

FTC Commissioners set to hear oral arguments tomorrow in data security case involving LabMD Inc.

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By Alexei Alexis

March 4 — Federal Trade Commissioners will hear oral arguments on March 8 in a high-stakes data security case that was dismissed by an administrative law judge and then appealed by enforcement staff at the agency (In re LabMD, Inc., F.T.C., No. 9357)..

At issue is how far the FTC must go in order to prevail in a claim alleging an “unfair” practice that was harmful to consumers. Commissioners will consider whether the FTC must show that a company's lax data security made identity theft not only possible, but probable.

While the case has to do with data security, it has the potential to impact the FTC's enforcement of a broad range of issues across §5 of the FTC Act, which prohibits unfairness.

“I think the stakes are high enough for both parties at this point that whoever doesn't prevail before the commission—and I'm assuming that it's going to be LabMD—will turn to a court of appeals,” Peter Miller, a senior counsel at Crowell & Moring LLP, told Bloomberg BNA.

Chief ALJ D. Michael Chappell ruled in November that the FTC failed to show that the allegedly weak data-security practices of LabMD Inc., a medical testing laboratory, caused injury to consumers (See previous story, 11/17/15).

It's an important test case, given that the FTC has typically settled data security matters and has rarely litigated them in public, according to Miller, a former chief privacy officer for the agency.

In a related case, the U.S. Court of Appeals for the Third Circuit held in 2015 that the commission had authority under §5 to bring a data security action against hotelier Wyndham Worldwide Corp. (See previous story, 08/25/15). Wyndham settled a few months later (See previous story, 12/10/15).

Brill Recusal

Three of four FTC commissioners—Chairwoman Edith Ramirez and Terrell McSweeney, both Democrats, and Maureen Ohlhausen, a Republican—are expected to hear oral arguments in the LabMD case. Commissioner Julie Brill, a Democrat, has recused herself at LabMD's request. One Republican commissioner's seat is currently vacant.

A “probable” risk of identity theft standard would force the FTC to meet a much higher burden, according to Janis Kestenbaum, a partner at Perkins Coie LLP.

“It’s historically rare for the commission to side with a respondent over the FTC staff in administrative appeals, and so this case may be eventually headed for a federal court of appeals,” Kestenbaum, a former senior legal adviser to Ramirez, told Bloomberg BNA.

Enforcement staff argued that LabMD violated §5 by failing to prevent unauthorized access to patient information in two separate incidents, exposing consumers to identity theft and other potential harms. However, Chappell said there was no evidence that the company’s alleged “unreasonable” data security caused, or is likely to cause, substantial consumer injury.

“The LabMD decision is an important challenge to the FTC’s data security enforcement program—especially because it comes from the commission’s own chief administrative law judge,” Charles Kennedy, principal of The Kennedy Privacy Law Firm, told Bloomberg BNA.

Chappell held that complaint counsel had, at best, proven the “possibility” of harm, but not any “probability” or likelihood of harm. “Fundamental fairness dictates that demonstrating actual or likely substantial consumer injury under Section 5(n) requires proof of more than the hypothetical or theoretical harm that has been submitted by the government in this case,” he said.

FTC Appeal Brief

In an appeal brief, complaint counsel said the ALJ had failed to analyze LabMD’s “multiple, systemic, and serious” security failures before issuing his ruling.

“The decision is wrong as a matter of law and fact,” the brief said.

Laura VanDruff, an attorney in the FTC’s Bureau of Consumer Protection, is expected to present the FTC’s case before the commissioners.

LabMD is being represented by the Cause of Action Institute, a Washington non-profit organization that advocates for limited government regulation.

An amicus brief in support of LabMD has been filed by TechFreedom, a technology think tank with libertarian leanings.

Brill’s recusal had to do with speeches she delivered in 2013 that included references to LabMD. Based on those speeches, the company contended that Brill had prejudged facts

in the case. She disagreed with that argument, but ultimately decided that her participation “would likely create an undue distraction.”