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PERSPECTIVE

Retail outlets: a steal or not for real?

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Outlet stores have a long history in the United States. Historically, manufacturers of clothing and other goods established outlet branches to sell irregular, damaged or excess product at discount prices. But the nature of merchandise offered at outlets has changed over the years. As shoppers have become increasingly price-sensitive, traditional retail stores have struggled to retain their customer base and sales have been sluggish. Dovetailing with this trend, consumers have become more interested in "affordable luxury" products bearing highly sought-after brand names, but offered at a fraction of traditional retail prices. Manufacturers have responded to these trends by adjusting their production and pricing models, and sales at outlet and discount stores have skyrocketed.

The shifting nature of the merchandise carried by outlet stores has led public officials to scrutinize their sales practices. In January, Sens. Sheldon Whitehouse, Richard Blumenthal and Ed Markey and Rep. Anna Eshoo sent a letter to the Federal Trade Commission in which identified an alleged increase in merchandise of purportedly inferior quality and specially manufactured for sale in outlets, which they believe was never offered for sale in traditional retail stores. They expressed concerns about potential deceptive marketing practices for the products, and called for the FTC to investigate. Perhaps in response to this letter, the FTC issued a consumer information release in which it and encouraged outlet shoppers to "make sure you're satisfied with the price you're paying for what you're getting." To date, the FTC has not taken any enforcement action.

Plaintiffs' class action attorneys picked up where the public officials left off, filing a series of lawsuits against manufacturers and retailers. At least six putative class actions have recently been filed, all of which allege that manufacturers and retailers violated consumer protection laws by either falsely representing outlet merchandise as being originally sold in traditional stores at higher prices or being of the same quality as merchandise offered for sale in traditional retail outlets.

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In each lawsuit, the plaintiffs claim that they had been misled by representations made by the defendants, and had they not been misled, they would not have paid the stated price for the products purchased, or would not have purchased them at all. All of the pending lawsuits bring claims under the trio of California consumer protection laws most often utilized by plaintiffs' lawyers: the Consumer Legal Remedies Act, Unfair Competition Law and False Advertising Law. California is particularly attractive to class action plaintiffs' attorneys, as it is both the most populous state in the country and one of the most plaintiff-friendly states for false advertising and consumer protection claims.

Regardless of California's generous consumer protection laws, plaintiffs will have several hurdles to clear in their quest to prove liability for these allegedly deceptive sales practices. At the outset, most of these cases are likely to be fought in federal courts, due at least in part to the availability of removal procedures under the Class Action Fairness Act of 2005. In federal courts, plaintiffs must establish Article III standing and meet strict federal pleading standards for claims "sounding in fraud," as is the case in each of the pending lawsuits. Further, plaintiffs must plead and prove affirmative misrepresentations, rather than omissions, unless they can establish that a material fact was not disclosed.

Assuming that plaintiffs' claims survive a motion to dismiss, their cases will rise and fall on the facts, such as the specifics of the labels on the merchandise, marketing and advertisements, and other consumer-facing communications. Manufacturers and retailers have different practices with respect to their pricing models and labeling. Some make no use of comparative pricing at all, and others use comparative models that are not based on discounting each item's former selling price. Merchandise offered under a comparison price model need not have been manufactured and offered for sale at the stated higher prices in traditional retail stores, as there are other legitimate manners of establishing comparison pricing. In any event, plaintiffs' ability to certify a class in these cases will largely depend on consumer behavior-focused fact and expert discovery — the intersection of the consumer-facing communications with what shoppers understood they were getting when they visited outlet stores and purchased the merchandise at issue.

Plaintiffs may have an uphill battle proving damages on a class-wide basis; shoppers are heterogeneous and have different purchase motivations and expectations regarding what they are getting and the value that they receive for their dollars when outlet shopping. Shoppers also have ample opportunity to, for example, examine the stitching and feel the fabric used when determining whether they believe the product is a good value for the price.

These six lawsuits represent the beginning of a trend. All manufacturers and retailers that offer merchandise for sale at outlet stores, or regularly discount merchandise from their standard retail prices, should take notice and be prepared to document, and if necessary, defend their sales practices.

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