



THE CHAIRMAN

FEDERAL TRADE COMMISSION  
WASHINGTON, D.C. 20580

November 14, 2008

Michelle Jun, Esq.  
Consumers Union  
101 Truman Avenue  
Yonkers, NY 10703-1057

Re: *Petition for Rulemaking and Other Agency Actions Relating to Retail Gift Cards*

Dear Ms. Jun:

Thank you for your September 11, 2008 letter on behalf of the Consumers Union, Consumer Federation of America, the National Consumer Law Center, and U.S. PIRG (hereinafter, the "Petition"). The Petition requests that the Federal Trade Commission ("FTC" or "Commission") promulgate a new rule and take other actions to address consumer protection concerns raised by the sale of gift cards by retailers that subsequently file for bankruptcy.

As I discuss below, the Petition raises significant issues that can greatly impact consumers and businesses. The magnitude of these issues necessitates careful study before the FTC can respond fully to the Petition. Thus, this is an interim response setting forth the FTC's actions in this area as well as the intended course of action going forward.

As you know, the Commission has used its enforcement authority to address problems with gift cards. In March and April 2007, the Commission announced enforcement actions against Kmart Corp. and Darden Restaurants, Inc. (which owns Red Lobster and Olive Garden). The Commission approved consent orders in these matters in August and May 2007 respectively. In both cases, the FTC alleged that the companies promoted their gift cards as equivalent to cash, but failed to disclose adequately dormancy fees assessed when a gift card is not used for a period of time. The Commission alleged in these cases that many consumers did not learn about the dormancy fee until they attempted to use their cards. In settling the cases, the companies agreed to disclose dormancy fees prominently in future advertising, disclose the existence of any such fees on the front of their gift cards, and provide refunds to affected consumers. Both companies voluntarily stopped charging dormancy fees on their cards.

More generally, retailers have moved away from the use of dormancy fees on gift cards and have improved their disclosure practices. Fees on retail gift cards are now less common, and numerous states have proposed and passed laws prohibiting or limiting such fees. The

Montgomery County, Maryland, Office of Consumer Protection, which provided invaluable assistance to the Commission in this area, noted in its annual gift card survey that, with few exceptions, it now may be difficult to find national retail cards with fees or expiration dates.<sup>1</sup>

In addition to our law enforcement actions, we have worked to educate consumers about gift cards so that they can make informed decisions. In February and December 2006, the Commission issued consumer education materials in both English and Spanish regarding buying, giving, and using gift cards. These materials are available in print and online. The FTC also released consumer guidance in the form of a news article distributed via North American Precis Syndicate (“NAPS”).<sup>2</sup> Among other points, the FTC advised consumers to read the fine print before they buy, to ask about any expiration dates or fees, and to check on any purchase exemptions. Commission staff have also conducted business outreach to discuss the consumer protection issues raised by retail gift card marketing.

The Petition asks the FTC to promulgate a rule requiring retailers to segregate and hold in trust gift card funds, and declare the failure to do so an unlawful and deceptive practice. The intended result of such actions would be to guarantee that consumers are able to obtain the value of their gift cards in the event the issuing retailer files for bankruptcy. The Petition also requests that the FTC intervene in bankruptcy proceedings, develop a registry to track the gift card practices of retailers in bankruptcy proceedings, and halt sales of gift cards by bankrupt retailers as well as any third party vendors.

As you know, the Commission may initiate a rulemaking, under Section 18 of the FTC Act, to prescribe “rules which define with specificity acts or practices which are unfair or deceptive acts or practices in or affecting commerce.” 15 U.S.C. § 57a(a)(1)(B).<sup>3</sup> In determining whether to conduct a Section 18 rulemaking proceeding, the Commission considers a number of factors including: the nature of the practices at issue; the prevalence of such practices; the cost and feasibility of challenging enforcement of those practices; the extent of the harm caused by those practices; and the likely reduction of harm should the proposed rule be adopted. In addition, the Commission compares the likely costs of undertaking rulemaking and ultimately enforcing the proposed rule to the benefits of the proposed rule.

Your petition raises a number of significant and complex factual and legal questions, particularly with respect to bankruptcy law. Bankruptcy law already establishes a set of priorities for unsecured creditors. Congress set consumer creditors at a lower priority than

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<sup>1</sup> *Gift Cards 2007: Best and Worst Retail Cards; A Deeper View of Bank Cards Doesn't Improve Their Look*, MONTGOMERY COUNTY, MARYLAND, OFFICE OF CONSUMER PROTECTION, <http://www.montgomerycountymd.gov/content/ocp/giftcards2007final.pdf>.

<sup>2</sup> NAPS is a service that distributes news to over 10,000 newspapers across the country.

<sup>3</sup> The Commission may also commence a rulemaking when directed by Congress under the Administrative Procedures Act.

employees' wages and contributions to employee benefit plans.<sup>4</sup> One issue raised by your Petition is whether a Commission rule could alter the mandated order of the Bankruptcy Code priorities by allowing claims of consumers holding gift cards above those of employees. In addition, there are a number of related legal questions, including whether segregated funds still would be considered part of the debtor's estate, how the automatic stay would apply to the funds, and the role of state laws. Ultimately, your proposal requires careful consideration of how it would affect the goal of successfully reorganizing the corporation and ensuring it creates future earnings to pay off its debts.

Apart from these bankruptcy law issues, analysis is needed on how your proposal intersects with corporate, accounting, and financial considerations when selling and redeeming gift cards. Finally, the differing types of gift cards (purchased, promotional, those given in lieu of refunds, corporate incentive programs, etc.) will need to be considered in the overall analysis.

In the interim, however, it is important for consumers to realize that there is a risk that they might not obtain the full value of their gift cards if a retailer files for bankruptcy or goes out of business. Accordingly, we have revised our gift card consumer education materials to advise consumers of this risk.<sup>5</sup>

I have determined that, in connection with assessing the Petition's requests, the Commission needs to obtain additional factual and legal information about these and other issues. I have instructed my staff to work on these issues, and they are in the process of reaching out to retailers and experts who may have relevant information. My staff would welcome any additional information you may have or the opportunity to discuss these issues with you. Please contact Peggy Twohig, Associate Director, Division of Financial Practices, at 202-326-3224 or [ptwohig@ftc.gov](mailto:ptwohig@ftc.gov). The Commission appreciates the concerns raised by Consumers Union and looks forward to working together in the future to protect America's consumers.

Sincerely,



William E. Kovacic  
Chairman

cc: Jean Ann Fox, Consumer Federation of America  
Lauren Saunders, National Consumer Law Center  
Ed Mierzwinski, U.S. PIRG

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<sup>4</sup> 11 U.S.C. § 507(a)

<sup>5</sup> FTC Consumer Alert: Buying, Giving, and Using Gift Cards, *available at*: <http://www.ftc.gov/bcp/edu/pubs/consumer/alerts/alt010.shtm>.