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Can State Price Gouging Laws Be Practically Applied to Long-Run Events?

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Introduction

Price gouging laws prohibit firms from unilaterally raising price excessively when demand exceeds supply, usually due to an emergency.

While there is no federal U.S. price gouging law, numerous states have price gouging laws that vary widely in scope, threshold for a price increase, and potential defenses.[1] Such variation raises many questions regarding which aspects of current state price gouging laws could be improved, such as whether uniform standards should apply across states, which products should be subject to price gouging laws, and the difference between the magnitude of a price increase that is legal and the magnitude of a price increase that is classified as price gouging. This article seeks to address the specific question of whether current state price gouging laws are suitable for addressing price gouging claims in the context of long-run events such as the COVID-19 pandemic.

Prior to the pandemic, price gouging was a phenomenon that was primarily associated with events of limited duration, such as natural disasters.[2] In contrast, price gouging emergency regulations related to COVID-19 lasted for a year or longer in many states.[3] To obtain a sense of the magnitude of consumer complaints related to COVID-19, Pennsylvania alone had received over 21,500 consumer complaints related to COVID-19 as of January 2021, many of which were specifically related to concerns over price gouging for items such as cleaning supplies, paper products, and medical equipment.[4]

There exists a fundamental question as to whether any type of price gouging law is appropriate for application to long-run events. High prices serve as signals of profitability for firms, and such signals incentivize entry as well as production increases from existing firms. But expansion and entry require time, and hence a primary justification for the existence of price gouging laws is to protect consumers from large price increases (however defined) due to events that are unanticipated and short lasting. Indeed, one might argue that the inability to anticipate an event is a necessary (but not sufficient) condition for making a cogent price gouging claim. For this reason, the extent to which it is appropriate to apply the term *price*

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[1] *See* Michelle K. Fischer and Tiffany D. Lipscomb-Jackson, "USA: Does a federal gouging law even make sense – and, if so, what should it look like?" *Concurrences*, 2020 (4).

[2] *See* Timothy Snail and Mary Beth Savio, "Price Gouging in a Time of Sea Change," *CPI Antitrust Chronicle*, September 2020, who note that "many price gouging laws were enacted with a specific type of emergency or natural disaster in mind, such as a hurricane or wildfire, which are relatively discrete events."

[3] *See, e.g.*, "States' COVID-19 Public Health Emergency Declarations and Mask Requirements," nashp.org/governors-prioritize-health-for-all/ (last visited Feb. 12, 2022).

[4] First Term Report, Office of Attorney General Josh Shapiro, Commonwealth of Pennsylvania (https://www.attorneygeneral.gov/wp-content/uploads/2021/01/first_term_report.pdf)

gouging to long-run events is not necessarily obvious.[5]

If, at the outset of an unanticipated event during which there is excess demand, potential entrants know that price gouging states of emergency will expire after a short period of time, they may be incentivized to make plans for entry in anticipation of the expiration of the price gouging statute. If, however, the effective period of the price gouging statute is long, then firms may lack the incentive to increase production and potential entrants may not enter. This may create a situation of enduring excess demand, which may be worse than no price gouging laws at all.

Whether one agrees or disagrees with the suitability of price gouging laws for long-run events, one may ask whether the current price gouging laws properly address specific temporal issues that may arise in the context of longer run events. Most price gouging laws are triggered by a state of emergency declaration and cite a pre-emergency period for purposes of comparing (1) allegedly excessive prices following the emergency declaration to (2) prices prior to the emergency.[6] Comparison of prices over longer time periods—the type of analysis called for in the context of the pandemic—requires close attention not only to the length of the relevant time periods but also to a variety of potential economic factors that may influence price over longer periods of time.

This article addresses several topics related to analyses of prices over time that may arise in relation to *any* price gouging claim but that are particularly relevant for allegations of price gouging in the context of long-run events such as the pandemic, including (1) the appropriate emergency period, (2) the appropriate non-emergency period for comparison, (3) seasonality, (4) whether a permanent change in demand has occurred, and (5) price response to cost changes.

Is the declared emergency period appropriate for analyzing price gouging?

States of emergency were declared at similar times at the beginning of the epidemic, often in March 2020, but end dates vary more widely, and in many cases, occurred well over a year after the beginning of the pandemic. For example, Arkansas's state of emergency expired on May 30, 2021.[7] The state of emergency in neighboring Missouri expired on August 31, 2021.[8] In Oregon, the governor announced in April 2021 that she was lifting the state's executive order on price gouging with the statement, "The days of hand sanitizer and, yes, toilet paper scarcity are far behind us."[9] In this instance, the administration declared that scarcity was resolved prior to the expiration of Oregon's price gouging statute.

The preceding (Oregon) example raises questions regarding whether an economic analysis of price gouging is well suited to track state-imposed emergency declaration dates. While there is perhaps less doubt associated with the beginning date of an emergency, an alleged episode of price gouging may have ceased prior to the emergency end date determined by the state. Therefore, an econometric test of price gouging that adopts a state-declared emergency end date may not necessarily lead to the correct conclusion regarding the existence or magnitude of an alleged price gouging episode.

Does the declared non-emergency period serve as an appropriate comparison period?

The appropriate non-emergency period for comparison presents another important question

[5] Note that the focus on price gouging in connection with events in this article is a separate discussion from one relating to price gouging of drugs, a topic that is not addressed here.

[6] For a more detailed exposition of state laws relating to triggers and the pre-emergency period for comparison, see Michelle K. Fischer and Tiffany D. Lipscomb-Jackson, "USA: Does a federal gouging law even make sense – and, if so, what should it look like?" *Concurrences*, 2020 (4).

[7] "Arkansas governor: Virus emergency declaration to end," *AP News*, May 20, 2021 (https://apnews.com/article/arkansas-coronavirus-pandemic-health-government-and-politics-53b5daad58951eece3563c4152678cbe)

[8] "Governor Parson signs executive order 21-07 extending state of emergency in Missouri, March 26, 2021" (https://governor.mo.gov/press-releases/archive/governor-parson-signs-executive-order-21-07-extending-state-emergency).

[9] https://kpic.com/news/local/oregon-governor-extends-state-of-emergency-for-covid-19-until-june-28

for analytical purposes. As noted earlier, most price gouging laws cite a pre-emergency period for purposes of comparing prices following the emergency declaration to prices prior to the emergency, but the periods vary significantly by state. For example, in North Carolina, the pre-period is defined as 60 days prior to the emergency.[10] In neighboring Virginia, the pre-period is defined as 10 days prior to the emergency.[11] Other states do not impose a specific limit on the duration of the pre-period.

There exist a variety of economic factors that would cause an economist to question whether it is appropriate for a statute to prescribe the precise length of the non-emergency period. One such factor that is more likely to be relevant when analyzing long-run events is seasonality.

Why is seasonality important?

Seasonality may play a role in determining the appropriate non-emergency period discussed above. That is, if seasonal demand differs in the time period prior to the alleged price gouging, then it may be appropriate to consider a non-emergency period for analysis during which seasonal demand is comparable to seasonal demand during the period of the alleged price gouging. Failing to control for seasonality risks misattributing a seasonal demand effect to price gouging. Examples of allowances for seasonality may be found in certain states, such as in the following examples:

- Kentucky: A price is not prohibited if it is "generally consistent with fluctuations in applicable commodity, regional, national, or international markets, or seasonal fluctuations."[12]
- South Carolina: A price increase that "reflects the usual and customary seasonal fluctuation in the price" is not prohibited.[13]
- Virginia: A price increase is not unconscionable if the increase in the amount charged was attributable solely to a regular seasonal or holiday adjustment.[14]

However, references to seasonality are absent from many state price gouging statutes. Such statutes would benefit from explicit reference to the potential for seasonality to influence price.

Would price be expected to increase if a demand increase is permanent?

In addition to the importance of accounting for seasonal demand in the context of long-run events, long-run events are also more likely to feature permanent increases in demand for goods and services defined as "necessary" according to state law. Such permanent increases in demand may occur for a variety of reasons, including changes in consumer preferences. For instance, consider the goods and services defined by Virginia state law as "necessary":

> "Necessary goods and services" means any necessary good or service for which consumer demand does, or is likely to, increase as a consequence of the disaster, and includes water, ice, consumer food items or supplies, property or services for emergency cleanup, emergency supplies, communication supplies and services, medical supplies and services, home heating fuel, building materials and services, tree removal supplies and services, freight, storage services, housing, lodging, transportation, and motor fuels.[15]

Demand for building materials has remained high since the beginning of the pandemic.[16] One might argue that demand for building materials has remained high due to a long-term shift in consumer preferences toward home renovation projects. A price increase given a permanent increase in demand would be an ordinary phenomenon to observe in the absence of price

[10] N.C. Gen. Stat. § 75-38.

[11] Va. Code § 59.1-526. Definitions.

[12] Ky. Rev. Stat., 367.374.

[13] S.C. Code Ann., § 39-5-145.

[14] Va. Code, § 59.1-527. Prohibitions.

[15] Va. Code, § 59.1-526. Definitions.

[16] *See, e.g.*, Lydia O'Neal, Builders Hunt for Alternatives to Materials in Short Supply, THE WALL ST. J. (Oct. 6. 2021).

gouging. State price gouging laws should recognize that a permanent increase in demand is one factor that may be accounted for when determining whether price gouging has taken place.

Can price gouging laws capture the complexities of price-cost relationships?

The relationship between price and cost may be complex in practice for a variety of reasons, particularly in the case of long-run emergency events. First, it is not uncommon for cost changes to precede price changes by days, weeks, or months depending on the product or industry in question. Second, when price response to a cost change does occur, the cumulative response to a particular cost change may occur over a period of time. Third, depending on the market in question, price would not necessarily be expected to change by the same amount as the cost change. An understanding of when and how prices would be expected to respond to cost changes in a particular industry can help to inform whether price gouging has taken place.

In some cases, state law includes language regarding cost effects, such as in the following examples:

- Alabama: A price is unconscionable if the increase in the price charged is not attributable to reasonable costs incurred in connection with the rental or sale of the commodity.[17]
- Colorado: A price will not be considered unreasonably excessive if the seller can prove that, due to the events giving rise to the disaster declaration, the price charged is directly attributable to additional costs imposed by the seller's supplier or suppliers or other direct costs of providing the good or service sold or offered for sale.[18]
- Florida: A price is unconscionable unless the price increase is attributable to additional costs incurred in connection with the rental or sale of the commodity.[19]

One would not expect state laws to address the many potential complexities associated with measuring price response to cost changes. However, every state law should contain language regarding cost effects, and economists have a role to play in making the courts aware of the potential complexities associated with measuring price response to cost changes, particularly in the context of long-run events.

Conclusion

It is debatable whether price gouging laws are appropriate for long-run events. At a minimum, to the extent that state price gouging laws are applied to such events, such laws would benefit from consideration of factors such as the appropriate duration of the event period and pre-event period, seasonality, permanence of demand, and the impact of costs on prices—factors that are likely to require particular attention in an analysis of pricing behavior over longer time periods.

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17 Ala. Code Title 8 – Commercial Law and Consumer Protection. Chapter 31 – Alabama Unconscionable Pricing Act. Section 8-31-4 – Determination of Unconscionable Price During a State of Emergency.

18 Colo. Rev. Stat § 6-1-730.

19 Fla. Stat. Title XXXIII. Regulation of Trade, Commerce, Investments, and Solicitations § 501.160. Rental or sale of essential commodities during a declared state of emergency; prohibition against unconscionable prices.


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