Sonnenschein
SONNENSCHEIN NATH & ROSENTHAL LLP

1301 K Street N.W.
Suite 600, East Tower
Washington, D.C. 20005-3364
202.408.6400
202.408.6399 fax
www.sonnenschein.com

Chicago
Kansas City
Los Angeles
New York
Phoenix
San Francisco
Short Hills, N.J.
St. Louis
Washington, D.C.
West Palm Beach

Christopher Smith
202.408.9231
kitsmith@sonnenschein.com

Elaine D. Kolish
202.408.3243
ekolish@sonnenschein.com

November 15, 2006

The Honorable Donald S. Clark
Secretary
Federal Trade Commission
600 Pennsylvania Ave., N.W.
Washington, DC 20580

Re: Request For a Staff Advisory Opinion

Dear Mr. Clark:

On behalf of Sony Electronics Inc. (Sony) we are requesting a staff advisory opinion, pursuant to 16 C.F.R. § 1.1, on the question of whether Sony may lawfully market and sell as new certain returned consumer electronics products that have never been used and that are indistinguishable from products straight from the factory. Specifically, Sony seeks guidance on the acceptability of selling consumer electronics products as new products under a narrowly defined program in which Sony or its authorized vendor would:

(i) identify, from among the products returned by retailers to Sony or its authorized vendor, those that have never been turned on;

(ii) visually inspect those products that have not been turned on and reject any damaged products;

(iii) ensure that returned products that satisfy the first two conditions have all of their requisite parts, components, and manuals;

(iv) repackage the returned products that meet the above conditions;

(v) provide the same warranty for these returned products as for new products that have never been sold; and

(vi) return them to a retailer for sale as new products.[1]

This request is based on our understanding of prior Commission policy and precedent that require a seller to disclose when it is selling goods that have been previously used, but do not require returned goods that have merely been "inspected" by consumers to be described as used when resold. Sony's request does not require the FTC staff to define the entire scope of actions that can reasonably constitute inspection. Instead, we only ask the staff to conclude (a) that a product that has never been turned on will not be considered used, and (b) that the other elements of Sony's proposed program will assure that a consumer buying such a product will encounter the same product purchase and usage experience as if he or she had bought a new consumer electronics product that had not been purchased previously.

We explain below the reasons for Sony's proposed course of action and provide additional details about how the program would be implemented. Additionally, we set forth an analysis of why we believe Sony's proposed conduct is legally permissible and why it is appropriate for the FTC staff to provide the requested guidance.

Sony's Proposal to Sell Certain Unused Returned Consumer Electronics as New

Like many other consumer electronics companies, Sony experiences a high volume of product returns from consumers, the wholesale value of which has grown dramatically in recent years. As a matter of policy, Sony generally treats all opened returned products as if they have been used by consumers. These returned products, which are often inspected and serviced, are designated by Sony as "Class B" products. These products are sold as refurbished products at a significantly discounted price, and they typically include a 90-day limited warranty rather than a longer new product warranty.

Because of the undifferentiating nature of its resale policy, many products designated as Class B by Sony have never even been turned on – having merely been inspected by purchasers before being returned to Sony. Such products have nothing wrong with them when returned by consumers and require no servicing before they are sold at a Class B discount.

[1] The consumer electronics products potentially covered by Sony's program include but are not limited to the following products: video products (*e.g.*, DVD players/recorders, digital cameras, camcorders, televisions, and combination TV/VCR or TV/DVD players); computers (desktop and notebook PCs and related equipment); video game systems; audio products (desktop, component and portable devices); cell phones; portable digital assistants; and vehicle electronics.

The financial cost to Sony of its Class B resale policy is substantial. Consequently, Sony would like to modify its policy to distinguish between returned products that have not been turned on and those that have been operated. Such a modification would provide Sony with greater flexibility in both inventory control and supply chain management while ensuring compliance with the Commission's policies.

Although even some use of a product reasonably could be considered mere "inspection," Sony proposes to take an extremely conservative approach to the question of whether a returned Sony product has been used by a consumer. Sony's proposed program is based on the simple, bright line standard of whether a product has been turned on – *i.e.*, if it has not been turned on, it has not been used. This approach avoids a potential slippery slope, because it does not require the FTC to evaluate or determine how much use is acceptable.

To implement this policy change in a consistent, verifiable manner, Sony would use existing, reliable product and packaging technologies to determine if a purchaser has turned on a returned product. For example, some of Sony's electronic products contain an internal chip or clock that allows Sony to determine if a product has been turned on and for how long. Sony also may use tamper-evident tape, seals or labels, which can be affixed to AC plugs, connectors or battery compartments, to provide a clear indicator of consumer use of a product. Sony would determine on a product-by-product basis which technology it would use to determine if a consumer has turned on a product. If the consumer has turned on the product at all – even if only to conduct a cursory inspection of the product's operation – Sony would disqualify the product from future sale as a new product. Sony's plan thus avoids subjective evaluations about whether or to what extent a returned product has been used by a consumer. Stated in its simplest terms, if electrical power has been applied to any of the product's circuitry, then it cannot be sold as "new."

The other elements of Sony's program ensure that the consumer purchasing experience would be the same as it would be with other new products. Sony would visually examine unused products to ensure that they are complete and undamaged, and if so, place them in new packaging.[2] Sony also would provide the same warranty for these repackaged products as for

[2] This program will not involve refurbishment of products to a "good as new" condition. If there is visible damage, such as scratches, dents or cracks, the product would not be eligible for the program. Of course, minor cosmetic blemishes, such as fingerprints that a consumer might leave on a product when handling it, would be removed and would not render the product ineligible for the program. Otherwise damaged products would be designated for Sony's refurbished sales program. Moreover, if the product is otherwise acceptable but a minor part or piece of product information (*e.g.*, a headphone, manual, or warranty card) is missing because the consumer omitted the item from the package when returning the product, then the missing item would be replaced.

other new similar products. Because Sony (or its authorized agent), and not retailers, would run the program, Sony can ensure that the policy is properly and uniformly applied across all returns.

Sony and Industry Experience With Returns Show the Significance of Sony's Request

Currently, as would be the case under the new program, retailers send all returned products to return centers operated by Sony or its authorized agent. These return centers perform the necessary inspections and refurbishment to prepare a returned item for resale as Class B products. Sony's experience through these return centers indicates that only a very small percentage of returns are actually defective products and that a very significant percentage fall into the "no problems found" (NPF) category. Because many of the NPF products are items that have never been turned on, Sony incurs significant losses from their sale as Class B products.

Similar industry-wide patterns of returns also have been reported. For example, a consumer survey conducted by the Consumer Electronics Association (CEA) in 2005 indicated that many consumers return products for reasons other than a defect, including (a) to obtain a different brand or model, (b) because they no longer wanted it, (c) because they already owned it, or (d) because they spent too much money on it.[3] The CEA survey also indicated that nearly 50 percent of all returns occur within a week after purchase. Overall, these statistics suggest that many purchasers of consumer electronics products may merely open the box and inspect the product without using it before returning it to the retailer or to the manufacturer.

Sony's Proposed Course of Action Is Lawful

Sony believes that its proposed course of action, as described in this letter, is lawful and would not be deceptive under the FTC Act or under the standards the Commission has expressed in its 1984 Policy Statement on Deception and in its 1969 Enforcement Policy on "Merchandise Which Has Been Subjected To Previous Use On Trial Basis and Subsequently Resold as New." The 1969 policy statement is particularly relevant. Although the 1969 Enforcement Policy predates the Commission's Policy Statement on Deception, it has not been repudiated by the Commission. Moreover, we believe that application of the Deception Statement's analytical tools leads to the same conclusion the Commission reached in its 1969 Enforcement Policy.

The 1969 statement, while reaffirming the Commission's long-held view that consumers have a preference for new or unused goods, also draws an important distinction between

[3] "Return Rates and Issues for CE Products Update," Consumer Electronics Association (CEA) Market Research Report (Nov. 2005).

"inspection" and "use."[4] Specifically, the Commission concluded that trial use by a consumer and subsequent refurbishment of returned products to a good-as-new condition requires disclosure, but that its "policy applies only to merchandise that has been used, and not to merchandise that has merely been inspected but not used."[5]

Under the Deception Policy Statement there must be a representation, omission or practice that is likely to mislead a consumer, acting reasonably under the circumstances, to his or her detriment.[6] In other words, the representation, omission or practice must be a material one. Under its proposed program, Sony would treat the products as new, in terms of their pricing, packaging and warranty. The resulting implied representation that the repackaged products are new would not be misleading to consumers because the products would in fact be new, having never been used by their previous purchasers.[7]

Although Sony recognizes that the FTC appreciates empirical data on consumer expectations when it is available, we are unaware of any such empirical data in this case. Nevertheless, the absence of such data is not a bar to an advisory opinion. It is well established in Commission case law that the Commission may use its accumulated expertise to determine what facts are material to consumers and when it is deceptive to omit those facts from marketing materials.[8] In the past, the Commission has generally alleged a deceptive failure to disclose information only when the omitted information involved health or safety or the key financial terms and conditions of a transaction.

We also suggest that the FTC can find additional support for Sony's proposed course of action in various state laws that expressly or impliedly permit "unused" goods to be sold as new. Many of these states have based their laws on the Uniform Deceptive Trade Practices Act and the Uniform Consumer Sales Act, which prohibit the resale, as new, of returned products only if the products have been used, altered, reconditioned or reclaimed. Under those statutes, mere

---

[4] 34. Fed. Reg. 176, 177.

[5] *Id.* at 177.

[6] *Appended to Cliffdale Associates, Inc.*, 103 F.T.C. 110, 174 (1984).

[7] Just as we believe that Sony has no legal obligation to disclose that goods are "used" because they have never been turned on and thus fall squarely into the "inspected" category, we also believe that disclosure of the mere fact of prior purchase is not a material omission that might trigger a disclosure requirement. The Commission's Policy Statement expressly recognizes that "not all omissions are deceptive, even if providing the information would benefit consumers...." *Id.* at 183, n.4. Such a disclosure requirement also would be inconsistent with state laws, as discussed below.

[8] *See, e.g., Pfizer*, 81 F.T.C. 23, 58 (1972).

inspection that does not entail use or alteration of the product would not change the status of the product from "new" to "used."[9] Notably, the Ohio Administrative Code states affirmatively that "returned goods, which have not been used by a previous purchaser, shall be considered new or unused."[10]

Furthermore, in 1998 the Office of the Attorney General of the State of California came to the same conclusion reached by the FTC in 1969 when it analyzed the question: "must merchandise be advertised as 'secondhand or used' if it is used, worn, or sampled for a short time by a consumer and then returned in like-new condition pursuant to the retailer's policy allowing returns of merchandise at the customer's discretion." Attorney General Daniel E. Lungren concluded that it must be so advertised," *unless such use is for inspection purposes only.*"[11]

In analyzing the question, Attorney General Lungren was guided in part by the Oregon Supreme Court's decision in *Weigel v. Ron Tonkin Chevrolet Co.*[12] In that case the court held that because there was a transfer of legal possession of the auto and the purchaser had discretionary use of the vehicle for his or her own purposes for five days, the auto must be represented as used or secondhand. The court's decision was based not on the fact of the sale, but on the purchaser's use of the product. In that case, the court also commented on the common practice of using goods for inspection purposes only, stating that "merchandise other than automobiles sometimes is sold, examined, or tried out at home, and returned to the seller. Whether such merchandise is 'new' or 'used' does not depend on the fact of an earlier sale; it depends on whether the article was used."[13] The Attorney General believed that *Weigel* correctly interpreted the terms "secondhand or used" for its purposes. Thus, under the Attorney General's opinion, disclosure of the prior purchase of a product depends upon whether the product has been used, unless such use is for inspection purposes only.

---

[9] *See* Michael P. Sullivan, "What Goods or Property are 'Used,' 'Secondhand,' or the Like, for Purposes of State Consumer Laws Prohibiting Claims that Such Items are New," 59 A.L.R. 4th 1192, § 2.

[10] Section 109:4-3-08. Other states such as Mississippi and Idaho have taken similar positions ("goods are not considered used if a prior consumer was given a full refund or exchange for the goods, in the normal course of business, and if the goods are not known to presently or formerly have defects"). *See, e.g.*, Mississippi, 24 000 002 R.51 (2006), and Idaho, IDAPA 04.02.02.113 (Returned Goods) (2005). *See also* Louisiana, LAC 16:III.511(2003).

[11] Opinion of Daniel E. Lungren, Attorney General, Clayton P. Roche, Deputy Attorney General, No. 97-1009 (May 22, 1998) (emphasis added).

[12] 690 P.2d 488 (1984).

[13] *Id.* at 490, n.2.

Sony believes that, under its proposed program, consumer electronics products that have not been turned on will not have been subjected to any use. The act of merely opening the packaging and examining a product without turning it on should be considered "inspection" and should not trigger any affirmative disclosure duties nor any prohibition on representing the goods as new.

At its most basic level, Sony's proposed program embodies the principles contained in the Commission's 1969 policy statement and in the principles expressed in state laws and in the California Attorney General's opinion regarding a company's disclosure duty. We believe that the principles of the 1969 policy statement remain valid and are consistent with those in the more recent Deception Policy Statement. Accordingly, Sony submits that it would be appropriate for the FTC to conclude that Sony consumer electronics products returned by consumers without ever being turned on can be considered "merely inspected" and not "used" and thus be eligible for sale as new products.

Sony's Request Satisfies the Commission's Criteria for a Staff Advisory Opinion

Sony believes that the issues raised by this request satisfy the criteria in the Commission's Rules of Practice for issuance of a staff advisory opinion. The question posed by Sony is not a purely hypothetical or theoretical one, because Sony is prepared to act upon a favorable opinion issued by the staff. Sony is seeking this advisory opinion because, as noted above, the FTC has not issued guidance in this area in nearly 40 years, and there is no clear FTC or other guidance on the particular question posed by Sony. Furthermore, because of uncertainty about this issue, Sony and possibly other manufacturers are unnecessarily designating unused, "merely inspected" products as Class B products. This situation creates substantial economic injury to manufacturers such as Sony, as well as to consumers, who may pay higher overall retail prices or may experience the effects of reduced marketplace competition resulting from lower manufacturer profitability. Thus, resolution of Sony's question is likely to be of significant public interest.

Conclusion

The conservative approach Sony is proposing will assure that returned products that qualify under this program will be indistinguishable from new products delivered from the factory. The fact that a qualifying product was previously purchased will not affect its performance because the product will never have been turned on and thus never have been used. Moreover, Sony's plan to examine qualifying returned products visually for damage and completeness prior to repackaging and to provide a new product warranty will ensure that the returned products are indistinguishable from products that have never been sold. This

comprehensive plan will eliminate any potential harm to subsequent purchasers resulting from the qualifying products' previous purchase. Accordingly, Sony believes that its proposed program to sell, as new, returned products that have not been turned on and that meet the program's other criteria will satisfy the Commission's consumer protection objectives and requirements.

We appreciate your consideration of this request. Please let us know if you would like us to provide additional information to assist the staff's review. We would also be pleased to meet with the staff to discuss any questions they might have.

Yours very truly,

Christopher Smith

Christopher Smith
Elaine D. Kolish

cc: Lydia B. Parnes, Director, Bureau of Consumer Protection
James A. Kohm, Associate Director, Division of Enforcement
Sandy Prabhu, Esq., Division of Enforcement