Podcast Transcript

Every Breath You Take: Emerging AI Pricing Laws and Guidelines

Date: November 17, 2026

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Run Time: 30:23

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Fluharty: Thank you for joining us for another episode of BakerHosts Ad Nauseam, a podcast series focusing on new and trending advertising issues with an

emphasis on the FTC and the NAD. I am Christina Fluharty, and you're listening to BakerHosts.

Today, Amy and Daniel are joined by Lauren Bass, an associate on the Advertising, Marketing and Digital Media team. Together, they discussed the evolving legal landscape of AI-driven personalized pricing, including emerging state and federal restrictions, disclosure requirements and implications for retailers and loyalty programs. With that, welcome to Ad Nauseam, and let's turn it over to Amy and Daniel.

Mudge: Welcome back, dear Ad Nauseam followers. Daniel and I took a little August break that maybe extended a little bit into early fall. Frankly, it was just too hot and muggy to do anything in D.C. other than fan ourselves and sip mint juleps. And we just couldn't really think about navel-gazing about consumer protection developments, but we hope you missed us. We know we missed you. And now that we're moving into crisp fall temperatures, we're raring to go, sharing our musings with our listeners.

And today, we welcome a guest you haven't met before, at least on Ad Nauseam. It's our associate colleague, Lauren Bass from our New York office. And Lauren has been tracking diligently the emerging laws on algorithmic pricing, which we know is a hot topic.

Kaufman: And yes, welcome back, Amy, and welcome, Lauren. It is great to see you. This is, I believe, your first time on the Ad Nauseam soundstage, and you are the perfect guest to have for this important topic since your practice has really been split between advertising and Web3. And algorithmic pricing really brings together Section 5 issues and AI issues.

Bass: Yes. And thank you guys for having me. I'm really happy to be here.

Kaufman: We are so glad to have you and I am holding Amy back because Miss Coupon Cutting Cheapskate loves a bargain. And so, I know she can't wait to delve into this spicy topic. But Lauren, you're one of our millennial colleagues. And while we know you got the smarts, we got to see if you're up to the time-wasting '80s pop culture topics that Amy and I love.

Mudge: Indeed, Daniel. All guests must be hazed. And in this one, will Lauren surprise and delight, or will she crater and disappoint with her knowledge of what I believe we can all agree is the greatest decade?

Kaufman: Yeah, I have faith in Lauren. I think she's going to do well.

Mudge: You do? Okay, alright, alright. So Lauren, let's start with an easy one. First question, what was the first music video to debut on MTV?

Bass: So this one is very much in the pop culture zeitgeist and I do know it. It's Video Killed the Radio Star.

Mudge: Can you sing it? Alright, I will, alright. Video killed the radio star…

Bass: Yes, but I was like, I can, but I'm not going to.

Mudge: I did sing, we'll see if they edit it out. Alright, Daniel, what do you got?

Kaufman: How about in Back to the Future, what is the time travel speed required for the DeLorean?

Bass: So, I'm going to give the only two buzzwords that I remember regarding Back to the Future and the DeLorean, neither of which I think is the correct answer, gigawatt and flux capacitor.

Kaufman: Okay, I think you get half a point for that. The number was 88 miles per hour. That's what you had to hit, but excellent terminology there.

Mudge: Alright, Lauren, high school in the Breakfast Club?

Bass: I have absolutely no idea.

Mudge: Oh, boo, well, you could, at least you know what state it was in?

Bass: I think. Was it Illinois?

Mudge: Yes, all John Hughes movies, all, all Illinois. Alright, we'll give you that, but it was Shermer High.

Kaufman: Okay. Who sang the classic hit, I wear my Sunglasses at Night?

Bass: I don't know the full name, but I know that the first name is Corey.

Kaufman: You get the point, Corey Hart, H-A-R-T, I believe it was spelled.

Mudge: Alright, and let's bring us closer back to our topic at hand. Lauren, what was the price of a Big Mac in 1985? What was the price of a, they didn't call it value meal back then, but Big Mac with fries and a Diet Coke?

Bass: I'm assuming this is a pop culture reference and I have legitimately no idea. But I'll go with $0.50. I don't know. Wait, was I right?

Mudge: But with the fries and the Coke, we're talking a buck 50.

Bass: Okay.

Mudge: I just, I can't...

Kaufman: Are you sure, Amy? I just Googled it. I got, it was about a buck 50 for a Big Mac and $2.59 for including the price in the Diet Coke.

Mudge: Oh my gosh, so I got it wrong. Okay, I must be harkening back to the '70s.

Kaufman: I think you're going back a little too far there.

Bass: In the 1930s, if I guessed $0.50, so.

Mudge: So look, here's what I do know, when I was a kid a candy bar was a quarter. I still to this day when I buy a candy bar, I'm like, it should be a quarter.

Kaufman: Completely agree. But Google is great for something. So Amy, asking about pricing, it of course brings us back to the topic of the day and let's hope Lauren is going to be equally as stellar there. So, let's start with understanding exactly what we're talking about. What is algorithmic pricing?

Bass: So, algorithmic pricing is an automated pricing strategy that leverages computer algorithms, artificial intelligence and machine learning to set and adjust prices in real time based on multiple data inputs and predefined rules. And the term really encompasses two distinct but related models, both dynamic pricing, which is a term that I think people know, and surveillance, or now what's being called personalized pricing. And dynamic pricing is, it's like what it says, it's an adjustment of prices in real time based on market conditions like supply and demand, competition or other factors that aren't specifically tied to personally identifiable data. And dynamic pricing, it's also sometimes called surge pricing. And I think, A, it's been in practice for years and we engage with it a lot when we buy airline tickets or concert tickets or when you try and get an Uber in the rain. And as the supply goes down, the price goes up. And as competition increases, the price often decreases. And to be clear, the practice of dynamic pricing is not actually what's implicated in the laws that we're going to be discussing today.

Those laws are actually meant to address the second model that I mentioned, which has come to be known as surveillance pricing. And surveillance pricing is the practice of using data analytics to generate prices that are tailored to individual customers based on data that's collected about that customer's personal characteristics and behaviors. Now, this could include who they are, where they've been, what they've searched for online, all in order to determine that customer's potential willingness to pay a particular price. And part of the reason for the naming of this type of pricing is that consumer data that is used can be collected through what is known as electronic surveillance technology. So sensors, cameras, device tracking, biometric monitoring, all of which are technologies that are capable of gathering personally identifiable information about a consumer's behavior, their characteristics, their location or other attributes, both in the physical and the digital environment.

Mudge: Whew, we have lots to talk about today. And in this space, because it is so hot, there are both state and federal developments. Lauren, can you, you talked about the two different definitions of algorithmic pricing. And so, we know we're focused on the surveillance pricing, which is the more nefarious way to describe it. The personalized pricing, I think is more descriptive, but there are also two different basic types of emerging laws that we're seeing. Can you walk us through that?

Bass: Yeah, so broadly speaking, the laws that govern algorithmic pricing or personalized pricing are either banning the practice outright in certain sectors or

they're not banning it, but they are requiring transparency through disclosures when the practice is occurring. But there are also some states that go both ways, they ban it sometimes and they require disclosures in other circumstances.

Kaufman: Can you walk us through what one of the early disclosure laws requires, let's say New York?

Bass: Sure. So, New York's Algorithmic Pricing Disclosure Act was the first in the nation and it went into effect actually last November. As the name suggests, it's a disclosure law. It doesn't prohibit the use of algorithmic pricing. Instead, it simply requires that there's transparency and for the business to disclose when algorithmic pricing that uses consumers' personal data is used to establish a price that's being shown. Specifically, the law applies to the use of algorithmic pricing in connection with the sale of any good or service that's offered to a consumer by an entity that's either domiciled or doing business in New York.

So by those definitions, the reach is actually pretty broad. And when algorithmic pricing is used to set a price for a good or a service, the business has to include a clear and conspicuous disclosure, and I'm sure your listeners are very familiar with that phrase. And the disclosure here should state, this price was set by an algorithm using your personal data. There are carve-outs for existing subscription-based contracts, for financial institutions, for ride services. Enforcement is by the state AG, and penalties can go up to $1,000 per violation. It is not to labor this, but it is worth noting that this is the first New York law. New York actually passed a second law, which falls under the ban, but it hasn't been signed into law by Kathy Hochul yet.

Mudge: Ah, this is one of those can't make up its mind states. Okay, alright. So, it might do both. And Lauren, give us an example of one of the ban laws. Maybe we take another one that's already been enacted in New Jersey.

Bass: Yep. So right across the river, New Jersey's Fair Price Protection Act, which takes effect in August of next year, is a ban that prohibits the use of consumers' personal data to set individualized prices for groceries and other foodstuffs. And that's a specifically defined term in the statute that's defined broadly to include groceries, beverages, paper products, household cleaning items, health and beauty products, pet food and supplies and similar household necessities.

Mudge: That's not a foodstuff. What? That's alright, alright.

Bass: Apparently, it came out of the COVID pandemic about what was considered a necessity for people. So that's where the definition stems from. Although prepared foods, if a prepared food is sold on premises, that's considered outside the scope. And the act does exempt certain pricing practices, such as reasonable costs associated with providing items to different consumers, bona fide discounts, especially when the eligibility criteria is publicly disclosed and uniformly applied, as well as discounts that are offered as part of the consumer loyalty program, provided of course that the program has clear and conspicuous and publicly disclosed terms as well as voluntary opt-in. And there is a caveat

that the personal data that is used for permitted price difference, so for one of those exceptions, it can't be repurposed without explicit consent from the consumer.

Violations here can go up to civil penalties from $10,000 for a first offense to up to $20,000 for subsequent offenses, as well as injunctive relief and restitution. And one important point about New Jersey concerns the right of private litigation. Earlier versions of the legislation included an express private right of action that didn't appear in the enacted statute. However, because the act amends the New Jersey Consumer Fraud Act, it is possible that plaintiffs could argue that existing Consumer Fraud Act remedies do remain available for alleged violations of this act. It's going to be up to the courts to decide how that fares.

Kaufman: That is interesting. Of course, the FTC is now getting involved and came out recently with a draft personalized policy statement. The comment period for that just closed. And the FTC focuses heavily on disclosure because this FTC sticks closely to what Congress has authorized it to do and does not believe it has the authority to ban any particular pricing practice.

But the policy says, or the draft policy, says in some circumstances it may be misleading or even unfair to use personalized data to set an individual price, and in such cases, the policy suggests an advertiser may need to disclose not just that it engages in algorithmic pricing, but detailing what data is used and how it affected price.

Mudge: Yeah, indeed. The FTC is very focused specifically on when AI and PII help to raise a price. It's not really clear what happens where my shopping habits were used to raise my price, but maybe Daniel, who's a savvier shopper, when his shopping habits were used to lower his price. But look, the examples the FTC gave is ones that likely violate Section 5 where they were pretty egregious. They were things like charging more for milk to a family with young children, charging more for a hotel room to someone who's in town for a funeral or charging more for a ride share for someone who's going to the hospital for an emergency. All practices we hope are not going on and are decidedly horrific.

Kaufman: Yeah, those would not be good looks. But…

Mudge: Not good looks at all.

Kaufman: Yeah, but look, the FTC notes that personalized pricing may already be common in some industries and that this policy is really not focused on that, such as setting a higher price for an Uber outside of a stadium when a show gets out. It's based on location data, so it's personalized, but consumers reasonably expect this to be the case mostly.

The FTC goes on to say, when a consumer walks into a retail store or shops online, however, she's not expecting her price to be different from someone else's based on her prior shopping patterns or history. But the statement isn't

clear if the FTC is concerned with this general practice, or only when it's used in some of those more extreme examples that Amy just outlined.

Bass: Yeah, it's going to be interesting to see what happens, because recently, the FTC sent (6)(b) information requests to about nine different companies, three airlines, rideshare companies and a food delivery service to provide info to allow the agency to study whether and how personal data was actually being used to set prices and also compensation for gig workers. Daniel, can you walk us a little bit through how this process works and what do you think the outcome will likely be?

Kaufman: Oh, thank you, Lauren. I love these kinds of questions. (6)(b) is a provision of the FTC Act, the core statute, that specifically allows the FTC to do industry-wide studies. And the FTC over the years have done a lot of really interesting things and studies on different topics. And as part of this process, they're authorized to send requests to companies for a lot of information and pretty detailed information. So, this is the process that the FTC uses to issue these kinds of industry-wide reports.

One of the interesting things to focus on here is that among the recipients of the (6)(b)s here were a few airlines, and FTC geeks may be scratching their head a little bit because the FTC does not generally have authority over common carriers. (6)(b) is different, however, it doesn't have that jurisdictional limitation. And since the airline industry is certainly one area where this issue has come up, those are included among the entities that are going to be looked at in this process. But it's going to take a while, at least a year, before a report comes out, and a year would be pretty truncated. So, we're probably looking at 2028 before we see something.

Bass: Thanks, Daniel. And it is worth noting that while the states have been front and center on this issue, there are two companion bills, one in each chamber of Congress that have been introduced to address this issue of personalized pricing. Specifically, they are H.R. 4966 and S. 3892, which are commonly referred to as the Stop Price Gouging in Grocery Stores Act. And each of them, they mirror each other and they would prevent retail food stores from using consumers' personal data to set prices.

Mudge: Yeah, it does sound like the states are way ahead here. And Lauren, I was gobsmacked by the detail in these bills that if companies are going to want to go through with this practice, they're really going to have to keep up on what states are doing what, when they're enacted, and really roll up their sleeves and be prepared to get into the weeds. But the states are really the ones to watch. And clearly, I think what our listeners want to know is, can they even begin the exploration of using their rich banks of consumer data to try to set the right price for each customer.

Look, every state enforcer I have talked to about this concept of personalized price absolutely hates the idea, thinks it's just abominable. And it actually might be better for everyone if people who are less cost sensitive are charged more,

and then the people who are more cost sensitive are charged less. And right now, that sort of happens when a good is offered at full price right up front and then later it's put on sale. People who want it now pony up the ticket price and people who want it a little less kind of wait and see if there'll still be some left and then they go on sale. But what if we could use the data that we have to identify what is the right price for each person and that could be set up front. There's some cool stuff that could happen here.

Kaufman: I know this is, of course, this is Ad Nauseum and not Privacy Nauseum because that doesn't have a good ring to it. But generally speaking, there's a lot of people that want to know what information is collected about them, how it is being used. And a lot of people may not like it if data is used to target ads to them, but they may live with it.

Now, using personal data to set prices is one area where many consumers are going to want to know about it if it's happening. And the FTC policy is clear, and some of these state laws are as well, that putting information like this in a privacy policy is not likely going to cut it. The FTC also said a business may violate Section 5 if it's using PII to set personalized prices.

Bass: Yeah, and something related to flag here is the use of electronic shelf labels in brick and mortar stores. So electronic shelf labels are digital price tags that are used by retailers to display product pricing, and they can be automatically updated from a central computer server. So, what this does is allow a retailer to set a price and to change it very easily without the need to physically go and re-sticker the entire store.

Now, part of New Jersey's law was that it implemented a one-year moratorium on the new use of any electronic shelf labels, and that moratorium goes into effect as of February 1 of next year. Importantly, it doesn't require businesses to remove existing electronic shelf labels, and it does permit new labels to be purchased, installed or deployed, but solely to repair or replace existing labels that are already operating at the same place of business. And the reason that the moratorium was implemented was actually to give New Jersey time to study what effect, if any, these labels had on surveillance pricing. So, with any of these studies, a study is going to be due, a report is going to be due six months before the moratorium expires. And then after the moratorium expires, new labels may be able to be used in compliance with the applicable law unless the legislature decides to enact a different law to specifically address that.

And importantly, New Jersey isn't the only state that's dealing with electronic shelf labels. Actually, Vermont has a law on the books already that prohibits the use of electronic shelf labels to raise the prices or to otherwise use real-time dynamic pricing to increase prices while a retail establishment is open to the public. The prices can increase only if it's made to correct a genuine price error or to otherwise fix a price, but you can't actually shift the price in real time during the store's opening, which I think is really interesting.

Mudge: Yeah, it is interesting. The personalized pricing is the, it's the what that regulators are focused on. But these ESLs really are the how such a thing can be accomplished in physical stores. And I think you raise a good point with these. And I think Daniel raised a good point, just focused on data generally.

Some of these things just have an ick factor, especially with the ESLs. If it's, Daniel has better shoes than I do, and that's always the case, if they charge Daniel more because cameras in the store thought that Daniel could afford more, that I get why folks want to take a look at that. But I certainly don't think that's what our listeners are contemplating with these ESLs. There's some great efficiencies to them. Now, Lauren, we should flag, though, that it's even more complicated than all these state laws, that there are even some localities that are getting into the game, right?

Bass: That is correct. So earlier this month, the Seattle City Council passed the Fair and Transparent Pricing Policy, which prohibits large grocery retailers from using AI and personal data to set individual prices for shoppers. Now, this marks the first U.S. city to adopt this type of legislation. And as with some of the other laws that we discussed today, this one allows for loyalty discounts that are openly advertised to broad groups such as seniors or veterans, as well as for standard coupons.

The ordinance also requires that certain disclosures relating to pricing and the decision behind the pricing, which vary by the type of entity using this type of data and include the eligibility for the discount. So, Seattle was really going all in on disclosure and transparency. And enforcement here would be by the city attorney, and it can include civil penalties of up to $3,000 per violation and $10,000 for subsequent violations. And the ordinance also contains a private right of action. So, Seattle ticked all of the boxes.

Mudge: Alright. And indeed, this is a very popular topic of discussion right now. And Lauren, you and our other colleague, Allyson Himelfarb, have done some really excellent blogs in this area and also did one of the, we do a webinar every month, a CLE webinar and you did a recent, I thought it was one of the best ones I've seen.

Bass: Thank you.

Mudge: So, kudos to you and I do encourage our listeners to watch the other content that especially Lauren and Allyson are posting in this space. Now I'm wondering though as I think a little bit more about this, is maybe all of this going to get sorted out in the court of public opinion? If consumers just have the big ick about the idea that they might pay more for something based on their shopping patterns, would consumers ever shop at a store that had to have a big headline that says, we use AI in here and your data to set prices. It seems like that would be a pretty big impediment.

Bass: Yeah, but I think it depends, right? As you said before, about how people want to determine where to spend their money, which is the whole premise behind these

disclosure laws, right? To allow consumers to make informed decisions. And consumers make these kinds of decisions all the time. For example, they'll opt into a loyalty program. They'll readily provide their data and then they'll reap the benefit of getting those rewards, which could include lower prices or coupons or opportunities to go to a sale earlier than everybody else. And based on the popularity of brand loyalty programs, many, if not all of the state laws actually passed created explicit carve outs for the use of consumer data in connection with pricing for loyalty programs, provided, of course, that broadly the programs offer transparency to the consumer about how the data is collected and will be used and that they are voluntarily opt in.

Mudge: No, it's a very fair point about loyalty programs that you're right, there are consumers that choose to shop in stores where the loyalty members pay less and the non-loyalty members pay more, and they're generally okay with that. But I think the loyalty, and maybe this is, maybe we should do another episode on this, Daniel. I was at a consumer protection conference recently, and there were multiple state AGs there was speaking on the subject, and they actually said that they're beginning to look at traditional loyalty programs with a different lens. And they said they really hadn't considered before whether these type of programs might be problematic and discriminatory, but they're taking a fresh look.

So, I just wanted to pass that on for what it's worth. I think it's a good tip for our listeners maybe to take a fresh look at their loyalty programs to see how the discounts are set, to see how the price breaks are set. But I think it is also something that's important to know that in this area, we are beginning to see lawsuits.

Kaufman: Yeah. The first and a continuing wave is focusing on company and competitive use of third-party algorithmic pricing tools, where the allegation was that such shared pricing recommendation tools facilitated price fixing among competitors. And our antitrust colleagues are involved in defending some of these suits, but the PII wave is coming and, in fact, has already started.

Bass: That's right. Target actually recently settled a lawsuit in California that alleged it used a geofencing tool in its app to show customers lower prices when they were outside of the store. But then as soon as they stepped into the store, the app showed them higher prices. And the settlement there was around $5 million.

Kaufman: Yeah. And in April, JetBlue was sued in New York, alleging that the airline used embedded trackers and third-party analytics platforms to harvest PII used to alter ticket prices individual users based on their perceived willingness to pay. And there, the suit was alleging violations of the Federal Electronic Communications Privacy Act.

Mudge: And this summer, our very own newspaper, The Washington Post, was sued over a scheme where the paper allegedly looked at subscriber demographics, reading history and browsing habits to set individualized subscription renewal rates. And look, while D.C. does not yet have a specific AI pricing law, the suit is brought under the general D.C. Consumer Protection Procedures Act. And I do

find this ironic. Allegedly, this practice was discovered when the paper complied with the New York disclosure laws and included the required language that they were setting individual prices using AI.

Kaufman: Fascinating, and good thing I still read my original hometown paper, of course, the New York Times.

Mudge: Well, good thing I focus on People Magazine for my news and avoid all of this, of course. Lauren, can you bring us home and give our readers some takeaways and how they should process what we talked about today?

Bass: Absolutely. Surveillance pricing, personalized pricing, algorithmic pricing, whatever name you give it, it's a rapidly evolving area with new laws that are pending or being enacted in multiple jurisdictions. And Daniel, as you mentioned, the FTC has shown renewed interest in the practice. So now it's a great time for retailers to review their current consumer data and pricing practices, along with the terms of any loyalty or other discount programs to better understand and potentially amend how consumer data is obtained and utilized with respect to the pricing of covered items.

As a high level, retailers should consider what consumer data feeds its pricing systems. Are discounts offered on standardized terms? Does an algorithm determine actual prices or does it merely identify promotions? Are protected characteristics or proxies for protected characteristics influencing pricing outcomes? Do existing loyalty programs adequately disclose how consumer data is collected and used? And do similarly situated loyalty program participants receive the same benefits?

Mudge: Lauren, thank you so much for joining us. This was an action-packed, exciting episode. I know our listeners really enjoyed having you here. And that, everyone, is a wrap for another episode of Ad Nauseam.

Fluharty: Thank you, Amy, Daniel and Lauren. If you have any questions for Amy, Daniel or Lauren, their contact information is in the show notes. As always, thanks for listening to BakerHosts.

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