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Consumer *Law*

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Consumer Class Actions

Class Action Waiver Provisions In Consumer Contracts And Class Arbitration

Consumer contracts increasingly include class action and class arbitration waiver provisions. The following is a typical waiver:

"No party to this arbitration agreement shall be permitted to participate as a representative, claimant, or member of any class action lawsuit or class arbitration with respect to any claim that is subject to this arbitration agreement. The parties hereby waive any right they may have had to participate in any such class action lawsuit or class arbitration. Any arbitration between the parties hereto can only address and determine the individual claims of the parties, which cannot be consolidated or joined with the claims of any other person; and the arbitrator selected pursuant to this agreement shall not have the authority to require or conduct any consolidated, joint, or class arbitration as to any claims. Should any court or arbitrator determine that this subsection is invalid, void, voidable, or unenforceable for any reason, the remainder of this arbitration agreement will then be null and void, notwithstanding the severability provision below."

Reasons for using class action waivers in arbitration agreements include stemming frivolous or potentially devastating class litigation, controlling excessive compensatory and punitive damages awards, reducing litigation costs, speeding up resolutions, and exercising greater control over dispute resolution procedures (for example, specifying the required qualifications of the arbitrator, the methods and extent of discovery, whether the case will be decided on live testimony or briefs, and whether the award will be written and reasoned and whether it will be confidential).

Where a class arbitration waiver is express, a court is likely to decide any attack on its enforceability. See, *e.g., Kristian v. Comcast Corp.,* 446 F.3d 25 (1st Cir. 2006); but see *Carbajal v. H&R Block Tax Services, Inc.,* 372 F.3d 903 (7th Cir. 2004).

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Where the agreement is silent, however, determination of whether class arbitration is permitted under the agreement could be left to the arbitrator. See, *e.g., Bazzle v. Green Tree Financial Corp.,* 123 S. Ct. 2402 (2002) (plurality opinion); *Rollins, Inc. v. Garrett, 2006* U.S. App. LEXIS 9811 (11th Cir. April 19, 2006).

The enforceability of class action waivers is currently a hotly litigated issue. Amici on behalf of consumers frequently include AARP, National Association of Consumer Advocates, and state attorneys general. See, *e.g., Muhammad v. County Bank of Rehoboth Beach*, 2006 N.J. LEXIS 1154 (Aug. 9, 2006). Class action waivers have been attacked on the grounds that they impede federal or state statutory remedies, are unconscionable, and are contrary to public policy.

Courts have differed on this issue. Some have enforced the waivers and barred class actions and class arbitrations. See, *e.g., Gilmer v. Interstate/Johnson Lane Corp*., 895 F.2d 195 (4th Cir. 1990), aff'd, 500 U.S. 20 (1991) (ADEA); *Jenkins v. First American Cash Advance of Georgia, LLC,* 400 F.3d 868 (11th Cir. 2005) (Georgia RICO), cert. denied, __ U.S. __ (February 27, 2006); *Randolph v. Green Tree Fin. Corp.,* 244 F.3d 814 (11th Cir. 2001) (TILA); *Johnson v. West Suburbian Bank,* 225 F.3d 366 (3d Cir. 2000) (TILA); *Livingston v. Associates Fin., Inc.,* 339 F.3d 553 (7th Cir. 2003) (TILA); *Iberia Credit Bureau Inc. v. Cingular Wireless LLC,* 2004 U.S. App. LEXIS 15030 (5th Cir. July 21, 2004) (La. UTPA); *Snowden v. Checkpoint Check Cashing,* 290 F.3d 631 (4th Cir. 2002) (TILA and RICO).

Other courts have held such waivers to be unenforceable. See, *e.g., Rollins, Inc. v. Garrett,* 2006 U.S. App. LEXIS 9811 (11th Cir. April 19, 2006) (under Florida law, consumer contract that prohibits class actions is unconscionable); *Kristian v. Comcast Corp.,* 446 F.3d 25 (1st Cir. 2006) (federal antitrust claims); *Tamayo v. Brainstorm USA,* 2005 U.S. App. LEXIS 20669 (9th Cir. Sept. 21, 2005) (Calif. law); *Ramsdell v. Lenscrafters, Inc.,* 2005 U.S. App. LEXIS 12337 (9th Cir. June 21, 2005); *Ting v. AT&T,* 319 F.3d 1126 (9th Cir. 2003); *Muhammad v. County Bank of Rehoboth Beach,* 2006 N.J. LEXIS 1154 (Aug. 9, 2006); *Wong v. T-Mobile USA, Inc.,* 2006 U.S. Dist. LEXIS 49444 (E.D. Mich. July 20, 2006); *Luna v. Household Fin. Corp. III,* 2002 WL 31487425 (W.D. Wash. Nov. 4, 2002).

Where a court or arbitrator invalidates a class arbitration waiver but otherwise enforces the agreement to arbitrate, class claims will be submitted to arbitration. See, *e.g., Rollins, Inc. v. Garrett,* 2006 U.S. App. LEXIS 9811 (11th Cir. April 19, 2006); *Kristian v. Comcast Corp.,* 446 F.3d 25 (1st Cir. 2006).[1] This raises several potential risks. The arbitrator may be unfamiliar with class certification standards and may employ relaxed standards for deciding class certification or the merits. In addition, judicial

1 Alternatively, a court might invalidate entire arbitration provision and allow the case to proceed in court. See, *e.g., Lowden v. T-Mobile, USA, Inc.,* 2006 U.S. Dist. LEXIS 46424 (W.D. Wash. July 10, 2006) (referring to unpublished 4/13/06 decision).

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review of such determinations is very limited. However, several national arbitration providers, including the American Arbitration Association, JAMS, and the National Arbitration Forum, have established class arbitration procedures and rules.

Considerations for drafting class action waivers include the following.

- Fair, even-handed terms increase the likelihood of enforcement.

- A severability clause could save the arbitration provision if some terms, such as the class arbitration waiver, are held to be unenforceable. Since this may be an undesirable result, consideration should be given to a clause that voids the agreement to arbitrate should a court or arbitrator invalidate a class arbitration waiver. See, *e.g., Wong v. T-Mobile USA, Inc.,* 2006 U.S. Dist. LEXIS 49444 (E.D. Mich. July 20, 2006) (holding a class arbitration waiver to be unenforceable under Michigan law and denying defendant's motion to compel arbitration because the arbitration agreement by its terms did not apply if the class action waiver provision was held unenforceable).

- Augmented appeal rights should be specified if class arbitration is permitted (for example, a panel of 3 arbitrators to hear the appeal with specific grounds supplementing the limited statutory grounds for vacating the award).

- The waiver should expressly apply to class, consolidated, and representative arbitration proceedings, not just class action lawsuits. See, *e.g., Genus Credit Management Corp. v. Jones,* 2006 U.S. Dist. LEXIS 16933 (D. My. April 6, 2006) (arbitrator's decision to permit class arbitration upheld where agreement forbade a "class action lawsuit," but was ambiguous as to class arbitrations).

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Consumer Credit

Supreme Court Broadens The Definition Of "Willful" Violations Of The Fair Credit Reporting Act

The United States Supreme Court recently addressed the important issue of what constitutes a "willful" violation of the Fair Credit Reporting Act. In *Safeco Insurance Company of America v. Burr,* 127 S. Ct. 2201 (June 4, 2007), the Court held that the statutory definition of "willful" includes not only knowing but also reckless disregard of the statute's requirements.

The FCRA provides a private right of action against companies that use credit reports but fail to comply with certain statutory requirements. Consumers are entitled to actual damages for negligent violations; however, the FCRA provides actual, statutory, and even punitive damages for "willful" violations. In Safeco, the plaintiffs alleged that the defendant insurers' practice of basing insurance rates on consumer credit history willfully violated the adverse action notice requirements of the FCRA. Addressing a threshold question, the Court ruled that "willful" included reckless, as well as intentional, violations.

Prior to Safeco, some federal circuits required a showing of an intentional violation before allowing a jury to consider whether to award punitive damages. While the Supreme Court has now broadened the definition of "willful" to include recklessness, plaintiffs continue to bear a significant burden of proof. However, as a practical matter, the Safeco decision may permit more claims to go to trial, as the determination of whether the defendant acted with reckless disregard or simply negligence could in some circumstances be a fact question for the jury. As a result, businesses in the consumer finance and credit reporting industries should review their practices to ensure their objectively reasonable compliance with the FCRA.

Significantly, the Court held as a matter of law that a defendant did not violate the lower "reckless disregard" standard because it had acted in accordance with a reasonable interpretation of the statute. Thus, the Safeco holding emphasizes the need for businesses to seek legal counsel in structuring their programs in compliance with the FCRA and assure them of this valuable

defense to a “reckless disregard” FCRA claim. Defendants still will remain liable for negligent FCRA violations; however, the lesser damages available to plaintiffs and decreased likelihood of class actions in negligence actions result in substantially smaller exposure than allegations of intentional or reckless violations.

As the district courts move forward in applying Safeco, questions still remain that will likely generate more litigation. Although Safeco employed an objective standard for determining reckless disregard, the Supreme Court declined to draw a distinct line between reckless and negligent violations. However, the decision assists both plaintiffs and defendants by clarifying the standard of proof needed to obtain statutory and punitive damages in FCRA cases.

The District Of Columbia Attorney General Settles Hidden Finance Charge Case With USA Discounters

The Attorney General of the District of Columbia has entered into an Assurance of Voluntary Compliance with USA Discounters, Ltd., settling allegations that the company violated disclosure requirements under the Truth in Lending Act and the usury limit under District of Columbia law. USA Discounters sells furniture, electronics and auto accessories to consumers at negotiable prices. Most of its customers use the retailer’s in-house closed-end financing program. The Attorney General alleged that the company routinely charged higher prices to customers using its financing program than to its cash customers, and that the markup differential constituted an undisclosed or “hidden” finance charge in violation of the Truth in Lending Act. The Attorney General further alleged that the actual finance charges exceeded the 24% *per annum* permitted under District of Columbia law.

Under the Assurance, USA Discounters agreed that for the next five years, its retail price for credit sales would not exceed 79% of the price determined by applying the highest markup used in its District of Columbia store in November 2006. The Company also agreed to pay $50,000 to the District of Columbia’s Consumer Protection Fund.

[Editors’ Note: And you thought that hidden finance charge cases were a thing of the past!]

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Debt Collection

Debt Collector Pays $1 Million To Settle FTC Charges Of Unlawful Collection Practices

Capital Acquisitions and Management Corp. and its affiliated companies (CAMCO) agreed to entry of a $1 million judgment against them to settle Federal Trade Commission charges that their consumer debt collection practices violated the Federal Fair Debt Collection Practices Act. The FTC agreed to deposit the settlement proceeds in a consumer redress fund. In addition, the settlement bars the companies, which were closed in December 2004 by a court-appointed receiver, from engaging in debt collection. A previous settlement agreement required eight of the companies' principals, officers and managers to pay an additional $300,000 and also permanently banned them from engaging in debt collection, and in March of this year, the FTC settled with the remaining individual defendant, bringing the case to a close.

The FTC commenced this action in December 2004 in the Northern District of Illinois. The complaint charged the defendants with using abusive and deceptive practices to collect debt that consumers never owed, was discharged in bankruptcy or whose collection was time-barred. According to the complaint, CAMCO purchased consumer debt from large retailers and credit card issuers across the country, claiming to have purchased more than $2 billion of such debt since it went into business in 1997.

The impermissible practices alleged include: (i) threats to sue, garnish wages, attach property or report consumers to credit reporting agencies when CAMCO had no intention of doing so; (ii) making false claims about the legal status of debts, that collectors were government agents or attorneys and that consumers faced arrest or imprisonment; (iii) attempting to collect disputed debt prior to verification; (iv) impermissibly communicating with third-parties for purposes other than locating the consumer; (v) impermissibly communicating with consumers who have directed that communications cease; and (vi) harassing consumers, their neighbors, families and co-workers by telephoning at inconvenient times, using profane language, screaming and leaving threatening messages.

Product Safety

Fisher-Price Fined Nearly $1 Million For Delay In Reporting Choking Hazard

Earlier this year, toy manufacturer Fisher-Price, Inc. agreed to pay a $975,000 civil penalty to the Consumer Products Safety Commission to settle allegations that it failed timely to report that its Little People Animal Sounds Farm toy posed a choking hazard to young children. According to the CPSC, Fisher-Price first became aware of the choking hazard six months before reporting it to the CPSC. The CPSC charged that under the Consumer Product Safety Act, the choking hazard should have been reported immediately because Fisher-Price had "sufficient information to reasonably support the conclusion that the Farms contained a defect which could create a substantial product hazard, or created an unreasonable risk of serious injury or death."

Fisher-Price first learned in September 2002 of an incident in which a nail fastener disengaged from the toy barn stall doors. By November 2002, nine consumers reported to Fisher-Price that the nail fasteners had come loose. In mid-February 2003, Fisher-Price learned that on December 14, 2002, a fourteen month old child underwent emergency surgery after the toy barn nail fastener aspirated into his lung. Before reporting the choking hazard Fisher-Price had what the CPSC noted were at least thirty-three reports that the nail fastener came loose, including four reports of children who had placed the nail fastener in their mouths. Fisher-Price did not report the choking hazard to the CPSC until March 14, 2003.

Twenty-Seven States Reach A $19.5 Million Settlement With Purdue Pharma Regarding Marketing Of OxyContin

In May 2007, twenty-six states and District of Columbia entered into a civil settlement with Purdue Pharma, L.P., the privately held pharmaceutical company that manufactured and sold about $1 billion of OxyContin annually. As part of this settlement, Purdue agreed to pay $19.5 million to these jurisdictions and further agreed to numerous restrictions regarding the marketing of OxyContin. Until 2001, Purdue aggressively marketed OxyContin, a high-narcotic analgesic, as being less likely to be abused or to lead to

addiction than other narcotics such as Vicodin or Percocet due to its twelve-hour time-release formula. The complaint alleged that Purdue had:

- employed hundreds of sales representatives to visit doctors, nurses, pharmacists and other health care professionals to expand the prescription-writing base and increase prescription writing for OxyContin;
- prepared and distributed sales aids, visuals, handouts and "leave behind" promotional items to be used by sales representatives and distributed to healthcare professionals; and
- conducted seminars, training sessions and educational programs for healthcare professionals to promote treatment of pain through increased usage of OxyContin and similar medications.

The attorneys general alleged that to encourage doctors to prescribe OxyContin, Purdue sought to:

- "enhance the acceptance of opioids for non-cancer pain," and, with respect to OxyContin, avoid any stigma attached to use of opiates;
- expand OxyContin tablets' use in the non-malignant pain market by positioning it as "the one to start with and the one to stay with;"
- establish OxyContin as the first-line choice at Step 2 of the World Health Organization pain ladder (mild to moderate pain);
- increase the use of OxyContin tablets for a wide variety of conditions, and for acute and sub-acute pain (e.g., "post-op pain, trauma, fractures"); and
- encourage assessment of pain by physicians and communication of pain by patients, and attach an emotional aspect to non-cancer pain so physicians treat it more aggressively.

The states asserted that, taken together, Purdue's marketing to physicians expanded the prescriber-base and usage of OxyContin without adequate focus on OxyContin's health and safety risks, particularly abuse and diversion. The Complaint alleged that Purdue's marketing of OxyContin violated each jurisdiction's false advertising laws.

The Consent Judgment, filed in each of the twenty-seven jurisdictions, contains Purdue's assurance that it will not promote

OxyContin in a manner directly or indirectly inconsistent with the "Indication and Usage" section of the OxyContin package insert. Specifically, Purdue agreed that:

- Purdue will not make any written or oral promotional claim of safety or effectiveness for off-label uses of OxyContin in a manner that violates the Food, Drug and Cosmetic Act;

- Purdue will not provide healthcare professionals with written materials describing off-label use of OxyContin that have not appeared in a scientific or medical journal or reference publication, except upon an unsolicited request for such information; and

- Purdue will for three years maintain records of the identity of all healthcare professionals to whom Purdue has provided materials relating to the off-label use of OxyContin.

The settlement defines "scientific or medical journal" as a publication whose articles are published in accordance with regular peer-reviewed procedure; that uses experts to review or provide comment on proposed articles; and that is not in the form of a special supplement funded in whole or in part by pharmaceutical manufacturers. The settlement similarly defines "reference publication" as a publication that has no common ownership or other affiliation with a pharmaceutical or medical device manufacturer, that has not been written, edited, excerpted, or published for such a manufacturer and that has not been influenced by such a manufacturer.

Two days after entering into this settlement, Purdue resolved criminal charges in the Western District of Virginia arising from the same marketing practices. Purdue Frederick, a Purdue affiliate, pled guilty to a felony charge and Purdue's chief executive, general counsel and former medical director pled guilty to misdemeanor charges of misbranding, a crime that includes marketing a drug with false or misleading information or promoting it for an unapproved use. In connection with these pleas, Purdue agreed to pay $470 million in fines and payments to state and federal agencies and at least $130 million to resolve some of the civil lawsuits brought by patients. The three individual defendants agreed to pay an additional $19 million in fines.

Bayer Enters Into Consent Judgments With Thirty State Attorneys General For Its Drug "Baycol"

On January 22, 2007, thirty state attorneys general reached an $8 million settlement with Bayer Corp. regarding its cholesterol-lowering statin drug Baycol. Amid allegations that the company

failed adequately to disclose known safety risks to customers, Bayer withdrew Baycol from the U.S. market in August of 2001. According to the attorneys general, Bayer learned through post-marketing research that the risks of myopathy, a neuromuscular disease, and rhabdomyolysis, a severe muscle reaction that can cause fatal kidney failure, were significantly higher for Baycol than for other statins, especially when taken in higher doses or in combination with another cholesterol-lowering drug. Although Bayer informed the Food and Drug Administration about the drug's elevated risks, it allegedly did not sufficiently warn consumers or physicians.

Under the settlement, Bayer is required to register most of its clinical studies in advance and then post the results at the end of each study, and is prohibited from making false or misleading claims in future marketing and sales of its products.

Vonage Settles With Six State Attorneys General Regarding Its 911 Services

Vonage Holdings Corporation, the nation's largest provider of Voice Over Internet Protocol telephone services, reached a settlement in December 2006 with the attorneys general of six states, Florida, Illinois, Massachusetts, Michigan, North Carolina, and Texas, requiring Vonage to inform its customers about the important differences between dialing 911 using Internet-based phone service as compared with traditional telephone service.

Vonage customers did not automatically have the ability to reach emergency services by dialing 911. Rather, customers were required to go through a separate process to activate the 911 feature. If customers failed to activate the 911 service at the time they signed up for Vonage phone service, they received a recorded message when they attempted to dial 911 in an emergency. As part of the settlement, Vonage has agreed to automatically activate consumers' ability to dial 911 when they sign up for Vonage's Internet-based telephone services.

The states had other concerns as well. Vonage did not transmit the 911 caller's telephone number and location information to emergency operators. Vonage did not directly route 911 calls to local emergency response personnel through the local 911 network but instead routed them to administrative lines which, in some areas, were answered only during regular business hours or by an Interactive Voice Response System. Despite these limitations, Vonage promoted its "911 dialing" and advertised its service as a "replacement" for landline service.

The settlement requires that Vonage:

- Disclose to customers the differences between its emergency dialing service and traditional landline telephone 911 service;

- Require customers to provide Vonage with their physical location before activating their phone service; and

- Disclose to customers that, since Vonage service is portable, each time they move or otherwise change their physical address, they should actively update their address, and that there could be a delay in updating this information in Vonage's records.

As part of the settlement, Vonage agreed to pay the states a total of $500,000.

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False Advertising

InPhonic Settles With The District Of Columbia Attorney General Over Deceptive Advertising And Processing Of Rebates

InPhonic, Inc., an Internet retailer, recently settled an action brought by the Attorney General of the District of Columbia in connection with InPhonic's advertising and sales of wireless phones and phone plans (usually sold as packages) to consumers throughout the United States. The Complaint alleged that InPhonic's marketing relied heavily on prominently advertised rebates ranging from $100 to $400. The rebates were usually contingent on the consumer maintaining the wireless service plan for a certain period of time.

The Complaint alleged that InPhonic engaged in deceptive trade practices by: (i) requiring that consumers include with their rebate claim form, a wireless plan bill dated at least 120 days after activation, but also requiring that all rebate claim forms be postmarked within 120 days from activation; (ii) stating in small print on the back pages of rebate offers, the details of such offers, such as that consumers would not be eligible for rebates if they switched to another rate plan, changed their phone number or ported their existing phone number after activation; (iii) denying claims based upon failure to receive rebate forms, even when consumers had proof of InPhonic's receipt via certified mail; (iv) failing to provide consumers with rebate forms or providing the wrong address for submission of rebate claims, and then denying the claims as untimely; and (v) failing to process rebate claims within the stated 10-12 week time period.

The Complaint also challenged the manner in which InPhonic disclosed its "purchase discounts" of $250. According to the Complaint, in small print on the back pages of many of its advertisements, InPhonic stated that it had provided an upfront discount on the phone of $250 in exchange for the consumer maintaining its wireless account for 180 days and that the $250 would be charged to the consumer without further notice if the consumer switched to a lower monthly service rate plan or failed to maintain service in good standing for 180 days. Many consumers were unaware of this potential charge until the charge appeared on their credit card statements.

The 22 page Consent Order and Final Judgment is remarkable for the level of detail in regulating how InPhonic will conduct its business going forward. It specifies the exact words, location and font size to be used in InPhonic's price advertising; requires that consumers be apprised of all terms and conditions of rebate offers and affirmatively consent by checking a box, which unless checked, will prevent the transaction from being completed; and specifies that all terms of a rebate or other offer must be made available by clicking a link titled "Rebate [credit or discount] terms" and providing specific requirements for the typeface, font size, and color used on the page that is linked. In addition, InPhonic agreed to alter its customer service practices to include e-mailing acknowledgment of receipt of rebate claims; maintaining a website and toll-free number where consumers can check the status of their rebates; and maintaining a toll-free number for rebate questions which must be staffed 5 days a week from 8:00am to 7:00pm CST by live operators who must answer such calls within 60 seconds and not exceed a 6% abandoned call rate. InPhonic also agreed to pay $100,000 to the District of Columbia and make restitution to some 9,000 consumers nationwide.

Recent NAD Decisions Of Interest

The National Advertising Division of the Council of Better Business Bureaus has issued the following recent decisions of interest.

A Wachovia Bank Commercial Featuring A True Vignette Of Extraordinary Customer Service Could Mislead Consumers Into Believing They Could Replicate The Identical Experience.

As part of its routine monitoring program, the NAD reviewed a series of "true vignettes" television commercials for Wachovia Bank that share a common tagline stating, "At Wachovia we are absolutely obsessed with satisfying our customers." The NAD took issue with one of these commercials. It featured Joe Carta, a Wachovia customer, who explained that on Christmas Day, the day before his son was scheduled to leave for a Caribbean vacation, the son realized that his passport was in the family's safe deposit box at Wachovia. Mr. Carta says that he called his Wachovia banker at home that day to ask for her help, and that "[she] and her team spent their holiday working on it." At 5 a.m. the next morning, they opened the vault just for Mr. Carta. The commercial ends with a voice-over delivering the "obsessed with customer service" tagline and Mr. Carta stating that his son made the flight and "I'm with Wachovia."

Wachovia explained that as a result of the many large bank mergers over the past two decades, consumer dissatisfaction with service has been a problem in the industry for years,

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and Wachovia became determined to improve its customer satisfaction ratings. To that end, in the late 1990's Wachovia developed an internal program designed to stress the importance of personal commitment to customers through high level monthly reviews and discussions of customer service issues and solutions, and company-wide employee recognition and incentive programs.

As a result, Wachovia rose from a subpar national customer satisfaction rating in 1999 to be ranked first in customer service for the last several years by the American Customer Satisfaction Index, to be ranked "highest" by J.D. Power & Associates in customer satisfaction with home equity lines of credit and home sales, and to receive numerous other accolades and awards.

The NAD found that the commercial contained an express claim that "At Wachovia we are absolutely obsessed with satisfying our customers." And the NAD further found that the facts presented by Wachovia provided a reasonable basis for that claim.

The NAD then posed the question whether the commercial also contained an implied claim that "The service depicted is representative of a service a Wachovia customer can typically expect." Wachovia had not produced any consumer perception evidence and so the NAD used its own experienced judgment to evaluate that question and concluded that the commercial did contain such an implied claim. The NAD went on to find that although Wachovia does provide excellent customer service, the Joe Carta story was "predicated upon a number of serendipitous circumstances." The NAD noted that Wachovia does not have a policy that employees should disrupt their family activities to help customers, that bankers give out their home telephone number, or that requires them to take customer calls at home. Thus, the NAD found that the precise elements of the service in this true vignette could not typically be replicated. In that regard the NAD cited the FTC Guides on Endorsements and Testimonials, which state that "where the endorser's experience is not typical of what a consumer would generally achieve, the advertisement should either clearly and conspicuously disclose what the generally expected performance would be in the depicted circumstances or clearly and conspicuously disclose the limited applicability of the endorser's experience to what consumers may generally expect to achieve." The NAD concluded that Wachovia should discontinue the commercial.

Claims For Pledge Furniture Cleaner That It Kept Furniture Less Dusty Longer Were Not Supported By Studies On The Appearance Of Dust

Colgate-Palmolive Company, the manufacturer of Murphy Soft Wipes, challenged television, website and free-standing insert

advertising claims made by S.C. Johnson & Son, Inc. regarding its Pledge furniture cleaning products.

The challenged claims stated, “DUST LESS Pledge Anti-Dust formula keeps your wood less dusty longer;” “Keep your furniture less dusty – longer!;” “New anti-dust formula keeps surfaces less dusty, longer;” and “Anti-dust formula lets you dust less often.”

Pledge works by employing an anti-static agent to remove dust and then depositing a thin film of silicone on the surface to increase the surface’s shine or gloss and reduce the visibility of accumulated dust. S.C. Johnson described two studies it conducted, which it argued supported its claims that Pledge kept surfaces less dusty longer. The first study used a wood surface, half dusted with Pledge and half dusted with a dry cloth. After one week’s worth of dust accumulated, all respondents in the study determined that there appeared to be more dust on the untreated half. The second study used a variety of surfaces, and most respondents reported that the surface treated with Pledge appeared less dusty.

The NAD found that the claims that Pledge is an “anti-dust” formula that keeps wood and furniture “less dusty, longer” had to be supported “by data showing the product’s ability to reduce the actual amount of dust on wood and furniture,” but that both studies were “designed to assess Pledge’s effect on the appearance of dustiness – not the product’s ability to actually remove dust.” While the NAD did not question Pledge’s ability to reduce the appearance of dustiness, it determined that these studies were insufficient to support claims concerning the actual amount of dust.

Additionally, the NAD found that S.C. Johnson’s submission regarding its wood study did not include relevant facts concerning its methodology, such as the amount of Pledge used, whether the wood surfaces were finished, and if so, with what type of finish. Regarding the multi-surface study, S.C. Johnson evaluated the surfaces just one day after the product was applied, but the claims at issue were not limited to the product’s effectiveness after just one day. The NAD concluded that this study should have assessed the product’s effects for more than one day.

Although much of the advertising featured both Pledge spray and Pledge wipes, the studies were conducted exclusively on Pledge spray, and S.C. Johnson did not submit any evidence demonstrating how or why the spray’s performance could be extrapolated from the wipes’ performance. Without such evidence, the NAD concluded that the studies were insufficient to support a claim about the wipes.

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Starbucks Agrees To Modify The Name Of Its "Caramel Apple Cider" Based Upon Consumers' Expectations Regarding The Distinction Between "Cider" And "Juice"

The Better Business Bureau of Eastern Massachusetts, Maine and Vermont, Inc. challenged the truth and accuracy of Starbucks Corp. advertising for its steamed apple beverage "Caramel Apple Cider."

Starbucks's Caramel Apple Cider contained freshly steamed 100% apple juice, which was a pasteurized blend of sweet and tart apples, mixed with cinnamon syrup and Starbucks's proprietary buttery caramel sauce. The Better Business Bureau argued that Starbucks should not use the name "cider" to describe this beverage because it was made with apple juice and not cider.

Starbucks responded that no laws or regulations establish what constitutes cider or draw any distinction between apple cider and apple juice, that there is no established distinction between cider and juice and no single consumer point-of-view as to what constitutes cider or juice. Accordingly, Starbucks argued that naming and marketing its beverage as cider was neither inaccurate nor misleading to consumers.

The NAD considered whether Starbucks's marketing of its beverage as cider was accurate and consistent with reasonable consumer expectation. Acknowledging the absence of any regulatory authority or standard definitions making a distinction between cider and juice, the NAD found that in the absence of such guidance it was to be guided by the reasonable expectation of consumers. The NAD determined that, even though there was no standard definition of cider, consumers could reasonably expect the Caramel Apple Cider to contain some characteristics of cider as distinct from juice, such as expecting the beverage to be cloudy, brownish and minimally filtered or processed. Other factors consumers might associate with cider as compared to juice is that it would be fresher, more nutritious, have a shorter shelf life, and be unpasteurized. The NAD noted that consumers who ordered Caramel Apple Cider were served the beverage in a paper cup and thus could judge the drink only by its taste, but not the identity, color or freshness of the ingredients.

The NAD decided that even though the marketing and name of Starbucks's Caramel Apple Cider did not offend any government regulation, consumers could nonetheless be confused, and the product could convey a message inconsistent with consumers' understanding of the distinction between juice and cider.

Skin Doctors Cosmeceuticals Claims Regarding Its Eyetuck Anti-Bag Technology Found To Be Unsubstantiated

Continuing to demonstrate its ongoing interest in aging skin "solutions," the NAD requested substantiation for performance claims made in print and Internet advertising by Skin Doctors Cosmeceuticals for its Eyetuck Anti-Bag Technology.

Skin Doctors' print advertisement for Eyetuck displayed the product directly above the text, "an eyetuck without surgery?" and next to the text; "Skin Doctors introduces Eyetuck – the first and only product specifically developed to treat serious under eye bags and puffiness. Results in just 15 days!" Skin Doctors' Internet advertising claimed, "Discover the new technology that could make eye surgery a thing of the past!" The Internet advertisement also included before-and-after photographs of the under-eye area of a presumable product user showing a dramatic, visible reduction in puffiness under the eyes.

Skin Doctors argued that the text "An eyetuck without surgery?" was posed as a question and that it was offering an alternative to plastic surgery. The NAD has repeatedly held that absent competent and reliance scientific evidence, advertisers of cosmetic face creams or serums should not compare their product, expressly or by implication, to plastic surgery or injections that penetrate the skin. The NAD found that "An eyetuck without surgery?" was not a mere question, but an implication that the same results from surgery could be obtained through use of Eyetuck. In the absence of evidence that such results could be achieved with Eyetuck, the NAD recommended that Skin Doctors discontinue this claim. The NAD also found that "Discover the new technology that could make eye surgery a thing of the past!" implied that Eyetuck could deliver results comparable to those achieved through plastic surgery.

Skin Doctors voluntarily discontinued its claim that Eyetuck was the first and only product specifically developed to treat serious under-eye bags and puffiness, after being informed that competing products already contained the active ingredient Eyeseryl.

Skin Doctors contended its "Results in 15 days!" claim was supported by testing on Eyeseryl conducted by its manufacturer, although Skin Doctors had not conducted any testing on Eyetuck itself. The NAD found that in the absence of product testing, the advertiser "may not extrapolate testing results on a particular ingredient contained in its product to substantiate performance claims for its product" when it contains other ingredients that could affect the product's performance.

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The NAD found that the real photographs from the study of 20 women did not show results as clear as those depicted in the advertisement's before-and-after-photographs and that 11 out of the 20 participants actually experienced either slight or no reduction in puffiness. Thus, the NAD determined that the advertising photographs were not accurate representations of the performance results consumers could typically expect to achieve and recommended that the photographs be discontinued.

The NAD concluded that since Eyeseryl had been found to have some qualities that could help reduce puffiness under the eyes, Skin Doctors was free to advertise that fact.

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Unfair and Deceptive Trade Practices

Arizona Attorney General Settles With "Foreclosure Assistance" Company While Other States Take Aim At Such Companies Legislatively

In December 2006, Arizona Attorney General Terry Goddard announced a settlement with Deed and Note Traders, Inc. (DNT), a "foreclosure assistance" company, resolving allegations that DNT deceptively offered consumers a "simple way to save their homes" in violation of the Arizona Consumer Fraud Act. As part of the settlement, DNT agreed to no longer engage in the business of foreclosure assistance.

According to the Complaint, DNT offered a "HomeSavers" program, telling consumers they could sell their homes to DNT, rent them back and eventually (after approximately two years) repurchase their homes from DNT. The Attorney General alleged that this program was deceptive, because consumers would sell their homes for a *de minimus* amount, pay exorbitant rent to DNT until they could no longer afford to pay another month's rent, and then be evicted from their homes by DNT. At the time the Attorney General filed suit (earlier in December 2006), only two HomeSavers consumers had succeeded in repurchasing their homes from DNT on their own. A third consumer hired legal counsel to facilitate his repurchase.

The HomeSavers program allegedly worked as follows:

- DNT targeted consumers facing foreclosure with a certain amount of equity in their homes;

- DNT told consumers that the only way to avoid foreclosure was to transfer title to DNT by warranty deed;

- DNT reinstated consumers' mortgages and generally paid them off within a year, generally permitting DNT to acquire homes for 50-70% of their value.

DNT solicited consumers by promising them immediate cash, but actually paid very little, in one instance only $25. DNT also promised two months or more of free rent, but later reneged on all or part of the offer.

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DNT did not provide consumers a lease until they signed warranty deeds. Thus consumers were often unaware of what their monthly rent would be at the time they transferred title to DNT, permitting DNT to charge a rent equal to or greater than the consumer's mortgage payments had been. Even when DNT initially set consumers' rent at an amount lower than their mortgage payments had been, DNT often raised the rent within a few months. For example, one consumer was facing foreclosure because he could not afford his $380 monthly mortgage payment. DNT initially charged the consumer $300 rent, but after six months, raised the rent to $700 a month. When consumers were unable to pay their rent on time, DNT imposed a 20% fee, ensuring that consumers would fall farther behind. Eventually, the consumers would be evicted, and DNT would place the homes on the market.

Even when consumers were able to pay their rent, they were often unable to exercise their option to repurchase because of the onerous terms. These terms included a 10% down payment and financing through DNT at an interest rate of at least 10.5-11% over only seven years. When consumers could not afford this amount at the end of their lease term, DNT would agree to extensions on the condition that the consumers agree to a higher repurchase price. For example, DNT offered several extensions to one couple, but in return increased the repurchase price from $89,000 to $165,000. As a result, many consumers could not repurchase and were evicted.

When repurchase did not occur, DNT placed the homes it acquired on the market as "No Qualifying" Rent-to-Own Transactions. The Attorney General alleged that this offer was deceptive, because consumers were rarely able to purchase the homes they rented. Consumers paid DNT several thousand dollars as a non-refundable lease purchase deposit to enter into an eighteen-month lease with an option to purchase. Consumers also had to make a down payment on the house, often within six months of moving in. Like the HomeSavers program, the "No Qualifying" Rent-to-Own program targeted consumers with credit problems; DNT did not tell consumers the lease terms until they had paid their lease purchase deposit; DNT charged 20% late fees; and the terms of the option to purchase included financing through DNT-approved lenders or through DNT itself at a minimum interest rate of at least 10.5-11% over only seven years. From October 2004 through November 2005, only 3 of 74 consumers in "No Qualifying" Rent-to-Own Transactions purchased their rental from DNT.

The Attorney General alleged that DNT's HomeSavers program and "No Qualifying" Rent-to-Own Transactions, violated Arizona's Consumer Fraud Act. Without admitting its practices were deceptive, DNT agreed to stop offering foreclosure assistance

and to pay more than $400,000 in restitution, attorney's fees and costs. The company agreed to permit current customers to repurchase the homes in which they were living at a discount; to finance the purchase of those homes for at least fifteen years under affordable terms; and to reduce late payment fees to no more than 3% of the monthly payment and eliminate prepayment penalties and increases in the interest rate upon default. The company is permitted to remain in the rent-to-own business, and agreed to clearly disclose the rent-to-own agreement terms, including the fixed monthly rental payment, the dollar amount charged for late fees, the dollar amount of option payment or down payment, the number of months covered by the lease, the total amount of the security deposit, the date down payment is due, and the fixed purchase price.

Arizona is not the only state taking aim at foreclosure assistance or "mortgage rescue" companies. In May 2005, Georgia became the first state in the nation to specifically criminalize mortgage fraud. Since then a growing number of states have enacted or are considering mortgage fraud legislation. For example, Illinois enacted its Mortgage Rescue Fraud Act, effective January 1, 2007, requiring mortgage rescue companies to determine that the homeowner possesses the financial ability to make rental payments and repurchase the home before the property is sold, and requires mortgage rescuers to clearly disclose all material terms. Under the Act, when homeowners are unable to repurchase their homes, the rescuers must pay them at least 82% of the home's fair market value.

Texas Attorney General Settles With Lender Over Deceptive Marketing Of Subprime Credit Cards

In January 2007, the Texas Attorney General entered into an Agreed Final Judgment and Permanent Injunction with Cross Country Bank Inc. d/b/a Applied Card Bank and its affiliate Applied Card Systems, settling allegations that the Company violated the Texas Deceptive Trade Practices – Consumer Protection Act and the Texas Debt Collection Act by preying on financially marginal consumers, urging them to apply for credit cards to "improve their credit," and then surprising them with low credit limits and hidden charges, and engaging in threatening, harassing, and deceptive debt collection practices. Texas was the sixth state in two years to sue the bank.

According to the Attorney General's petition, Cross Country Bank advertised credit limits of "up to" $2,500, but generally set credit limits as low as $200 to $400. The bank also charged a $150 origination fee and a $50 annual membership fee or recurring monthly fees when consumers' applications were processed—charges which often consumed at least half the consumer's credit. Cardholders were often unaware of their low credit limit

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and the fees until they received their first statement, by which point many cardholders had already unknowingly exceeded their credit limit with just one or two small purchases, resulting in additional over-limit fees. The bank also charged cardholders fees for customer assistance services, such as receiving copies of billing statements or accessing account information.

The Attorney General alleged that when cardholders became unable to pay their mounting credit card charges, the bank engaged in threatening, harassing, and deceptive collection practices. For example, the bank would call consumers multiple times per day, both at home and at work; disclose consumers' financial situation to co-workers, neighbors, or family members; use derogatory, abusive, threatening, and obscene language; and threaten to garnish wages.

Under the settlement, defendants are permanently enjoined from engaging in misleading and harassing conduct. Defendants also agreed to clearly disclose fees, credit limits, the terms of expedited processing of applications (further requiring a material difference in the length of time in which the application is processed if an additional fee is charged), the material terms and automatic renewals of associated services, and the identity and affiliation of callers on behalf of defendants. Defendants agreed to pay $1.29 million in penalties and attorney's fees to the State, and to provide restitution to eligible consumers of all fees and other amounts charged to their credit cards, other than for authorized purchases. Defendants are also required to contact credit reporting agencies to update and correct their reports.

FTC Permits Resale Of Certain Returned Electronic Goods

In December 2006, the FTC responded to Sony Corporation's request for an advisory opinion regarding modification of Sony's policy on the resale of returned electronic products. Sony's policy had been to treat all opened returns as though they had been used by the customer. Sony designated these products as "Class B" and resold them as refurbished at a significant discount. Sony sought to modify its policy to exclude from its Class B inventory those products inspected by customers, but never turned on, and to resell those products as "new."

In its December 20, 2006 reply, FTC Associate Director of Consumer Protection James Kohm referred to the FTC's 1969 Enforcement Policy on "Merchandise Which Has Been Subjected to Previous Use on Trial Basis and Subsequently Resold as New," which states that deception lies where a marketer fails to disclose material facts relevant to a purchaser's decision to buy or not to buy, and that prior use is one such material fact. In that Enforcement Policy, the FTC distinguished between products that the purchaser had used and those that the purchaser had

merely inspected. The FTC's response to Sony stated that by limiting its program to products that the purchaser had never turned on, Sony would be reselling products that fell into the latter category, and therefore, Sony's customers would not be misled. Furthermore, Sony's proposed product inspection program was deemed to be comprehensive enough to prevent the resale of defective products.

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Privacy and Data Security

Massachusetts Bill Would Impose Liability On Retailers For Data Breaches

In what appears to be a first, a bill introduced in January in the Massachusetts House of Representatives would make "any commercial entity" liable for the costs of a bank's reasonable actions on behalf of its customers as a direct result of a data security breach. These costs would include the costs of the bank's actions: (i) to protect a customer's sensitive financial personal information and; (ii) to continue to provide financial services to customers. Commercial entities would also be liable for the costs incurred by banks to reimburse customers for unauthorized transactions.

The bill defines the term "commercial entity" broadly to capture virtually any legal entity that deals with consumers or their personal data, including business organizations of all types, not-for-profits and governmental entities.

A public hearing on the bill was held in April 2007, but the bill does not appear to have advanced within the Massachusetts legislature since that time. Supporters of the bill say that their goal is to encourage any business or organization that deals with sensitive personal information—whether a retailer, a governmental entity, or a not-for-profit organization—to place tighter security controls on their systems. The impact on consumers is not clear, as federal law already places a $50 limit on a consumer's liability for fraudulent charges, and many credit card companies already waive this charge.

Smaller banks, in particular, have argued that they must absorb the costs of data leaks, and they are not happy picking up the tab for data leaks that are not their fault. Retailers counter that they already pay high costs for potential fraud through the imposition of what are commonly referred to as "interchange fees." These are charges assessed by the bank and credit card industry for each transaction and equal approximately $2 for every $100 of retail purchase. Often, the credit card issuing bank receives between 70 and 90 percent of the fee, while the credit card company receives the balance.

At least five other states, California, Connecticut, Illinois, Texas and Minnesota, subsequently considered similar legislation. In Minnesota, the legislation passed by an overwhelming majority in both houses and was signed into law by the Governor in May, and will apply to data breaches occurring on or after August 1, 2008. This issue will no doubt be raised in other states and perhaps soon at the national level, given reports that Congress may be looking at similar legislation.

Sony BMG Settles FTC Charges Over Anti-Piracy Software

In June, the Federal Trade Commission approved a settlement of charges against music industry giant Sony BMG Music that it did not adequately inform consumers about intrusive anti-piracy software included on its CDs. The software, known as digital rights management (DRM) software, automatically installed itself when consumers inserted the CDs on their computers, restricted the number of copies the consumer could make of the CD to three, prevented the music from being directly transferred to certain devices, including Apple's market-dominating iPod, and monitored the consumer's listening preferences for marketing purposes.

The FTC asserted that the software was unreasonably difficult to uninstall and exposed the consumers to security risks because it allowed hackers and other third parties to gain access to their computers. The FTC concluded that Sony BMG's failure to disclose the existence of the DRM software and what it would do to the consumer's computer was a deceptive trade practice.

Under the settlement, consumers who purchased CDs with the DRM software will be allowed to return the CDs to Sony BMG in exchange for versions of the CDs without the software. The settlement did not require Sony BMG to pay any civil penalties and does not bar Sony BMG from selling CDs with DRM technology. Sony BMG will, however, have to clearly and prominently disclose on the packaging of its CDs the existence of any software restricting the use of playback devices or limiting the number of copies that can be made. Sony BMG is required to obtain the consent of consumers before any DRM software is installed and is barred from using the information on consumers' listening preferences collected through the monitoring technology installed on their computers to send targeted advertising. In addition, Sony BMG is required to disclose the existence of any monitoring technology included on its CDs and obtain consumers' consent before using that technology. Because the software is alleged to be difficult to locate and uninstall, the settlement requires Sony BMG to reimburse consumers up to $150 if their computers were damaged by attempts to uninstall the software.

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The DRM software was included on more than one hundred Sony BMG titles and the FTC estimates that at least 17 million CDs were sold with the software. The settlement comes at a time when the music industry, facing several years of declining sales, struggles in its efforts to stop music piracy. This case was not the only time Sony BMG's failure to disclose the DRM software's effects resulted in legal action. In 2005, Sony BMG settled a class action suit filed in the Southern District of New York, and in 2006, Sony BMG settled complaints brought by the attorneys general of California and Texas.

Newsbites

Earlier this year, the FTC announced that Florida-based telemarketing firm The Broadcast Team agreed to pay a $1 million civil penalty after the FTC alleged that the firm used "voice broadcasting" automatic dialing technology to make calls to over 64 million consumers in violation of the FTC's Telemarketing Sales Rule (TSR). The FTC's complaint, filed in late 2005 in the Middle District of Florida, stated that when the calls were answered by a live person, rather than by voice mail or an answering machine, The Broadcast Team would end the call immediately or would play a recorded message before hanging up the call. The TSR requires that calls answered by a person be connected to a live representative within two seconds. The FTC also alleged that The Broadcast Team called more than a million telephone numbers listed on the Do-Not-Call Registry and that The Broadcast Team placed calls on behalf of sellers who had not paid for access to the registry, also making the calls unlawful. The Broadcast Team made the vast majority of the calls at issue on behalf of debt management services-related companies.

* * *

In the last issue of the Newsletter (Fall 2006), we reported on the FTC's actions in October 2006, denying a 2004 proposal to establish a safe harbor under the FTC's Telemarketing Sales Rule for prerecorded telemarketing calls to established customers and revoking its previous policy of forbearing from enforcing the abandoned call prohibition against telemarketers who complied with the provisions of the proposed safe harbor. Shortly after we went to press, the FTC announced that it was extending that policy of non-enforcement until the completion of other prerecorded call amendment proceedings. Thus, the moratorium continues.

* * *

The FTC's Annual List Of Top Consumer Complaints For 2006:

(1) Identity Theft (36%)
(2) Shop-at-Home/Catalog Sales (7%)
(3) Prizes/Sweepstakes and Lotteries (7%)
(4) Internet Services and Computer Complaints (6%)
(5) Internet Auctions (5%)
(6) Foreign Money Offers (3%)
(7) Advance-Fee Loans, Credit Protection/Repair (2%)
(8) Magazines and Buyers Clubs (1%)
(9) Telephone Services (1%)
(10) Health Care (1%)
(11) Business Opportunities, Work-at-Home Plans (1%)
(12) Travel, Vacations, and Timeshare (1%)
(13) Office Supplies and Services (1%)
(14) Grants: Scholarships/Educational & Non-Educational (1%)
(15) Employment Agencies/Job Counselors/Overseas Work (1%)
(16) Investments (1%)

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