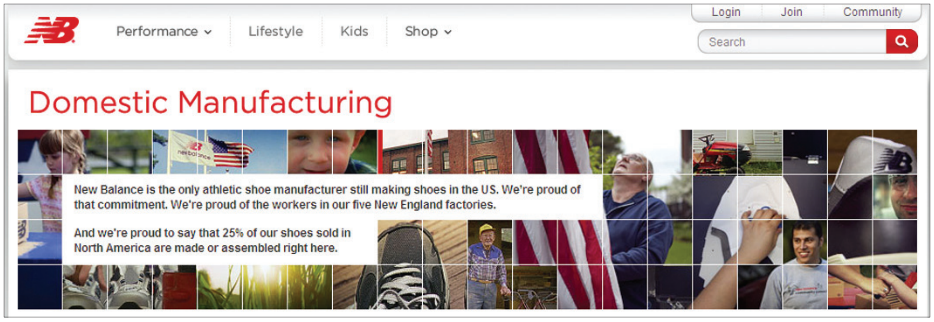


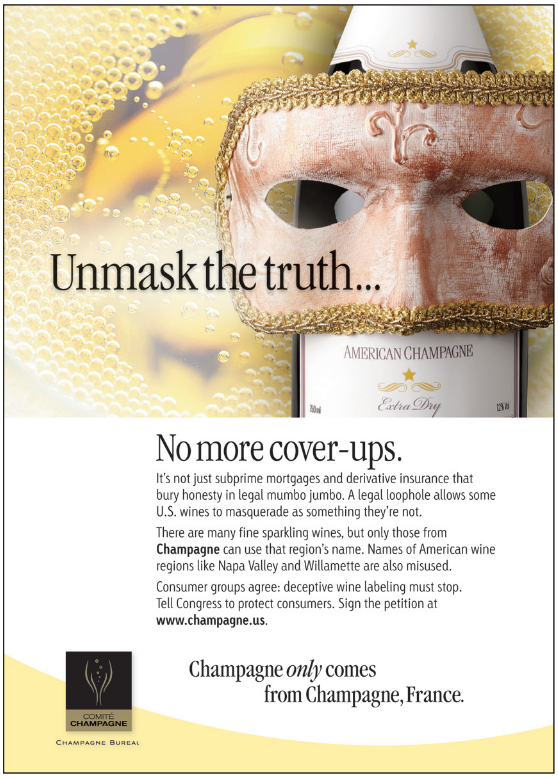

**EXHIBIT 22–10**
New Balance promotes its commitment to U.S. manufacturing

New Balance is a company that promotes its commitment to domestic manufacturing and the fact that 25 percent of its products are made in the United States (Exhibit 22–10).

In December 1998, the FTC issued new guidelines for American-made products. The guidelines spell out what it means by "all or virtually all" in mandating how much U.S. content a product must have to wear a "Made in USA" label or be advertised as such. According to the new FTC guidelines, all significant parts and processing that go into the product must be of U.S. origin and the product should have no or very little foreign content. Companies do not have to receive the approval of the FTC before making a "Made in USA" claim. However, the commission does have the authority to take action against false and unsubstantiated "Made in USA" claims just as it does with other advertising claims.[53]

Another interesting example of a case involving product origin claims is in the wine industry. The U.S. Champagne Bureau recently launched its "Unmask the Truth" ad campaign which has the goals of rallying consumers and demanding lawmakers protect place-of-origin names on wine sold in the United States. The ad, which is shown in Exhibit 22–11, features a mask over a sparkling wine bottle mislabeled "American Champagne" and asks consumers to voice their support for truthful labeling regarding where wine comes from. The campaign is designed to address a loophole in federal law that allows some U.S. sparkling wine producers to mislead consumers by labeling their products "Champagne" even though they do not come from the Champagne region of France. The trade association argues that names of American wine regions such as Napa Valley and Williamette also risk being misused.[54]

**EXHIBIT 22–11**
The U.S. Champagne Bureau is running ads calling for clarification of the region of origin on wine labels




## Advertising Substantiation

A major area of concern to regulatory agencies is whether advertisers can support or substantiate their claims. For many years, there were no formal requirements concerning substantiation of advertising claims. Many companies made claims without any documentation or support such as laboratory tests or clinical studies. In 1971, the FTC's **advertising substantiation** program required advertisers to have supporting documentation for their claims and to prove the claims are truthful.[55] Broadened in 1972, this program now requires advertisers to substantiate their claims before an ad appears. Substantiation is required for all express or implied claims involving safety, performance, efficacy, quality, or comparative price.

The FTC's substantiation program has had a major effect on the advertising industry, because it shifted the burden of proof from the commission to the advertiser. Before the substantiation program, the FTC had to prove that an advertiser's claims were unfair or deceptive.

Ad substantiation seeks to provide a basis for believing advertising claims so consumers can make rational and informed decisions and companies are deterred from making claims they cannot adequately support. The FTC takes the perspective that it is illegal and unfair to consumers for a firm to make a claim for a product without having a "reasonable basis" for the claim.


**EXHIBIT 22–12**

Weight-loss program marketers are now required to substantiate their claims as a result of an FTC ruling

In their decision to require advertising substantiation, the commissioners made the following statement:

> Given the imbalance of knowledge and resources between a business enterprise and each of its customers, economically it is more rational and imposes far less cost on society, to require a manufacturer to confirm his affirmative product claims rather than impose a burden on each individual consumer to test, investigate, or experiment for himself. The manufacturer has the ability, the know-how, the equipment, the time and resources to undertake such information, by testing or otherwise, . . . the consumer usually does not.[56]

Many advertisers respond negatively to the FTC's advertising substantiation program. They argue it is too expensive to document all their claims and most consumers either won't understand or aren't interested in the technical data. Some advertisers threaten to avoid the substantiation issue by using puffery claims, which do not require substantiation.

Generally, advertisers making claims covered by the substantiation program must have available prior substantiation of all claims. However, in 1984, the FTC issued a new policy statement that suggested after-the-fact substantiation might be acceptable in some cases and it would solicit documentation of claims only from advertisers that are under investigation for deceptive practices.

In a number of cases, the FTC has ordered advertisers to cease making inadequately substantiated claims. In 1993, the FTC took on the weight-loss industry when it filed a complaint charging that none of five large, well-known diet program marketers had sufficient evidence to back up claims that their customers achieved their weight-loss goals or maintained the loss. Three of the companies agreed to publicize the fact that most weight loss is temporary and to disclose how long their customers kept off the weight they lost. The agreement required the companies to substantiate their weight-loss claims with scientific data and to document claims that their customers keep off the weight by monitoring a group of them for two years[57] (Exhibit 22–12).

Nearly 10 years later, the FTC held a workshop to once again explore the problem of misleading weight-loss promotional pitches. The FTC used the workshop as a forum to suggest that the media should play a more active role in screening ads for diet products and programs. Professor Herbert Rotfeld has evaluated the FTC's efforts to deal with the problem of deceptive advertising in the weight-loss industry and concludes that its efforts to curb the deceptions have largely failed and that new strategies are needed. He argues that there needs to be more media self-regulation of deceptive weight-loss advertising. However, he also notes that if the FTC wants to see greater screening by the media, they need to give executives from the print and broadcast media a stronger incentive to do so by holding the media companies liable for knowingly carrying deceptive claims.[58]

Recently the FTC has stepped up its action against false and unsubstantiated claims in ads and infomercials. A few years ago, the commission fined the Home Shopping Network $1.1 million for making unsubstantiated advertising claims for two weight-loss products, an acne treatment, and a dietary supplement for menopause and premenstrual syndrome. Under the settlement Home Shopping is enjoined from making product claims about curing and treating diseases without "reliable scientific evidence."

## The FTC's Handling of Deceptive Advertising Cases

**Consent and Cease-and-Desist Orders** Allegations of unfair or deceptive advertising come to the FTC's attention from a variety of sources, including competitors, consumers, other government agencies, or the commission's own monitoring and investigations. Once the FTC decides a complaint is justified and warrants further action, it notifies the offender, who then has 30 days to respond. The

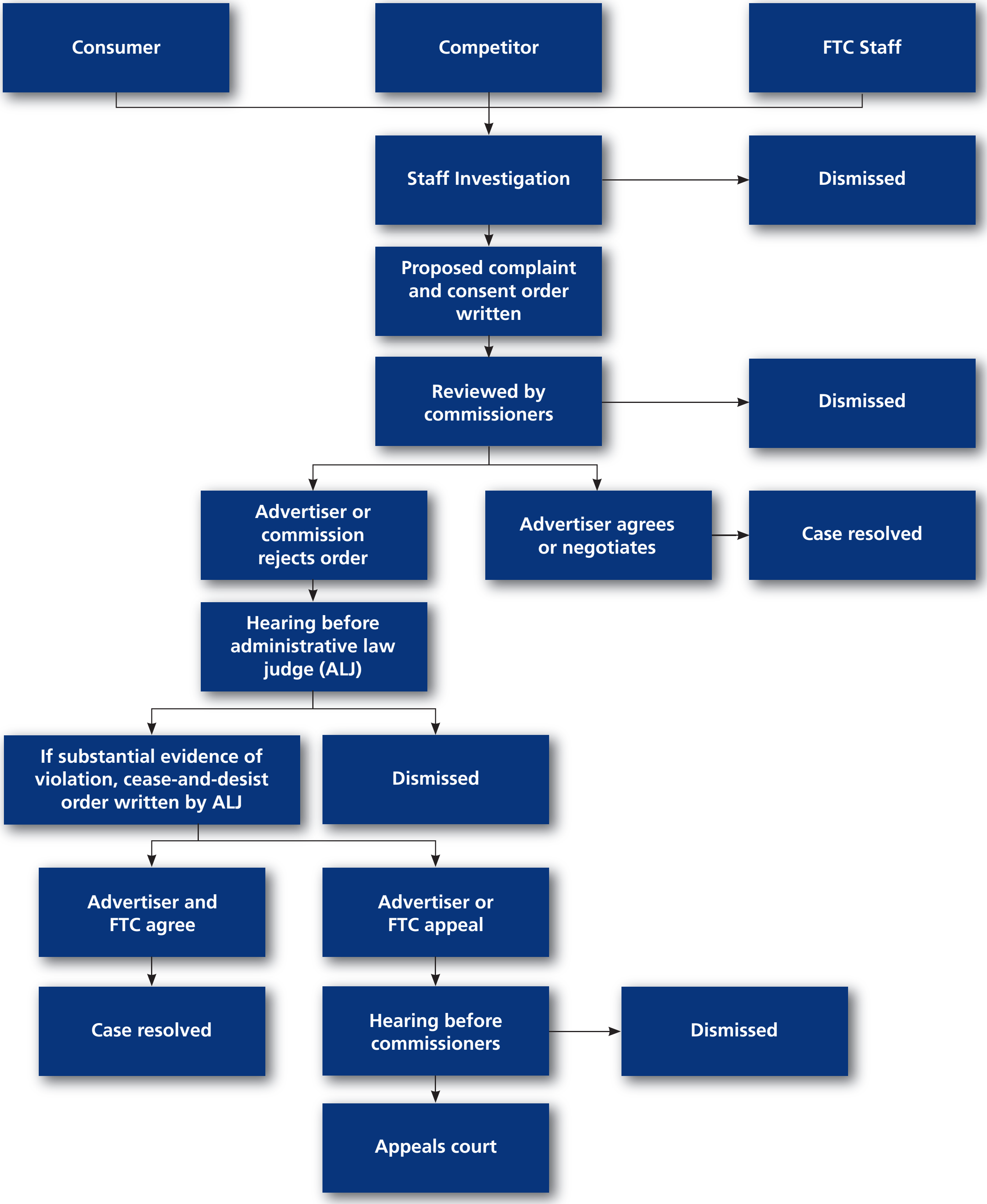



**FIGURE 22–4**

FTC Complaint Procedure

advertiser can agree to negotiate a settlement with the FTC by signing a **consent order**, which is an agreement to stop the practice or advertising in question. This agreement is for settlement purposes only and does not constitute an admission of guilt by the advertiser. Most FTC inquiries are settled by consent orders because they save the advertiser the cost and possible adverse publicity that might result if the case went further.

If the advertiser chooses not to sign the consent decree and contests the complaint, a hearing can be requested before an administrative law judge employed by the FTC but not under its influence. The judge's decision may be appealed to the full five-member commission by either side. The commission either affirms or modifies the order or dismisses the case. If the complaint has been upheld by the administrative law judge and the commission, the advertiser can appeal the case to the federal courts.

The appeal process may take some time, during which the FTC may want to stop the advertiser from engaging in the deceptive practice. The Wheeler-Lea Amendment empowers the FTC to issue a **cease-and-desist order**, which requires that the advertiser stop the specified advertising claim within 30 days and prohibits the advertiser from engaging in the objectionable practice until after the hearing is held. Violation of a cease-and-desist order is punishable by a fine of up to $10,000 a day. Figure 22–4 on page 26 summarizes the FTC complaint procedure.

**Corrective Advertising** By using consent and cease-and-desist orders, the FTC can usually stop a particular advertising practice it believes is unfair or deceptive. However, even if an advertiser ceases using a deceptive ad, consumers may still remember some or all of the claim. To address the problem of residual effects, in the 1970s, the FTC developed a program known as **corrective advertising**. An advertiser found guilty of deceptive advertising can be required to run additional advertising designed to remedy the deception or misinformation contained in previous ads.

The impetus for corrective advertising was another case involving Campbell Soup, which when making a photo for an ad, placed marbles in the bottom of a bowl of vegetable soup to force the solid ingredients to the surface, creating a false impression that the soup contained more vegetables than it really did. (Campbell Soup argued that if the marbles were not used, all the ingredients would settle to the bottom, leaving an impression of fewer ingredients than actually existed!) While Campbell Soup agreed to stop the practice, a group of law students calling themselves SOUP (Students Opposed to Unfair Practices) argued to the FTC that this would not remedy false impressions created by prior advertising and contended Campbell Soup should be required to run advertising to rectify the problem.[59]

Although the FTC did not order corrective advertising in the Campbell case, it has done so in many cases since then. Profile Bread ran an ad stating each slice contained fewer calories than other brands, but the ad did not mention that slices of Profile bread were thinner than those of other brands. Ocean Spray cranberry juice was found guilty of deceptive advertising because it claimed to have more "food energy" than orange or tomato juice but failed to note it was referring to the technical definition of food energy, which is calories. In each case, the advertisers were ordered to spend 25 percent of their annual media budgets to run corrective ads. The STP Corporation was required to run corrective advertising for claims regarding the ability of its oil additive to reduce oil consumption. Many of the corrective ads run in the STP case appeared in business publications to serve notice to other advertisers that the FTC was enforcing the corrective advertising program. The texts of the corrective messages required in each of these cases are shown in Figure 22–5 on page 28.

Corrective advertising is probably the most controversial of all the FTC programs.[60] Advertisers argue that corrective advertising infringes on First Amendment rights of freedom of speech. In one of the most publicized corrective advertising cases ever, involving Listerine mouthwash, Warner-Lambert tested the FTC's legal power to order corrective messages.[61] For more than 50 years Warner-Lambert had advertised that gargling with Listerine helped prevent colds and sore throats or lessened their severity because it killed the germs that caused these illnesses. In 1975, the FTC ruled these claims could not be substantiated and ordered Warner-Lambert to stop making them. In addition, the FTC argued that corrective advertising was needed to rectify the erroneous beliefs that had been created by Warner-Lambert as a result of the large amount of advertising it had run for Listerine over the prior 50 years.

**Profile Bread**

"Hi, [celebrity's name] for Profile Bread. Like all mothers, I'm concerned about nutrition and balanced meals. So, I'd like to clear up any misunderstanding you may have about Profile Bread from its advertising or even its name.

"Does Profile have fewer calories than any other breads? No. Profile has about the same per ounce as other breads. To be exact, Profile has seven fewer calories per slice. That's because Profile is sliced thinner. But eating Profile will not cause you to lose weight. A reduction of seven calories is insignificant. It's total calories and balanced nutrition that count. And Profile can help you achieve a balanced meal because it provides protein and B vitamins as well as other nutrients.

"How does my family feel about Profile? Well, my husband likes Profile toast, the children love Profile sandwiches, and I prefer Profile to any other bread. So you see, at our house, delicious taste makes Profile a family affair."

(To be run in 25 percent of brand's advertising, for one year.)

**Ocean Spray**

"If you've wondered what some of our earlier advertising meant when we said Ocean Spray Cranberry Juice Cocktail has more food energy than orange juice or tomato juice, let us make it clear: we didn't mean vitamins and minerals. Food energy means calories. Nothing more.

"Food energy is important at breakfast since many of us may not get enough calories, or food energy, to get off to a good start. Ocean Spray Cranberry Juice Cocktail helps because it contains more food energy than most other breakfast drinks.

"And Ocean Spray Cranberry Juice Cocktail gives you and your family Vitamin C plus a great wake-up taste. It's . . . the other breakfast drink."

(To be run in one of every four ads for one year.)

**STP**

As a result of an investigation by the Federal Trade Commission into certain allegedly inaccurate past advertisements for STP's oil additive, STP Corporation has agreed to a $700,000 settlement. With regard to that settlement, STP is making the following statement:

"It is the policy of STP to support its advertising with objective information and test data. In 1974 and 1975 an independent laboratory ran tests of the company's oil additive which led to claims of reduced oil consumption. However, these tests cannot be relied on to support the oil consumption reduction claim made by STP.

"The FTC has taken the position that, in making the claim, the company violated the terms of a consent order. When STP learned that the test did not support the claim, it stopped advertising containing that claim. New tests have been undertaken to determine the extent to which the oil additive affects oil consumption. Agreement to this settlement does not constitute an admission by STP that the law has been violated. Rather, STP has agreed to resolve the dispute with the FTC to avoid protracted and prohibitively expensive litigation."

**FIGURE 22–5**

Examples of Corrective Advertising Messages

Warner-Lambert argued that the advertising was not misleading and, further, that the FTC did not have the power to order corrective advertising. Warner-Lambert appealed the FTC decision all the way to the Supreme Court, which rejected the argument that corrective advertising violates advertisers' First Amendment rights. The powers of the FTC in the areas of both claim substantiation and corrective advertising were upheld. Warner-Lambert was required to run $10 million worth of corrective ads over a 16-month period stating, "Listerine does not help prevent colds or sore throats or lessen their severity."

Since the Supreme Court ruling in the Listerine case, there have been several other situations where the FTC has ordered corrective advertising on the basis of the "Warner-Lambert test," which considers whether consumers are left with a latent impression that would continue to affect buying decisions and whether corrective ads are needed to remedy the situation.

In a more recent case involving Novartis Consumer Health Corp.'s Doan's Pills, the FTC sent a strong message to advertisers and agencies that it will require marketers to run corrective ads to remedy any misleading impressions that were created through unsubstantiated advertising claims.[62] In this case, Novartis was ordered to spend $8 million, or the equivalent of the average annual ad budget for Doan's Pills over an eight-year period, on corrective ads to remedy any impressions that might exist from previous advertising that the brand is more effective than other analgesics for relieving back pain. Novartis was ordered to include the statement "Although Doan's is an effective pain reliever, there is no evidence that Doan's is more effective than other pain relievers for back pain" on packaging and in ads until $8 million was spent on the campaign. Novartis appealed the FTC decision ordering corrective advertising. However, the U.S. Court of Appeals unanimously upheld the FTC's right to demand corrective advertising in this case. Also at issue in the appeal was the FTC's standard for determining whether a lingering false impression exists from deceptive advertising and whether the commission has to prove that the years of advertising created the false impression or could assume that years of advertising would have done so. The courts described the evidence of lingering effect the FTC had amassed as "thin and somewhat fragmentary," but upheld the commission's decision based on the record as a whole.[63]

The appeals court decision in this case has very important implications for the FTC as well as for advertisers. The ruling reaffirmed the commission's authority to order corrective advertising and gave it greater freedom to use the remedy, whereas a loss could have limited its authority to do so. The ruling also has repercussions for advertisers who expressed concern over the FTC's contention that "corrective advertising is not a drastic remedy" but is an appropriate method for restoring the status quo. Advertisers fear that this is a sign the FTC will be more willing to apply the remedy in future cases. However, FTC officials indicated that the ruling would not substantially change its request for corrective ads. This appears to be the case thus far.

However, in 2009 another federal agency, the Food and Drug Administration (FDA), ordered Bayer to run a six-month, $20 million corrective advertising campaign for Yaz, the company's birth-control product. The FDA ruled that Bayer's marketing and advertising for Yaz, which is the leading nongeneric in the birth-control market, was deceptive and made false claims regarding its efficacy for acne and premenstrual syndrome. Bayer was ordered to spend nearly a third of the $66.7 million it spent in measured media the prior year on corrective ads and was also required to submit all of its advertising for Yaz to the FDA for approval for the next six years.[64]

## Developments in Federal Regulation by the FTC

By the end of the 1970s, the FTC had become a very powerful and active regulator of advertising. However, Congress was concerned about the FTC's broad interpretation of unfairness, which led to the restrictive legislation of the 1980 FTC Improvements Act. During the 1980s, the FTC became less active and cut back its regulatory efforts, due in large part to the Reagan administration's laissez-faire attitude toward the regulation of business in general. Some feared that the FTC had become too narrow in its regulation of national advertising, forcing companies and consumer groups to seek relief from other sources such as state and federal courts or through self-regulatory groups such as the NAD/NARB.[65]

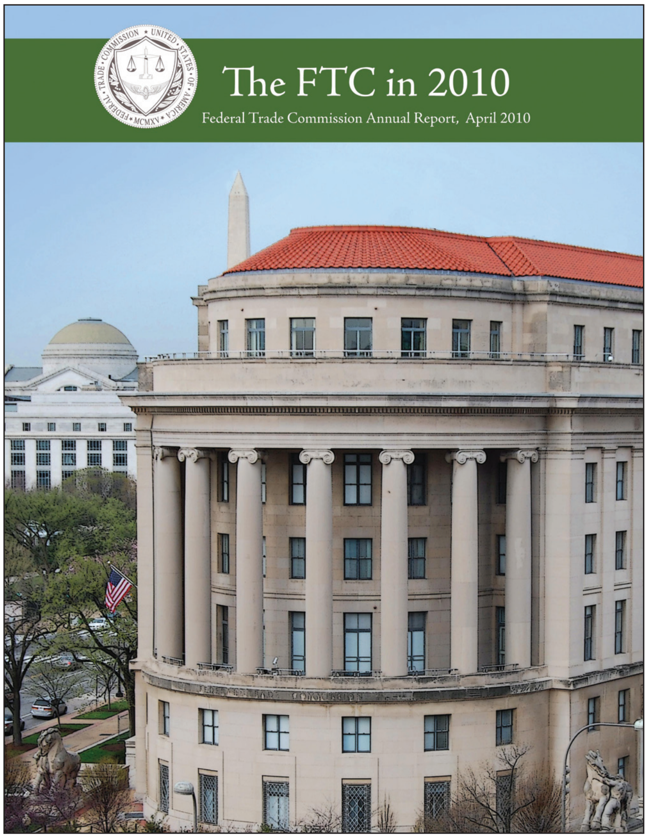
In 1988–89, an 18-member panel chosen by the American Bar Association undertook a study of the FTC as a 20-year follow-up to the 1969 report used by President Richard Nixon to overhaul the commission. The panel's report expressed strong concern over the FTC's lack of sufficient resources and staff to regulate national advertising effectively and called for more funding.

After more than a decade of relative inactivity, the Federal Trade Commission once again became active in the regulation of advertising. The commission showed particular interest in cracking down on misleading advertising in areas such as health, nutrition, weight loss, and environmental claims as well as advertising directed to children and the elderly.[66] The FTC also became more involved with potential fraud and deception through various other promotional methods such as telemarketing, 900 numbers, infomercials, and the Internet. In addition to monitoring deceptive claims made over the Internet, the FTC has become very involved in privacy issues and the collection of personal information on websites.

Robert Pitofsky, who served as FTC chairman during the Clinton administration, focused the commission's attention on developing new policies, particularly as the growth of the Internet created the need for laws and regulations regarding online privacy and ways of protecting children online. However, empirical evidence from a study conducted by Avery Abernethy and George Franke indicates that during this period when the FTC was most active and stringent in requiring advertising substantiation, the objective information contained in advertising actually decreased substantially. Abernethy and Franke suggest that it became more expensive for companies to provide factual information in their ads due to the regulatory burden placed on advertising. Thus, the overall information content of advertising fell, which suggests that increased government regulation can have unintended negative consequences.[67]

Under the Bush administration the FTC focused its attention on the enforcement of existing regulations, particularly in areas such as telemarketing and Internet privacy.[68] The FTC also has focused on eliminating false e-mail advertising and has stepped up its enforcement against senders of deceptive or misleading claims via e-mail. The commission also scrutinized the use of testimonial ads more carefully, particularly with respect to the use of a "results not typical" disclosure in situations where the outcomes are more likely to vary substantially than be typical for most consumers.[69] The FTC has been active in bringing enforcement action against deceptive health claims and companies and principals in the mortgage lending industry for deceptive and unfair practices in servicing mortgage loans. The FTC has also become more involved in the area of environmental marketing and the use of "green" claims for carbon offset, landfill reduction, and sustainable packaging.[70] Deborah Platt Majoras, who was FTC chair during most of the second term of the Bush administration, was a strong proponent of industry self-regulation, but also noted the need for self-regulatory organizations to have sufficient resources to do their job effectively and to be independent of influence from the lobbying efforts of member firms.[71]

**EXHIBIT 22–13**
The FTC issues an *Annual Report* on its activities and initiatives




Under the Obama administration, the FTC is becoming very active in the regulation of advertising as well as of other marketing practices. The administration, along with the new FTC Chairman Jon Leibowitz, have asked Congress to grant the agency increased powers to protect consumers from deceptive practices by unscrupulous providers of financial services and products. In its 2010 *Annual Report,* the FTC has noted that it intends to step up its efforts to stop fraud that targets financially distressed consumers (Exhibit 22–13). The FTC has joined forces with a number of states and other federal agencies to take action against mortgage modification and foreclosure rescue scams; phony debt reduction and credit repair operations; and payday lenders, get-rich-quick schemes, and bogus government grants.[72] To better protect consumers, Leibowitz is also seeking to streamline the FTC's rulemaking procedures, asking for power to bring charges directly against aiders and abettors of financial fraud and expanding the FTC's remedial powers.

The FTC is expected to take a more regulatory approach under the Obama administration rather than relying on the voluntary self-regulation that was used by the commission during the Bush presidency.[73] The FTC is focusing attention on protecting consumers' online privacy and the collection of sensitive information, particularly for those using social media such as Facebook and Twitter. In 2009 it passed a new set of guidelines for online endorsements that requires bloggers to disclose any "material connection" to an advertiser.[74] The new guidelines also call for self-regulation regarding online behavioral targeting, although it is expected that marketers will face more FTC scrutiny in this area.[75] The Federal Trade Commission will continue to be the primary regulator of advertising and marketing practices in the United States, although the direction of the FTC is likely to be influenced by the political party of the presidential administration.

While the FTC is the major regulator of advertising for products sold in interstate commerce, several other federal agencies and departments also regulate advertising and promotion.

## Additional Federal Regulatory Agencies

LO 22-3

**The Federal Communications Commission** The FCC, founded in 1934 to regulate broadcast communication, has jurisdiction over the radio, television, telephone, and telegraph industries. The FCC has the authority to license broadcast stations as well as to remove a license or deny renewal to stations not operating in the public's interest. The FCC's authority over the airways gives it the power to control advertising content and to restrict what products and services can be advertised on radio and TV. The FCC can eliminate obscene and profane programs and/or messages and those it finds in poor taste. While the FCC can purge ads that are deceptive or misleading, it generally works closely with the FTC in the regulation of advertising. For example, the Federal Communications Commission and the FTC held a joint workshop and publicly accused long-distance phone marketers of deceiving consumers in their advertising. Officials of both commissions expressed concern over per-minute ads for long distance and so-called dial-around long-distance services. They also warned long-distance marketers that they would take action if steps were not taken to clean up their advertising.[76]

Many of the FCC's rules and regulations for TV and radio stations have been eliminated or modified. The FCC no longer limits the amount of television time that can be devoted to commercials. (But in 1991, the Children's Television Act went into effect. The act limits advertising during children's programming to 10.5 minutes an hour on weekends and 12 minutes an hour on weekdays.)

Under the Reagan administration, the controversial Fairness Doctrine, which required broadcasters to provide time for opposing viewpoints on important issues, was repealed on the grounds that it was counterproductive. It was argued that the Fairness Doctrine actually reduced discussion of important issues because a broadcaster might be afraid to take on a paid controversial message in case it might be required to provide equal free exposure for opposing viewpoints. It was under this doctrine that the FCC required stations to run commercials about the harmful effects of smoking before passage of the Public Health Cigarette Smoking Act of 1970, which banned broadcast advertising of cigarettes. Many stations still provide time for opposing viewpoints on controversial issues as part of their public service requirement, not necessarily directly related to fairness.

In recent years, the FCC has become very active in enforcing laws governing the airing of obscene, indecent, and profane material. For example, in 2004, the commission fined "shock jock" Howard Stern $495,000 for broadcasting indecent content and also levied fines against Clear Channel Communications, the nation's largest owner of radio stations, which carried his syndicated show.[77] Concern over Stern's constant battling with the FCC led to a decision by Clear Channel to drop his daily radio show.[78] Stern subsequently signed a five-year contract with Sirius Satellite radio, the subscription-based radio service, where his show is not subject to FCC regulations. The FCC also stepped up its enforcement of obscenity in the

**EXHIBIT 22–14**
Janet Jackson's "wardrobe malfunction" during the 2004 Super Bowl half-time show led to greater enforcement of obscenity laws by the FCC

wake of the controversy following the baring of Janet Jackson's breast during the halftime show of the 2004 Super Bowl (Exhibit 22–14).[79] These incidents resulted in federal legislation dramatically increasing the amount both radio and television networks and stations can be fined for broadcast obscenity violations. In 2005, the FCC launched a new website explaining its broadcast obscenity, indecency, and profanity rules as well as complaint procedures and enforcement actions.

The FCC has also recently become involved in issues affecting the area of publicity and public relations. In 2005, the commission issued a missive insisting that broadcasters screen video news releases to ensure that they clearly disclose "the nature, source and sponsorship" of the material. The crackdown is designed to address a marketing practice whereby prepackaged promotional videos sent to TV stations by companies, organizations, and government agencies are represented as news stories.[80] And, as discussed in the chapter opener, the FCC is also currently considering the regulation of the use product placements in television shows.

### The Food and Drug Administration

Now under the jurisdiction of the Department of Health and Human Services, the FDA has authority over the labeling, packaging, branding, ingredient listing, and advertising of packaged foods and drug products, as well as cosmetics. The FDA is authorized to require caution and warning labels on potentially hazardous products and also has limited authority over nutritional claims made in food advertising. This agency has the authority to set rules for promoting these products and the power to seize food and drugs on charges of false and misleading advertising.

Like the FTC, the Food and Drug Administration has become a very aggressive regulatory agency in recent years. The FDA has cracked down on a number of commonly used descriptive terms it believes are often abused in the labeling and advertising of food products—for example, *natural, light, no cholesterol, fat free,* and *organic.* The FDA has also become tougher on nutritional claims implied by brand names that might send a misleading message to consumers. For example, Great Foods of America was not permitted to continue using the HeartBeat trademark under which it sold most of its foods. The FDA argued the trademark went too far in implying the foods have special advantages for the heart and overall health.

**EXHIBIT 22–15**
The Nutritional Labeling and Education Act requires that labels be easy for consumers to understand


Many changes in food labeling are a result of the Nutritional Labeling and Education Act, which Congress passed in 1990. Under this law the FDA established legal definitions for a wide range of terms (such as *low fat, light,* and *reduced calories*) and required straightforward labels for all foods beginning in early 1994 (Exhibit 22–15). In its current form the act applies only to food labels, but it may soon affect food advertising as well. The FTC would be asked to ensure that food ads comply with the new FDA standards.

The FDA has also become increasing active in policing health-related claims for food products. In 2009 General Mills received a warning letter from the FDA for violations stemming from claims the company has been making that eating Cheerios cereal can reduce cholesterol by 4 to 6 percent in six weeks. The FDA charged that the claims made for the product based on clinical studies would make it a drug, not a food, because it is intended for use in the prevention, mitigation, and treatment of disease. General Mills has been working with the FDA to resolve the issue as the cholesterol-reduction claims are an important part of the brand's positioning and used as the basis for much of its advertising.[81]

Another regulatory area where the FDA has been heavily involved is the advertising and promotion of tobacco products. In 1996, President Bill Clinton signed an executive order declaring that nicotine is an addictive drug and giving the FDA board jurisdiction to regulate cigarettes and smokeless tobacco. Many of the regulations resulting from this order were designed to keep teenagers from smoking.[82] However, the tobacco industry immediately appealed the order. While continuing to fight its legal battle with the federal government over the FDA regulations, the tobacco makers did agree to settle lawsuits brought by 46 states against the industry in late 1998 by signing the Master Settlement Agreement. This settlement was considered a better deal for the tobacco industry, as many of the onerous cigarette marketing restrictions contained in the original FDA proposal settlement were missing. The agreement allows large outdoor signs at retailers, whereas the original proposal banned all outdoor ads. The original deal banned all use of humans and cartoons in ads, while the current settlement bans only cartoons and even permits their use on cigarette packs. And while the original proposal eliminated sports sponsorships, the current agreement allows each company to continue one national sponsorship.[83]

An important provision of the Master Settlement Agreement was that the tobacco companies agreed not to target youth (those under the age of 18) in the advertising, promotion, and marketing of tobacco products either directly or indirectly. However, over the past several years there has been considerable debate over whether tobacco companies are complying with the agreement. Much of this debate centers on what is called the 15 percent rule, under which the tobacco companies voluntarily pledged not to advertise in magazines that have more than 15 percent of their readers under the age of 18. Some major tobacco companies such as Philip Morris have stopped advertising in magazines that have a substantial number of youth readers, such as *People, Sports Illustrated, Spin,* and *Rolling Stone*. However, other tobacco companies still advertise in these publications, and it appears that there remains a number of battles to fight in the war over the marketing and advertising of cigarettes.[84]

In 2000, the United States Supreme Court ruled that the Food and Drug Administration did not have the authority to regulate tobacco as a drug, and that Congress would have to specifically enact legislation to allow the FDA to regulate tobacco. As a result, all FDA tobacco regulations were dropped. However, in June 2009 Congress passed a tobacco-control bill giving the FDA sweeping new powers over the packaging, manufacturing, and marketing of tobacco products, and it was signed into law by President Obama shortly thereafter. The Family Smoking Prevention and Tobacco Control Act calls for restrictions on marketing and sales to youths including a ban on all outdoor tobacco advertising within 1,000 feet of schools and playgrounds; a ban on all remaining tobacco-brand sponsorships of sports and entertainment events; a ban on free giveaways of non-tobacco products with the purchase of a tobacco product; a limit on advertising in publications with significant teen readership as well as limiting outdoor and point-of-sale advertising, except in adult-only facilities, to black-and-white ads only; and a restriction on ads on vending machines and self-service displays to adult-only facilities.[85]

Immediately following the passage of the landmark legislation, six tobacco companies along with several other entities, including the Association of National Advertisers and the American Civil Liberties Union, filed a lawsuit in federal court challenging the constitutionality of the new law. The suit argues that the marketing and advertising restrictions laid out in the bill fail to comply with free-speech protections provided by the First Amendment.[86] In January 2010, the federal court ruled that the ban on the use of colors and illustrations does indeed violate the First Amendment, but upheld the remaining parts of the new law. While additional appeals by the tobacco companies are expected, the new law will have a significant impact on the marketing and advertising of tobacco products.

A number of consumer advocacy groups as well as health departments in many states run ads warning consumers against the dangers of smoking and tobacco-related diseases. For example, the American Legacy Foundation, which was established as part of the 1998 tobacco settlement and is dedicated to reducing tobacco use, has run a number of hard-hitting ads warning consumers of the risk of smoking. One of the most successful programs developed by the ALF has been truth®,

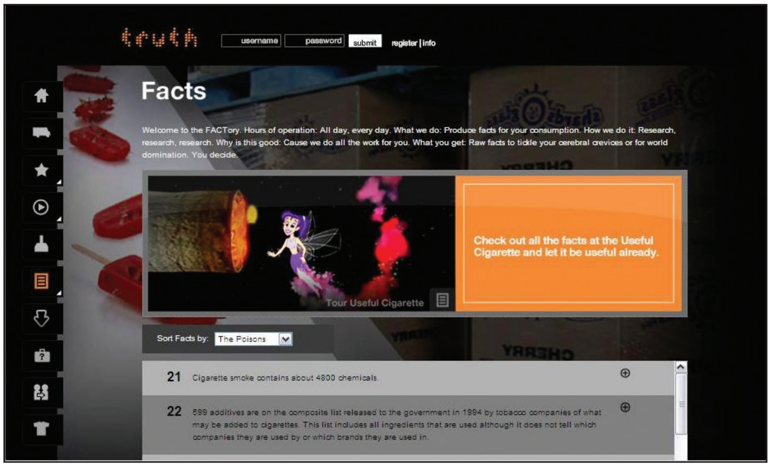



**EXHIBIT 22–16**

truth® has been a very effective youth smoking prevention campaign

which was launched in 2000 and is the largest national youth smoking prevention campaign. Truth® exposes the tactics of the tobacco industry, the truth about addiction, the health effects and consequences of smoking, and is designed to allow teens to make informed choices about tobacco use by giving them the facts about the industry and its products. Truth® is a fully integrated campaign which includes advertising in media that are popular with youth, a summer travel tour that allows teens to engage firsthand with the campaign, and a website (www.thetruth.com) that contains a number of distinctive interactive elements (Exhibit 22–16).

Another area where the Food and Drug Administration has become more involved is the advertising of prescription drugs. Tremendous growth in direct-to-consumer drug advertising has occurred since the FDA issued new guidelines making it easier for pharmaceutical companies to advertise prescription drugs to consumers. A number of studies have been conducted to examine the influence of DTC prescription drug advertising on consumers as well as patient–physician interactions.[87] Ethical Perspective 22–1 on page 36 discusses the concerns over the increase in direct-to-consumer drug advertising and the guidelines and regulations that have been developed by the FDA to address the issue.

### The U.S. Postal Service

Many marketers use the U.S. mail to deliver advertising and promotional messages. The U.S. Postal Service has control over advertising involving the use of the mail and ads that involve lotteries, obscenity, or fraud. The regulation against fraudulent use of the mail has been used to control deceptive advertising by numerous direct-response advertisers. These firms advertise on TV or radio or in magazines and newspapers and use the U.S. mail to receive orders and payment. Many have been prosecuted by the Post Office Department for use of the mail in conjunction with a fraudulent or deceptive offer.

### Bureau of Alcohol, Tobacco, and Firearms

The Bureau of Alcohol, Tobacco, and Firearms (BATF) is an agency within the Treasury Department that enforces laws, develops regulations, and is responsible for tax collection for the liquor industry. The BATF regulates and controls the advertising of alcoholic beverages. The agency determines what information can be provided in ads as well as what constitutes false and misleading advertising. It is also responsible for including warning labels on alcohol advertising and banning the use of active athletes in beer commercials. The BATF can impose strong sanctions for violators. The advertising of alcoholic beverages has become a very controversial issue, with many consumer and public-interest groups calling for a total ban on the advertising of beer, wine, and liquor.

## The Lanham Act

While most advertisers rely on self-regulatory mechanisms and the FTC to deal with deceptive or misleading advertising by their competitors, many companies are filing lawsuits against competitors they believe are making false claims. One piece of federal legislation that has become increasingly important in this regard is the Lanham Act. This act was originally written in 1947 as the Lanham Trade-Mark Act to protect words, names, symbols, or other devices adopted to identify and distinguish a manufacturer's products. The **Lanham Act** was amended to encompass false advertising by prohibiting "any false description or representation including words or other symbols tending falsely to describe or represent the same." While the

FTC Act did not give individual advertisers the opportunity to sue a competitor for deceptive advertising, civil suits are permitted under the Lanham Act.

More and more companies are using the Lanham Act to sue competitors for their advertising claims, particularly since comparative advertising has become so common. For example, a court ordered Ralston Purina to pay Alpo Petfoods $12 million for damages it caused by making false claims that its Purina Puppy Chow dog food could ameliorate and help prevent joint disease. The court ruled that the claim was based on faulty data and that the company continued the campaign after learning its research was in error. Alpo was awarded the money as compensation for lost revenue and for the costs of advertising it ran in response to the Puppy Chow campaign.[88]

Wilkinson Sword and its advertising agency were found guilty of false advertising and ordered to pay $953,000 in damages to the Gillette Co. Wilkinson had run TV and print ads claiming its Ultra Glide razor and blades produced shaves "six times smoother" than Gillette's Atra Plus blades. This case marked the first time an agency was held liable for damages in connection with false claims made in a client's advertising.[89] Although the agency was later found not liable, the case served as a sobering reminder to agencies that they can be drawn into litigation over advertising they create for their clients. To deal with this problem, many agencies insist on indemnification clauses in contracts with their clients.

Suing competitors for false claims was made even easier with passage of the TradeMark Law Revision Act of 1988. According to this law, anyone is vulnerable to civil action who "misrepresents the nature, characteristics, qualities, or geographical origin of his or her or another person's goods, services, or commercial activities." This wording closed a loophole in the Lanham Act, which prohibited only false claims about one's own goods or services. While many disputes over comparative claims are never contested or are resolved through the NAD, more companies are turning to lawsuits for several reasons: the broad information discovery powers available under federal civil procedure rules, the speed with which a competitor can stop the offending ad through a preliminary injunction, and the possibility of collecting damages.[90] However, companies do not always win their lawsuits. Under the Lanham Act you are required to prove five elements to win a false advertising lawsuit containing a comparative claim.[91] You must prove that:

- False statements have been made about the advertiser's product or your product.
- The ads actually deceived or had the tendency to deceive a substantial segment of the audience.
- The deception was "material" or meaningful and is likely to influence purchasing decisions.
- The falsely advertised products or services are sold in interstate commerce.
- You have been or likely will be injured as a result of the false statements, by either loss of sales or loss of goodwill.

**EXHIBIT 22–17**
Comparative claims involving the Prego and Ragu brands of spaghetti sauce resulted in a lawsuit


Over the years there has been a significant increase in the use of comparative advertising, and it has resulted in more and more companies' suing one another under the Lanham Act. In the mid-90s the Campbell Soup Co. advertised that its Prego brand of spaghetti sauce was thicker than Van Den Bergh Food's Ragu brand. Van Den Bergh sued to have Campbell's comparative ads for Prego halted but lost the case in district court as well as in appeals court. Campbell capitalized on its victory by creating an ad based on it. The ad tweaked Ragu by showing snippets of the comparison ads and then a shot of Prego with a breadstick standing up in the sauce (Exhibit 22–17). The tagline was, "Ragu took us to court. We made our case stand. Just like our breadstick." The two companies finally declared a truce in the spaghetti sauce wars in late 1999.[92]

# Ethical Perspective 22–1 > > >

## Direct-to-Consumer Drug Advertising Continues to Come under Attack

For years, pharmaceutical companies marketed most of their prescription drugs directly to physicians, either through their sales force or by advertising in medical journals. However, in 1997, the Food and Drug Administration (FDA) issued new guidelines to make it easier for pharmaceutical companies to advertise prescription drugs on television as well as in print media. Consumers still must have the explicit permission of a physician to buy a prescription medication so drug companies still have the challenge of motivating consumers to see their doctor while touting their brand as a remedy to the problem. However, with the change in guidelines, direct-to-consumer (DTC) drug advertising has exploded, and pharmaceutical companies are some of the largest consumer advertisers.

Direct-to-consumer drug advertising spending soared from $859 million in 1997 to over $5 billion in 2009. Brand-name prescription drugs such as Lipitor, Zoloft, Celebrex, Viagra, and Levitra have become as well-known to consumers as brands of soft drinks. The pharmaceutical companies argue that the increased spending on drug advertising has helped educate consumers about their options and has caused people, who might not do so otherwise, to see doctors about medications. However, a number of physicians, consumers, and health care groups have expressed concern over the increase in drug advertising for several reasons. A major concern is the accuracy of the ads and whether they inform consumers of all the risks associated with taking a drug. Consumer groups asked the Food and Drug Administration to enforce the "fair balance" provision, an FDA regulation governing broadcast commercials that requires drug ads to give both the benefits and the risks of taking a medication.

The FDA is charged with the responsibility of ensuring that drug advertising is fair, balanced, and truthful. However, the number of ads submitted annually for FDA scrutiny, including TV spots, magazine ads, Internet sites, and even pamphlets used by sales representatives has jumped nearly 35 percent over the past 10 years from just over 25,000 to nearly 40,000. However, the number of citation letters issued by the FDA to drug companies for ads that might be false, misleading, or otherwise out of compliance fell from 142 in 1995 to just 43 in 2008. The pharmaceutical companies say that the drop in citations shows that their advertisements are cleaner than before and that they are much more knowledgeable about the FDA guidelines. However, the FDA's director of the Division of Drug Marketing, Advertising, and Communication notes that with its limited resources the division cannot investigate all of the ads, so it focuses on ads deemed most critical: those that appear on television, make unusual claims, or raise a major public health issue.

Consumer advocates have argued for stricter regulations on drug ads noting that while advertisers must include statements about negative side effects or toxicity, the images of people with allergies romping happily outside or of someone who has chronic heartburn downing a pepperoni pizza are what people remember—not the cautionary voiceover. In 2009 the FDA published new advertising guidelines that caution companies not to downplay a drug's risk and/or side effects by using tactics to distract viewers such as loud music or using a typeface smaller than the one used to describe a drug's benefits. Both doctors and critics are also concerned that the ads lead patients to insist on specific drugs when other drugs or lifestyle changes might be better for them.

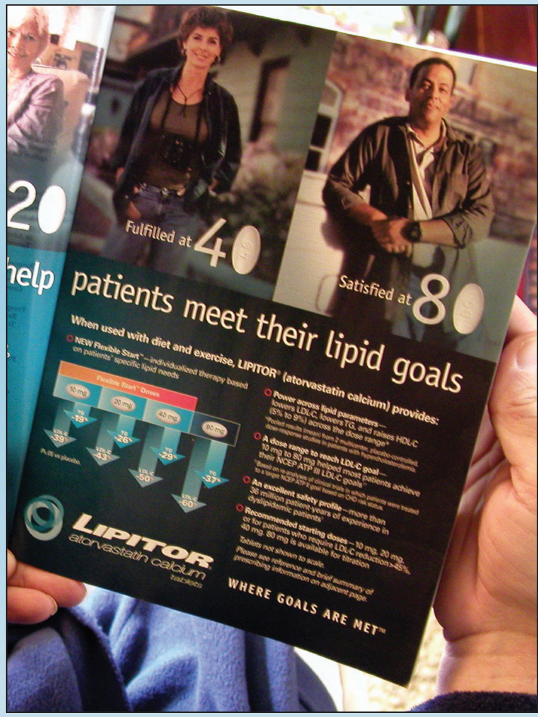
Concerns over DTC drug advertising escalated in the fall of 2004 when Merck and Co. had to pull its popular antiarthritis medication Vioxx from the market after it was determined that the drug increased patients' risk of heart attack. The industry received more negative publicity in 2009 when Pfizer agreed to pay $2.3 billion to settle the largest fraudulent health care marketing case in history. The government

In a recent suit brought under the Lanham Act, PepsiCo sued rival Coca-Cola over the advertising for a new version of the latter's Powerade brand sports drink. The issue in the case was an ad campaign promoting Powerade Ion4 as the "complete sports drink" and better than PepsiCo's Gatorade because it contains four electrolytes while Gatorade contains only two. PepsiCo argued that the Powerade superiority claims were false as there was no evidence that the rival brand was better than Gatorade, and that Powerade had the extra electrolytes in only trace amounts anyway. The case ended up in court where a federal judge denied PepsiCo's request that Coca-Cola stop running the comparative ads (because they had already done so). The judge also ruled that the company had not presented sufficient evidence that brand equity or sales of Gatorade had suffered or that Powerade's campaign had caused irreparable injury to PepsiCo. However, the judge did find evidence of possible misconduct by Coca-Cola for referring to Gatorade as incomplete despite concerns from one of its accused Pfizer of making false and misleading claims of safety and efficacy to promote Bextra for unapproved uses and for dosages above the approved level from 2002 through April 2005. Pfizer also was forced to stop running TV commercials for its blockbuster drug Lipitor, after the government and other critics charged that the ad misrepresented the credentials of Dr. Robert Jarvik who had endorsed the drug. The ad represented Jarvik as a medical expert when most of his career was spent on the invention of the artificial heart.

In 2007 Congress passed legislation giving the FDA more power to regulate DTC drug advertising. The new bill gives the FDA new power to require drug companies to submit TV ads for review before they run, but it can only recommend changes, not require them. The bill also granted the FDA the power to impose fines on a drug company if its ads are found false and misleading. The fines can amount to $250,000 a day for the first violation in any three-year period and up to $500,000 for any subsequent violation over a three-year period. The FDA will also be able to require that DTC ads disclose specific safety risks as well as clear, conspicuous, and neutral statements about any side effects. With newer drugs, the agency can require that the ads disclose the date the product won FDA approval.

Critics of DTC drug advertising have argued that the legislation did not go far enough as the FDA still does not have the authority to block a company from advertising a medication that carries serious safety concerns. However, the pharmaceutical industry is recognizing that it needs to address the problems with DTC advertising. In 2005, the Pharmaceutical Research and Manufacturers of America (PhRMA), the industry's trade organization, released its Guiding Principles on Direct-to-Consumer Advertisements about Prescription Medications. The voluntary guidelines called for better presentation of risk information and for drug companies to spend an appropriate amount of time to educate health care professionals about a new drug product, including the risks and benefits. However, critics argue that the PhRMA developed its own standards to preempt stricter guidelines that the FDA might impose.

Recently legislators have considered ending the tax deduction for drug ads as a way to raise money to help




pay for the federal government's new health care overhaul. Some critics have even called for a total ban on all DTC drug advertising, noting that the United States is one of only two countries that permit the practice. The other is New Zealand where there have been several attempts to ban DTC drug advertising. While it is unlikely that there will be a total ban on this advertising, the message being sent continues to be clear—industry heal thyself.

Sources: Rich Thomaselli, "Medical Groups Mum on DTC Ads," *Advertising Age,* February 28, 2008, pp. 4, 30; Rich Thomaselli, "Pharma Biz Cops to $5 Billion Drug Problem," *Advertising Age,* pp. 3, 39; Rich Thomaselli, "Pfizer to Pay $2.3 Billion in Fraudulent-Marketing Suit," *Advertising Age,* September 2, 2009, http://adage.com/print?article_id=138763; Natasha Singer, "Lawmakers Seek to Curb Drug Commercials," *The New York Times,* July 27, 2009, http://www.nytimes.com/2009/07/27/business/media/27drugads.html.



research scientists about the claim. Coca-Cola dropped the comparative claims for Powerade and both sides claimed victory in the case.[93]

Marketers using comparative ads have to carefully consider whether their messages have the potential to mislead consumers or may overstate their brand's performance relative to that of competitors. In some cases, a competitor may run an ad challenging a rival's claim if they feel that it misleading or is not based on accurate information. For example, Exhibit 22–18 on page 38 shows an ad run recently by the TaylorMade Golf Company challenging rival Callaway's claim of its driver being the number one driver used on the Professional Golf Association tour. Note how the ad provides information to substantiate TaylorMade's claim that it is the number one driver on tour. A study by Michael J. Barone and his colleagues provides a framework for developing measures to assess the misleading effects that may arise from various types of comparative advertising.[94]


**EXHIBIT 22–18**
TaylorMade ran this ad to challenge rival Callaway's claim of having the #1 driver on the PGA Tour

## STATE REGULATION

In addition to the various federal rules and regulations, advertisers must also concern themselves with numerous state and local controls. An important early development in state regulation of advertising was the adoption in 44 states of the *Printers Ink* model statutes as a basis for advertising regulation. These statutes were drawn up in 1911 by *Printers Ink,* for many years the major trade publication of the advertising industry. Many states have since modified the original statutes and adopted laws similar to those of the Federal Trade Commission Act for dealing with false and misleading advertising. For example, in California, the Business and Professional Code prohibits "unlawful, unfair, or fraudulent" business practices and "unfair, deceptive, untrue, or misleading advertising."

In addition to recognizing decisions by the federal courts regarding false or deceptive practices, many states have special controls and regulations governing the advertising of specific industries or practices. As the federal government became less involved in the regulation of national advertising during the 1980s, many state attorneys general (AGs) began to enforce state laws regarding false or deceptive advertising. For example, the attorneys general in New York and Texas initiated investigations of Kraft ads claiming the pasteurized cheese used in Cheez Whiz was real cheese.[95] The well-publicized "monster truck" deceptive advertising case involving Volvo and its advertising agency that occurred in the early 90s was initiated by the attorney general's office in the state of Texas.[96]

LO 22-3

The **National Association of Attorneys General (NAAG)** moved against a number of national advertisers as a result of inactivity by the FTC during the Reagan administration. In 1987, the NAAG developed enforcement guidelines on airfare advertising that were adopted by more than 40 states. The NAAG has also been involved in other regulatory areas, including car-rental price advertising as well as advertising dealing with nutrition and health claims in food ads. The NAAG's foray into regulating national advertising raises the issue of whether the states working together can create and implement uniform national advertising standards that will, in effect, supersede federal authority. An American Bar Association panel concluded that the Federal Trade Commission is the proper regulator of national advertising and recommended the state AGs focus on practices that harm consumers within a single state.[97] This report also called for cooperation between the FTC and the state attorneys general. In recent years state attorneys general have been working with the FTC and other federal government agencies on false advertising cases. For example, 27 state attorneys general worked with the FDA in the deceptive advertising case for Bayer's Yaz birth control pill that resulted in corrective advertising. A group of state attorneys general also worked with the FTC in a recent case against the makers of Airborne, a multivitamin and herbal supplement whose labels and ads falsely claimed that the product cures and prevents colds. Airborne had been making the false claims since 1999 and agreed to refund the money to consumers who had bought the product, as part of a $23.3 million class action settlement.[98]

Advertisers are concerned about the trend toward increased regulation of advertising at the state and local levels because it could mean that national advertising campaigns would have to be modified for every state or municipality. Yet the FTC takes the position that businesses that advertise and sell nationwide need a national advertising policy. While the FTC recognizes the need for greater cooperation with the states, the agency believes regulation of national advertising should be its responsibility.[99] Just in case, the advertising industry is still keeping a watchful eye on changes in advertising rules, regulations, and policies at the state and local levels.

## REGULATION OF OTHER PROMOTIONAL AREAS

LO 22-4

So far we have focused on the regulation of advertising. However, other elements of the promotional mix also come under the surveillance of federal, state, and local laws and various self-regulatory bodies. This section examines some of the rules, regulations, and guidelines that affect sales promotion, direct marketing, and marketing on the Internet.

### Sales Promotion

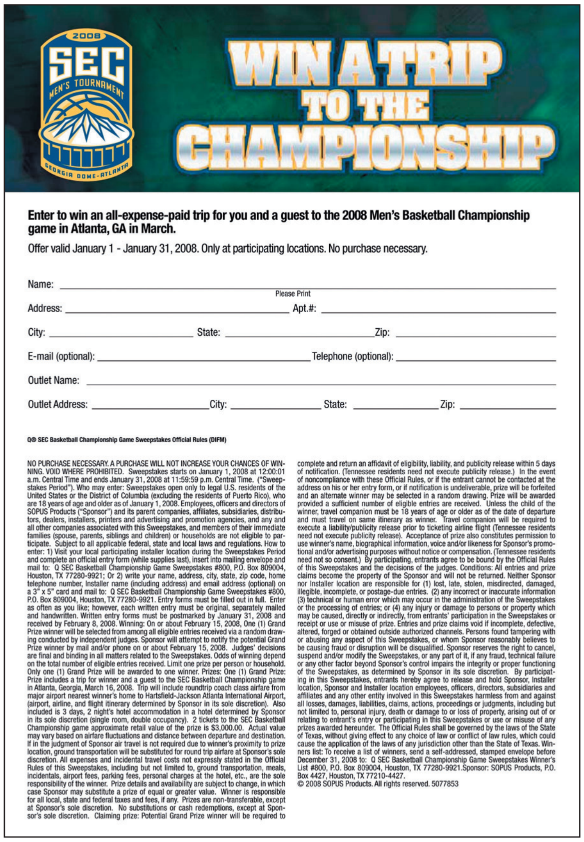
Both consumer- and trade-oriented promotions are subject to various regulations. The Federal Trade Commission regulates many areas of sales promotion through the Marketing Practices Division of the Bureau of Consumer Protection. Many promotional practices are also policed by state attorneys general and local regulatory agencies. Various aspects of trade promotion, such as allowances, are regulated by the Robinson-Patman Act, which gives the FTC broad powers to control discriminatory pricing practices.

**Contests and Sweepstakes** As noted in Chapter 16, numerous legal considerations affect the design and administration of contests and sweepstakes, and these promotions are regulated by a number of federal and state agencies. There are two important considerations in developing contests (including games) and sweepstakes. First, marketers must be careful to ensure their contest or sweepstakes is not classified as a *lottery,* which is considered a form of gambling and violates the Federal Trade Commission Act and many state and local laws. A promotion is considered a lottery if a prize is offered, if winning a prize depends on chance and not skill, and if the participant is required to give up something of value in order to participate. The latter requirement is referred to as *consideration* and is the basis on which most contests, games, and sweepstakes avoid being considered lotteries. Generally, as long as consumers are not required to make a purchase to enter a contest or sweepstakes, consideration is not considered to be present and the promotion is not considered a lottery.

The second important requirement in the use of contests and sweepstakes is that the marketer provide full disclosure of the promotion. Regulations of the FTC, as well as many state and local governments, require marketers using contests, games, and sweepstakes to make certain all of the details are given clearly and to follow prescribed rules to ensure the fairness of the game.[100] Disclosure requirements include the exact number of prizes to be awarded and the odds of winning, the duration and termination dates of the promotion, and the availability of lists of winners of various prizes (Exhibit 22–19). The FTC also has specific rules governing the way games and contests are conducted, such as requirements that game pieces be randomly distributed, that a game not be terminated before the distribution of all game pieces, and that additional pieces not be added during the course of a game.

A number of states have responded to concerns over fraud on the part of some contest and sweepstakes operators. In 1995, at least 13 states either passed or tightened prize notification laws, requiring fuller disclosure of rules, odds, and the retail value of prizes. And many of the states are following through with tougher enforcement of these laws. For example, Publishers Clearing House, known for its million-dollar giveaways, agreed to pay $490,000 to 14 states and to

**EXHIBIT 22–19**
Marketers are required to provide consumers with full details of a contest or sweepstakes






CHAPTER 22

change some of its language, better defining terms like "finalist" and "tie breaker." It also began to disclose the odds of winning prizes. More recently the controversy resulting from the lawsuits filed against American Family Publishing for misleading consumers regarding their odds of winning large cash prizes in its annual magazine subscription solicitation sweepstakes has led to investigations and stricter regulation of sweepstakes in a number of states. For example, New York passed a law requiring the odds of winning a sweepstakes "must be conspicuously disclosed in the same type face, size and boldness and adjacent to the most prominent listing of the prizes on the front of the first page of the offer." The state law also prohibits statements that someone is a "winner" or that his or her name "has been selected" when no prize has been won. The law carries a fine of $1,000 per incident, which could be $1,000 per letter received by New York residents. Some of the most ambitious legal actions are taking place in individual states, where prosecutors are taking sweepstakes and contest companies to court for misleading and deceptive practices.[101]

**Premiums** Another sales promotion area subject to various regulations is the use of premiums. A common problem associated with premiums is misrepresentation of their value. Marketers that make a premium offer should list its value as the price at which the merchandise is usually sold on its own. Marketers must also be careful in making premium offers to special audiences such as children. While premium offers for children are legal, their use is controversial; many critics argue that they encourage children to request a product for the premium rather than for its value. The Children's Advertising Review Unit has voluntary guidelines concerning the use of premium offers. These guidelines note that children have difficulty distinguishing a product from a premium. If product advertising contains a premium message, care should be taken that the child's attention is focused primarily on the product. The premium message should be clearly secondary. Conditions of a premium offer should be stated simply and clearly. "Mandatory" statements and disclosures should be stated in terms that can be understood by the child audience.[102] However, a recent study of children's advertising commissioned by CARU found the single most prevalent violation involved devoting virtually an entire commercial message to information about a premium. CARU guidelines state that advertising targeted to children must emphasize the product rather than the premium offer.[103]

Trade Allowances Marketers using various types of trade allowances must be careful not to violate any stipulations of the Robinson-Patman Act, which prohibits price discrimination. Certain sections of the Robinson-Patman Act prohibit a manufacturer from granting wholesalers and retailers various types of promotional allowances and/or payments unless they are made available to all customers on proportionally equal terms.[104] Another form of trade promotion regulated by the Robinson-Patman Act is vertical cooperative advertising. The FTC monitors cooperative advertising programs to ensure that co-op funds are made available to retailers on a proportionally equal basis and that the payments are not used as a disguised form of price discrimination.

As noted in Chapter 16, another trade promotion area where the FTC is becoming involved is the use of slotting fees or allowances paid to retailers for agreeing to handle a new product. In 1999, the Senate Committee on Small Business charged retailers in the grocery, drugstore, and computer software industries with illegally using slotting fees to lock out competitors and prevent consumers from having their choice of the best products. Packaged-goods marketers and retailers have argued that examining slotting fees alone is unfair since they are just part of a wide variety of inducements marketers use to secure the best shelf space. The FTC is investigating the use of slotting fees as anticompetitive weapons that make it difficult for small-size companies to secure retail shelf space.[105] In 2000, the FTC launched its first direct attack on slotting fees when it accused McCormick & Co., the leading spice maker, of offering discriminatory discounts on its products to several grocery chains.

McCormick agreed to settle a complaint that the discounts were a way of paying some retailers disproportionately more in slotting fees than others. The FTC charged that the slotting fees were a way for McCormick to gain more shelf space at the expense of smaller rivals. The practice that was deemed illegal by the FTC is a standard way of doing business in the grocery trade as well as other industries, and some legal experts have argued that this case could impact the use of slotting fees in the future.[106]

**Direct Marketing** As we saw in Chapter 14, direct marketing is growing rapidly. Many consumers now purchase products directly from companies in response to TV and print advertising or direct selling. The Federal Trade Commission enforces laws related to direct marketing, including mail-order offers, the use of 900 telephone numbers, and direct-response TV advertising. The U.S. Postal Service enforces laws dealing with the use of the mail to deliver advertising and promotional messages or receive payments and orders for items advertised in print or broadcast media.

A number of laws govern the use of mail-order selling. The FTC and the Postal Service police direct-response advertising closely to ensure the ads are not deceptive or misleading and do not misrepresent the product or service being offered. Laws also forbid mailing unordered merchandise to consumers, and rules govern the use of "negative option" plans whereby a company proposes to send merchandise to consumers and expects payment unless the consumer sends a notice of rejection or cancellation.[107] FTC rules also encourage direct marketers to ship ordered merchandise promptly. Companies that cannot ship merchandise within the time period stated in the solicitation (or 30 days if no time is stated) must give buyers the option to cancel the order and receive a full refund.[108]

Another area of direct marketing facing increased regulation is telemarketing. With the passage of the Telephone Consumer Protection Act of 1991, marketers who use telephones to contact consumers must follow a complex set of rules developed by the Federal Communications Commission. These rules require telemarketers to maintain an in-house list of residential telephone subscribers who do not want to be called. Consumers who continue to receive unwanted calls can take the telemarketer to state court for damages of up to $500. The rules also ban telemarketing calls to homes before 8:00 a.m. and after 9:00 p.m., automatic dialer calls, and recorded messages to emergency phones, health care facilities, and numbers for which the call recipient may be charged. They also ban unsolicited junk fax ads and require that fax transmissions clearly indicate the sender's name and fax number.[109]

The Federal Trade Commission has also been actively involved with the regulation of advertising that encourages consumers to call telephone numbers with a 900 prefix, whereupon they are automatically billed for the call. While there are many legitimate uses for 900-number technology, it has also been heavily used for sleazy sex operations, contest scams, and other unscrupulous activities.[110] One area of particular concern to the FTC has been ads targeting children and encouraging them to call 900 numbers. In 1993, the FTC issued its 900-Number Rule for advertising directed at children. The rule restricts advertisers from targeting children under the age of 12 with ads containing 900 numbers unless they provide a bona fide educational service. The rule also requires that 900-number ads directed at those under the age of 18 must contain a "clear and conspicuous" disclosure statement that requires the caller to have parental/guardian permission to complete the call. The rule also obligates advertisers to disclose the cost of the call and give the caller the opportunity to hang up without incurring any costs.[111]

The FTC enacted the 900-Number Rule under the provision that it would be reviewed within four years to consider its costs and benefits.[112] This review was undertaken and the rule was retained and revised, although under a new name. The name was changed to the Pay-Per-Call Rule, and in 1998 the rule was revised to give the FTC the authority to broaden its scope and add new provisions. Among other things, the new provisions combat telephone bill cramming, which is the placing of unauthorized charges on consumers' phone bills.[113]

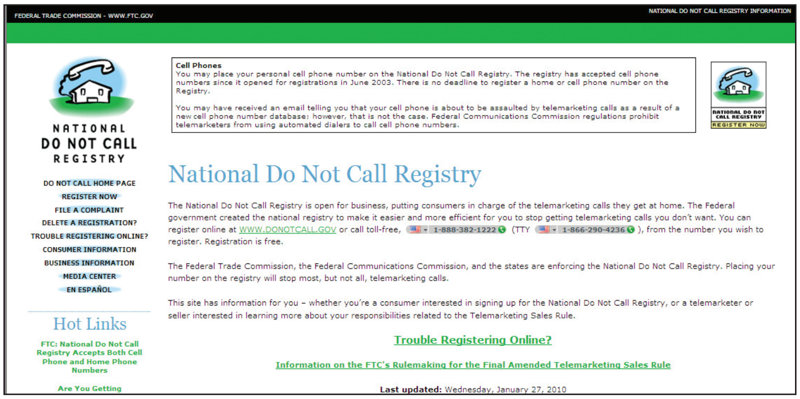



**EXHIBIT 22–20**

The National Do Not Call Registry protects consumers from calls by telemarketers

In 2003, Congress approved a Federal Trade Commission proposal for the formation of a National Do Not Call Registry allowing consumers to opt out of most commercial telemarketing.[114] Consumers can place their home phone numbers, as well as personal cell phone numbers, on the National Do Not Call Registry (Exhibit 22–20). Commercial telemarketers must pay a fee to access the registry and generally are prohibited from calling the listed numbers. Telemarketers have three months to comply once a number goes on the list, and a consumer's registration lasts five years. Political and charitable solicitation calls are not affected by the regulation, and telemarketers can call consumers with whom they have an established relationship. Marketers face penalties of $11,000 per incident for calling someone on the list. The Federal Trade Commission, the Federal Communications Commission, and individual states are enforcing the National Do Not Call Registry, which contained nearly 192 million phone numbers as of the end of 2009.

The National Do Not Call Registry affects the direct-marketing industry as it greatly reduces the number of households that telemarketers can call. As might be expected, the direct-marketing industry is strongly opposed to the registry, arguing that it violates their First Amendment rights and, further, that such a program is not needed. The Direct Marketing Association (DMA), which is the primary trade group for the direct-marketing industry, has argued that consumers already have a number of do-not-call options. They can ask to be excluded from an individual company's telemarketing list at the same time they can sign up with state lists or pay $5 to sign up on the voluntary national list maintained by the Direct Marketing Association. The DMA argues that the national registry will impose more bureaucracy on the direct-marketing industry and that the same goal can be achieved by the industry itself with better education and enforcement.

The Direct Marketers Association and the American Teleservices Association, which represent callers, challenged the legality of the registry on the grounds that it took away their rights to First Amendment–protected speech and that it was excessive and poorly drafted, with competitive marketers forced to abide by different rules. However, in February 2004, the U.S. Court of Appeals upheld the registry's validity, ruling that it is a valid commercial speech regulation. The appellate court said that because the registry doesn't affect political or charitable calls and because there is a danger of abusive telemarketing and invasion of consumer privacy from telemarketers, the government has a right to regulate its use. The two major trade associations have been reviewing the ruling and may yet appeal the case to the U.S. Supreme Court.[115]

Direct marketers have been adjusting their telemarketing strategies to deal with the restrictions imposed by the Do Not Call Registry. They are focusing more attention on generating leads through promotional efforts such as sweepstakes and direct-mail programs, prompting consumers to opt in and agree to receive calls from direct marketers.[116] Some industry experts as well as academics argue that the Do Not Call Registry may actually improve telemarketing practice and the general efficiency of the business because direct marketers must focus more attention on consumers who are receptive to receiving their telemarketing calls.[117] However, there is also concern that some companies are finding loopholes in the rules governing the Do Not Call Registry. For example, one technique that has emerged is the use of a marketing tool called a "lead card," which invites a recipient to mail a reply card for free information. However, the cards often fail to warn consumers that by sending a reply, they are giving up their right to avoid telephone solicitations from the sender—even if their phone numbers are listed on the Do Not Call list.[118]

Another tactic being used by some companies to avoid the Do Not Call Registry is to use sweepstakes entry forms as a way to harvest consumers' telephone numbers for telemarketing purposes. When done correctly, this may be a legitimate direct-marketing tool; however the FTC has cracked down on some companies that have violated Do Not Call regulations by calling phone numbers obtained via sweepstakes entry forms. Companies that want to collect telemarketing leads through a sweepstakes entry form must clearly and conspicuously disclose that their entry-form information will be used for telemarketing purposes and include a statement to be signed by consumers expressing agreement under the Do Not Call provision.[119]

The direct-marketing industry is also scrutinized by various self-regulatory groups, such as the Direct Marketing Association and the Direct Selling Association, that have specific guidelines and standards member firms are expected to adhere to and abide by. However, as discussed in IMC Perspective 22–3 on page 44, some critics argue that these self-regulatory groups are not doing enough to keep consumers from receiving unwanted marketing messages, such as calls from telemarketers and direct-mail offers and solicitations. Thus, it is likely that they will continue to call for more government intervention and regulations.

## Marketing on the Internet

The rapid growth of the Internet as a marketing tool has created a new area of concern for regulators. The same consumer protection laws that apply to commercial activities in other media apply to online as well. The Federal Trade Commission Act, which prohibits "unfair or deceptive acts or practices," encompasses Internet advertising, marketing, and sales. Claims made in Internet ads or on websites must be substantiated, especially when they concern health, safety, or performance, and disclosures are required to prevent ads from being misleading and to ensure that consumers receive material information about the terms of a transaction. There are several areas of particular concern with regard to marketing on the Internet. These include privacy issues, online marketing to children, and the use of spam or unsolicited e-mails for commercial purposes.

The major privacy issue regarding the Internet that has emerged involves undisclosed profiling whereby Web marketers can profile a user on the basis of name, address, demographics, and online/offline purchasing data. Marketers have suggested that profiling offers them an opportunity to target specific niches and reach consumers with custom-tailored messages. However, the FTC has stated that Internet sites that claim they don't collect information but permit advertisers to surreptitiously profile viewer sites are violating consumer protection laws and are open to a charge of deception.[120] In 1999, DoubleClick, the company that is the leader in selling and managing online advertising as well as tracking Web users and now owned by Google, set off a controversy by connecting consumers' names, addresses, and other personal information with information it collects about where consumers go on the Internet. The controversy resulted in the company being investigated by the Federal Trade Commission and lawsuits being filed in some states.[121]

In response to the profiling controversy, companies that collect Internet usage data and information joined together under the banner of the Network Advertising Initiative (NAI) to develop a self-regulatory code.[122] The NAI has developed a set of privacy principles in conjunction with the Federal Trade Commission that provides consumers with explanations of Internet advertising practices and how the practices affect both consumers and the Internet itself. The NAI has also launched a website (www.networkadvertising.org) that provides consumers with information about online advertising practices and gives them the choice to opt out of targeted advertising delivered by NAI member companies (Exhibit 22–21 on page 46). Another industry-driven initiative is the Platform for Privacy Preferences (P3P), which is a

## IMC Perspective 22–3 > > >

### Direct Mail Comes under Attack

If you are a typical consumer, every time you go to the mailbox it is likely you will find numerous forms of direct mail including advertising circulars, preapproved credit-card applications, postcards, brochures, and catalogs—most of which are unsolicited. It is estimated the typical American household receives about 40 pounds of direct mail each year, despite the fact that much of it goes unopened and only about 2 percent is responded to. Every time you order something over the phone, Internet, or through the mail; subscribe to a magazine; enter a contest or sweepstakes; apply for a credit card or become a member of a group; your name and address is captured and put on a list. While marketers maintain these lists to keep track of their own customers and prospects, they often sell your name and address to another company that wants to reach you—which means you are likely to receive even more unsolicited "junk mail." However, direct mail is the latest traditional marketing tactic being challenged by consumers as they continue to take control over the marketing messages they receive.

Consumer advocacy groups won a major battle against direct marketers at the beginning of the new millennium by lobbying the federal government to create a National Do Not Call Registry to protect consumers from unwanted calls from telemarketers. Since its creation in 2003, Americans have registered 192 million phone numbers on the list, thus shielding themselves from most phone solicitations. Now it appears that consumers are tired of seeing their mailboxes bulging with catalogs as well as other forms of direct mail and want to take action. A number of states are considering legislation to create state-run Do Not Mail list registries that would allow consumers to keep unsolicited direct mail out of their mailboxes.

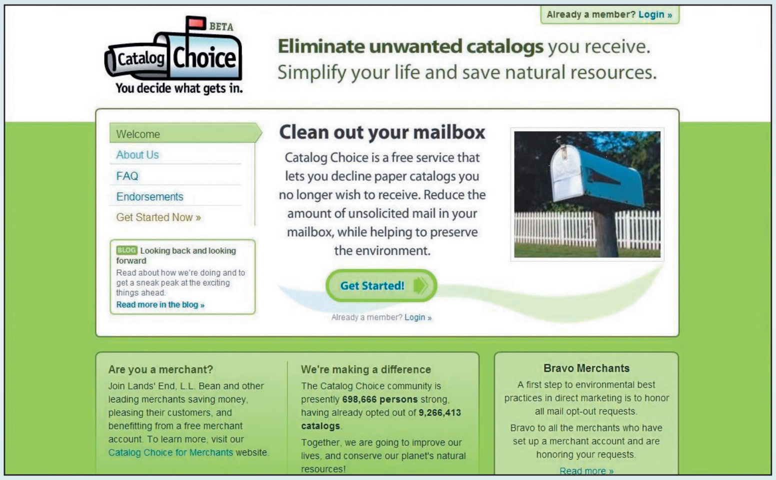
Thus far, none of the proposed Do Not Mail bills have made it beyond the hearing stage and it may take years before any type of legislation is enacted. However, a number of advocacy groups are not waiting for the government to address the problem and are taking steps to help consumers reduce the amount of unwanted direct mail they are receiving. Sever of these initiatives have been started by groups that are interested in reducing the environmental impact created by the direct-mail industry. Environmental groups claim American households receive 19 billion catalogs of various shapes and sizes each year and estimate that it takes 53 million trees to produce the 3.6 million tons of paper in those catalogs. When the energy required to make the paper and ship the catalog is added in, the groups argue that the process adds 5.2 million tons of carbon dioxide emissions to the atmosphere yearly, equal to the emissions of 2 million cars.

One initiative having a significant impact in terms of reducing the amount of direct mail is Catalog Choice, which was launched in October 2007 by the Ecology Center and is endorsed by the National wildlife Federation and the Natural Resources Defense Council. The mission of Catalog Choice is to reduce the number of repeat and unsolicited catalog mailings, and promote the adoption of sustainable industry best practices. The nonprofit group offers an online service that allows people to compile a list of catalogs they do not want to receive. The service then contacts the retailers with a request to take the person's name off their mailing list or makes a downloadable file available that merchants can then feed into their direct-mail database. By 2010, more than 1.2 million people had registered with Catalog Choice and opted out of receiving more than 10 million catalogs. Several hundred merchants have agreed to abide by the site's opt out requests including major companies such as Lands' End, Office Depot, and REI.

The direct-mail industry has noticed the growing popularity of Catalog Choice and other sites that allow consum-

new technology that lets consumers screen websites via operating system software. This technology gives consumers greater control over the collection of information by allowing them to specify their privacy preferences electronically and screen out websites that do not meet these preferences. The privacy debate is likely to escalate, and it is expected that legislation will be introduced to force companies to seek consumers' approval before sharing personal information captured from their websites.

While these proposals are aimed at protecting the privacy rights of adults, one of the biggest concerns is over restricting marketers whose activities or websites are targeted at children. These concerns over online marketing to children led to the passage of the **Children's Online Privacy Protection Act** of 1998 **(COPPA)**, which the FTC began enforcing in April 2000.[123] This act places tight restrictions on collecting information from children via the Internet and requires that websites directed at children and young teens have a privacy policy posted on their home page and areas of the site where information is collected. The law also requires websites ers to have their names removed from mailing lists. The industry's primary trade organization, the Direct Marketing Association, is responding to the attacks on the use of direct mail by its members. A spokesperson for the DMA notes that 1.7 million trees are planted every day in the United States to replace trees cut down for paper and wood products. He also argues that Americans can save 3.3 billion miles of driving if everyone eliminated two trips to a mall per year and shopped by catalog instead. This would prevent a billion tons of carbon emissions from entering the atmosphere and save 290 million gallons of gasoline.




The DMA also notes that it offers a Mail Preference Service (MPS) that, for $1, will put a person's name on a Do Not Mail list for three years. The service is supported by the United States Postal Service and has more than 4.5 million subscribers. The online service prevents companies from adding the person's name to their lists, but it does not stop catalogs and other mail solicitations the person is already receiving. The DMA has also questioned the integrity of the data gathered by third parties such as Catalog Choice and expressed concerns over how marketers can verify the legitimacy of the names and what might be done with them. However, a project manager for Catalog choice notes that this concern is unfounded since the organization uses the same e-mail verification system as the Federal Trade Commission's National Do Not Call Registry.

In 2006 the DMA, along with a number of other mailing community associations and companies, formed a direct-mail advocacy group. Mail Moves America, that is working with state business groups and communicating with legislators about the importance of direct mail for consumers, businesses, and the economy and is lobbying against the creation of a Do Not Mail list. The group notes that direct mail is a large and diverse part of the economy that creates nearly $700 billion of economic activity annually and would be adversely affected if a Do Not Mail bill is passed in any state. MMA also argues that legislation is not needed to provide consumers with options for removing their names from marketing lists, as they already have a variety of options for doing so, ranging from contacting an individual company, to registering their name with the DMA's Mail Preference Service.

Proponents of groups such as Catalog choice acknowledge many people want to get catalogs and other forms of direct mail. However, they argue that American consumers do not want most of the tons of junk mail they receive every year as it comes from companies they have never bought anything from and/or have no interest in buying from. Of course, it will ultimately be consumers who decide if they want to put a no-trespassing sign on their mailboxes and block another point of unwanted media entry into their lives.

Sources: Carol Krol, "Swelling Ranks of 'Do Not Mail' Lists Prompts DMA Response," *BtoB,* February 11, 2008, pp. 26–27; Steven Swanson, "Up to Here in Catalogs? There Is a Solution—Online," *Tribune Business News,* November 4, 2007; Ira Tenowitz and Ken Wheaton, "Do Not Market," *Advertising Age,* March 12, 2007, p. 1, 44; Jenny Rough, "Saving Trees and Your Sanity by Managing Junk Mail," *The Examiner, February* 14, 2010, p. 31.



aimed at children under age 13 to obtain parental permission to collect most types of personal information and to monitor chat rooms and bulletin boards to make sure children do not disclose personal information there. When the law was enacted in 2000, it was left to the FTC to determine how to obtain the required permission, and the FTC temporarily allowed websites to let parents simply return an e-mail to approve certain information. Since then no other solution to the permission issue has surfaced, and the FTC is proposing to make the solution permanent.[124] However, the issue continues to be an area of concern as many marketers close their websites to children under the age of 13, but children under this age will often lie about their ages to gain access to the sites. The prevalence of social media is adding to the problem as many young people want access to fan clubs, blogs, and other websites that allow online interaction.[125]

Concerns over consumer privacy have become a major issue among the government and various regulatory agencies such as the FTC.[126] The federal government

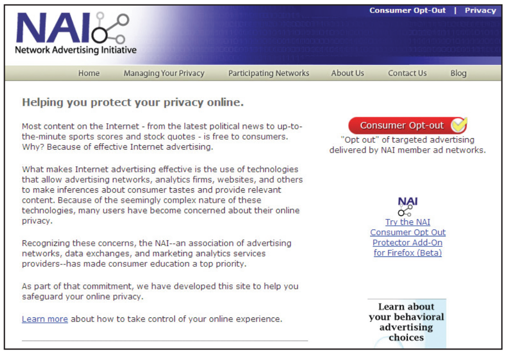



**EXHIBIT 22–21**

The Network Advertising Initiative website provides consumers with information about online advertising practices

is currently considering a number of privacy-related laws, many of which would have an impact on marketing and advertising over the Internet. In late 2007 the FTC requested that marketers voluntarily step up the disclosures they make about data they collect and seek permission from consumers before tracking their Internet surfing behavior.[127] Some privacy advocates have also proposed the creation of a Do Not Track list that would be an Internet version of the National Do Not Call Registry. Under the proposal, advertisers and others who use cookie-based tracking technology would be required to submit lists of their servers to a central regulatory body. Users who do not want to be tracked would download a browser plug-in that would identify those server logs and disallow cookies from them.[128]

Some states, such as California, have passed their own online privacy protection acts to protect the privacy of consumers. Consumer groups continue to urge the Federal Trade Commission to step up its actions on privacy protection, including the implementation of a do-not-track registry.[129]

Concerns over privacy have increased with the explosion in the popularity of social media sites such as Facebook, MySpace, Twitter, and others. In June 2010 the FTC settled a complaint against Twitter charging it deceived consumers and put their privacy at risk by failing to safeguard their personal information, marking the agency's first such case against a social networking service. The FTC ordered Twitter to establish a security program subject to government monitoring for the next 10 years. Twitter agreed to the terms in exchange for the FTC not pursuing a civil lawsuit against the company.[130] In May 2010, Facebook announced significant changes to its privacy policies giving users more control over their content, reducing the amount of their information that is available to others, and also making it easier to control whether applications and websites can access their information.[131]

The FTC has also taken action to address the issue of endorsements made through social media sites and blogs and ensure that the same rules apply in this context as they do in traditional advertising and infomercials. In 2009 the agency passed a new set of guidelines for online endorsements that require online endorsers and bloggers to disclose any "material connection" to an advertiser. Under the new guidelines, paid endorsers who post on social media sites such as Facebook or post product reviews on marketer sites such as Amazon can be held liable if they do not identify themselves as such.[132]

Another Internet-related area receiving regulatory attention is **spamming**, which is the sending of unsolicited multiple commercial electronic messages. Spamming has become a major problem; studies show that the typical Internet user spends the equivalent of 10 working days a year dealing with incoming spam.[133] Spam also costs businesses billions of dollars every year in terms of lost worker productivity and network maintenance. Moreover, most of these messages are fraudulent or deceptive in one or more respects.

A number of states have enacted antispamming legislation, and a comprehensive federal antispam bill, the Controlling the Assault of Non-Solicited Pornography and Marketing Act of 2003 (CAN-SPAM Act), went into effect on January 1, 2004. The act's general requirements for commercial e-mails include the following requirements:

- A prohibition against false or misleading transmission information.
- Conspicuous notice of the right to opt-out and a functioning Internet-based mechanism that a recipient may use to request to not receive future commercial e-mail messages from the sender.
- Clear and conspicuous identification that the message is an advertisement.
- A valid physical postal address for the sender.

Violations of the CAN-SPAM law include both civil and criminal penalties including a fine of $250 (calculated on a per e-mail basis) up to a maximum of $2 million.

While the CAN-SPAM Act carries severe penalties for violators, thus far it has done little to stop unsolicited e-mail messages. Spammers have been able to stay one step ahead of law enforcement officials by operating offshore and by constantly moving the Internet hosting source.[134]

## Summary

Regulation and control of advertising stem from internal regulation or self-regulation as well as from external control by federal, state, and local regulatory agencies. For many years the advertising industry has promoted the use of voluntary self-regulation to regulate advertising and limit government interference with and control over advertising. Self-regulation of advertising emanates from all segments of the advertising industry, including advertisers and their agencies, business and advertising associations, and the media.

The NAD/NARB, the primary self-regulatory mechanism for national advertising, has been very effective in achieving its goal of voluntary regulation of advertising. Various media also have their own advertising guidelines. The major television networks maintain the most stringent review process and restrictions.

Traditionally, the federal government has been the most important source of external regulation, with the Federal Trade Commission serving as the major watchdog of advertising in the United States. The FTC protects both consumers and businesses from unfair and deceptive practices and anticompetitive behavior. The FTC became very active in the regulation of advertising during the 1970s when it began several new programs and policies, including affirmative disclosure, advertising substantiation, and corrective advertising. Since 1980, the FTC has not been allowed to implement industrywide rules that would define unfair advertising practices. However, the advertising industry and Congress are nearing agreement on a definition of unfairness, and this power may be restored to the FTC.

In 1983, the FTC developed a new working definition of deceptive advertising. Recently the FTC has become more active in policing false and deceptive advertising. Under the Lanham Act, many companies are taking the initiative by suing competitors that make false claims. Many states, as well as the National Association of Attorneys General, are also active in exercising their jurisdiction over false and misleading advertising.

A number of laws also govern the use of other promotional mix elements, such as sales promotion and direct marketing. The Federal Trade Commission regulates many areas of sales promotion as well as direct marketing. Various consumer-oriented sales promotion tools such as contests, games, sweepstakes, and premiums are subject to regulation. Recently many states have become very active in the regulation of contests and sweepstakes. Trade promotion practices, such as the use of promotional allowances and vertical cooperative advertising, are regulated by the Federal Trade Commission under the Robinson-Patman Act. The FTC also enforces laws in a variety of areas that relate to direct marketing and mail-order selling as well as the Internet, while the FCC has rules governing telemarketing companies.

The rapid growth of the Internet as a marketing tool has created a new area of concern for regulators. The same consumer protection laws that apply to commercial activities in other media apply online as well. Major areas of concern with regard to advertising and marketing on the Internet are privacy, online marketing to children, and spamming or the sending of unsolicited commercial e-mail messages. Concerns over online marketing to children have led to the passage of the Children's Online Privacy Protection Act, which the FTC began enforcing in early 2000. The federal government passed the CAN-SPAM Act, which went into effect on January 1, 2004. This legislation sets stringent requirements for commercial e-mail messages. The Federal Trade Commission has become increasingly concerned over privacy issues related to the increasing popularity of social media and is requiring various sites to protect the privacy of users. The FTC also has issued new guidelines covering online endorsements that require endorsers and bloggers to disclose any material connection to an advertiser.

## Key Terms

**self-regulation** p. 6
**Better Business Bureau (BBB)** p. 8
**Council of Better Business Bureaus** p. 10
**National Advertising Review Board (NARB)** p. 10
**National Advertising Review Council (NARC)** p. 10
**Federal Trade Commission (FTC)** p. 16
**commercial speech** p. 16
**Central Hudson Test** p. 17
**Federal Trade Commission Act** p. 17
**Wheeler-Lea Amendment** p. 18
**trade regulation rules (TRRs)** p. 19
**unfairness** p. 19
**puffery** p. 20
**deception** p. 21
**affirmative disclosure** p. 22
**advertising substantiation** p. 24
**consent order** p. 26
**cease-and-desist order** p. 27
**corrective advertising** p. 27
**Lanham Act** p. 34
**National Association of Attorneys General (NAAG)** p. 38
**Children's Online Privacy Protection Act (COPPA)** p. 44
**spamming** p. 46

## Discussion Questions

1. The chapter opener discusses how the Federal Communications Commission is considering more stringent regulation of product placements in television shows. Evaluate the arguments for and against this policy by the FCC. (LO3)
2. Discuss the need for regulation of advertising and other IMC tools. Do you advocate more or less regulation of advertising and other forms of promotion by governmental agencies such as the Federal Trade Commission and the Food and Drug Administration? (LO1, LO3)
3. Discuss the role the National Advertising Review Council plays in the self-regulation of advertising. Do you view self-regulation as an effective way of protecting consumers from misleading or deceptive advertising? (LO2)
4. IMC Perspective 22–1 discusses the debate over hard liquor companies advertising on television. Do you agree with the DISCUS argument that hard liquor companies are at a competitive disadvantage against beer and wine marketers if they cannot advertise on television? Evaluate the decisions by NASCAR to drop its long-standing bans on sponsorships by hard liquor companies as well as decisions by professional sports leagues such as the NBA to allow spirits advertising within camera view. (LO2)
5. What are the three essential elements required to prove deception under the definition used by the Federal Trade Commission? (LO3)
6. Find several examples of advertising claims or slogans that are based on puffery rather than substantiated claims. Discuss whether you feel these advertising claims can be defended on the basis of puffery. (LO3)
7. Ethical Perspective 22–1 discusses the issue of direct-to-consumer advertising of prescription drugs. Evaluate the new authority the Food and Drug Administration has been given to regulate DTC drug advertising. Do you think the FDA needs more authority to regulate advertising in this area? (LO3)
8. Discuss the Lanham Act and how it affects advertising. What elements are necessary to win a false or deceptive advertising claim under the Lanham Act? (LO3)
9. Discuss how the Do Not Call Registry developed by the Federal Trade Commission is impacting the direct marketing industry. What arguments might direct marketers make in their efforts to have this program rescinded? (LO4)
10. IMC Perspective 22–3 discusses how a number of states are considering legislation that would create Do Not Mail list registries, which would allow consumers to keep unsolicited direct mail out of their mailboxes. Discuss the arguments for and against legislation that would prohibit marketers from sending direct mail to consumers. (LO4)
11. Do you agree with the new guidelines from the Federal Trade Commission requiring bloggers and endorsers to disclose any material connection to an advertiser? How might this impact companies that use social media in their IMC programs? (LO4)

# GLOSSARY CHAPTER 22

**affirmative disclosure** A Federal Trade Commission program whereby advertisers may be required to include certain types of information in their advertisements so consumers will be aware of all the consequences, conditions, and limitations associated with the use of the product or service.

**Better Business Bureau (BBB)** An organization established and funded by businesses that operate primarily at the local level to monitor activities of companies and promote fair advertising and selling practices.

**cease-and-desist order** An action by the Federal Trade Commission that orders a company to stop engaging in a practice that is considered deceptive or misleading until a hearing is held.

**Central Hudson Test** A four-part test used by the courts for determining restrictions on commercial speech.

**Children's Online Privacy Protection Act of 1998** Federal legislation which places restrictions on information collected from children via the Internet and requires that websites directed at children have a privacy policy posted on their home page and areas of the site where information is collected.

**commercial speech** Speech that promotes a commercial transaction.

**consent order** A settlement between a company and the Federal Trade Commission whereby an advertiser agrees to stop the advertising or practice in question. A consent order is for settlement purposes only and does not constitute an admission of guilt.

**corrective advertising** An action by the Federal Trade Commission whereby an advertiser can be required to run advertising messages designed to remedy the deception or misleading impression created by its previous advertising.

**Council of Better Business Bureaus** The parent office of local offices of the Better Business Bureau. The council assists in the development of codes and standards for ethical and responsible business and advertising practices.

**deception** According to the Federal Trade Commission, a misrepresentation, omission, or practice that is likely to mislead the consumer acting reasonably in the circumstances to the consumer's detriment.

**Federal Trade Commission (FTC)** The federal agency that has the primary responsibility for protecting consumers and businesses from anticompetitive behavior and unfair and deceptive practices. The FTC regulates advertising and promotion at the federal level.

**Federal Trade Commission Act** Federal legislation passed in 1914 that created the Federal Trade Commission and gave it the responsibility to monitor deceptive or misleading advertising and unfair business practices.

**Lanham Act** A federal law that permits a company to register a trademark for its exclusive use. The Lanham Act was amended to encompass false advertising and prohibits any false description or representation including words or other symbols tending falsely to describe or represent the same.

**National Advertising Review Board (NARB)** A part of the National Advertising Division of the Council of Better Business Bureaus. The NARB is the advertising industry's primary self-regulatory body.

**National Advertising Review Council (NARC)** An organization founded by the Council of Better Business Bureaus and various advertising industry groups to promote high standards of truth, accuracy, morality, and social responsibility in national advertising.

**National Association of Attorneys General** An organization consisting of state attorneys general that is involved in the regulation of advertising and other business practices.

**puffery** Advertising or other sales presentations that praise the item to be sold using subjective opinions, superlatives, or exaggerations, vaguely and generally, stating no specific facts.

**self-regulation** The practice by the advertising industry of regulating and controlling advertising to avoid interference by outside agencies such as the government.

**spam** Unsolicited commercial e-mail.

**spamming** The sending of unsolicited multiple commercial electronic messages.

**trade regulation rules (TRRs)** Industrywide rules that define unfair practices before they occur. Used by the Federal Trade Commission to regulate advertising and promotion.

**unfairness** A concept used by the Federal Trade Commission to determine unfair or deceptive advertising practices. Unfairness occurs when a trade practice causes substantial physical or economic injury to consumers, could not be avoided by consumers, and must not be outweighed by countervailing benefits to consumers or competition.

**Wheeler-Lea Amendment** An act of Congress passed in 1938 that amended section 5 of the FTC Act to read that unfair methods of competition in commerce and unfair or deceptive acts or practices in commerce are declared unlawful.

# ENDNOTES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