



UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION
WASHINGTON, D.C. 20580

Office of the Secretary

February 7, 2002

Dolores S. Smith, Director
Division of Consumer and Community Affairs
Board of Governors of the Federal Reserve System
Washington, D.C. 20551

Dear Ms. Smith:

This letter responds to your request for information regarding the enforcement activities of the Federal Trade Commission (“Commission” or “FTC”) under the Truth in Lending, Consumer Leasing, Equal Credit Opportunity, and Electronic Fund Transfer Acts (“Acts”) during the year 2001 for use in preparing the Federal Reserve Board’s (“Board”) Annual Report to Congress. You have asked for information regarding the Commission’s enforcement activities pursuant to those Acts, including methods of enforcement, and the extent to which compliance is achieved by entities subject to the Commission’s enforcement authority.¹ Also, you have asked whether the Commission recommends any changes to these laws or their implementing regulations or wishes to provide other comments or observations.

I. THE COMMISSION’S 2001 ENFORCEMENT ACTIVITIES UNDER THE ACTS ²

Truth in Lending Act and Consumer Leasing Act

In calendar year 2001, the Commission continued its enforcement efforts to curb abusive practices of some subprime mortgage lenders, which included one new action and two ongoing litigations against mortgage lenders for alleged violations of the Truth in Lending Act (“TILA”),

¹ The Commission is charged with enforcement of the FTC Act and various federal consumer financial laws and regulations, including the TILA, CLA, ECOA, and EFTA, with respect to most nonbank entities in the nation. The Commission does not have data regarding the extent of compliance by these numerous nonbank entities with these mandates. As a result, the letter does not provide information on this issue.

² Information concerning the Commission’s enforcement and other activities discussed in this report is also available at the Commission’s web site at “<http://www.ftc.gov>.”

Regulation Z, and the Federal Trade Commission Act (“FTC Act”). These cases seek orders awarding injunctive relief and consumer redress. In addition, the Commission obtained settlements in two other cases, one involving vacation travel packages and the other involving Internet access products and services, that alleged violations of the TILA, Regulation Z, and the FTC Act. These cases and other initiatives are discussed below. Other investigations of potential TILA and/or CLA violations are ongoing.

A. Mortgage Cases Alleging TILA Violations

The Commission filed a complaint in federal district court against Associates First Capital Corporation and Associates Corporation of North America (collectively, “The Associates”), Citigroup Inc. (“Citigroup”), and CitiFinancial Credit Company.³ The complaint charged The Associates – one of the nation’s largest subprime lenders at the time of its merger with Citigroup – with violations of the TILA, Regulation Z, and/or the FTC Act, as well as other laws.⁴ According to the complaint, The Associates engaged in deceptive practices and other law violations to induce consumers to take out or refinance loans with high interest rates, costs, and fees and to purchase high-cost credit insurance. The complaint charged The Associates with numerous violations of the FTC Act, including unfair collection practices, failure to disclose the cost and terms of credit insurance and misrepresentations of: 1) savings from consolidating debts into home equity loans; 2) the loan amount; 3) the cost and coverage of credit insurance; and 4) the credit insurance refund. The complaint also charged The Associates with violating the TILA, Regulation Z, and the FTC Act, by “splitting” one loan into two separate transactions, failing to provide required disclosures, and disbursing money prior to expiration of the rescission period. The complaint also charged The Associates with violating the TILA, Regulation Z, and the FTC Act, by failing in their advertisements to disclose clearly and conspicuously loan fees, balloon payments, and other information.

The Commission continued its litigation and filed an amended complaint against First Alliance Mortgage Co. and two affiliated companies, which had been among the nation’s largest subprime home equity lenders. The amended complaint added the CEO to the action, and a related individual as a relief defendant.⁵ The amended complaint charged defendants with violations of the TILA, Regulation Z, and/or the FTC Act, and alleged that defendants target homeowners with poor credit histories who may experience difficulty securing conventional home equity financing. Among other things, the amended

³ Federal Trade Commission v. Citigroup Inc., No. 1:01-CV-0606 (N.D. Ga. Mar. 6, 2001).

⁴ The complaint also charges Citigroup Inc. and CitiFinancial Credit Company, successor corporations to The Associates.

⁵ Federal Trade Commission v. First Alliance Mortgage Co., No. SACV 00-964 DOC (EEx) (C.D. Cal filed Oct. 3, 2000) (amended complaint filed Aug. 14, 2001).

complaint alleged that defendants:

1) misrepresented the total amount borrowed, upon which interest accrues, is the amount financed that appears on the TILA disclosure statement when, in fact, that amount does not include the loan origination fees; 2) misled consumers about the existence and amount of origination fees, the interest rate, and the monthly payments of their short-term “teaser rate” adjustable rate mortgages (“ARMs”); 3) did not have a reasonable basis to substantiate their claims that consumers will save money when consolidating debts through their loans; and 4) failed to provide borrowers with ARM loans with information required by the TILA and Regulation Z that explains ARMs.

Litigation also continued against Capital City Mortgage Corp. (“Capital City”), a Washington, D.C.-area mortgage company, and its owner, Thomas K. Nash.⁶ The complaint’s allegations include that defendants violated the TILA and Regulation Z, and engaged in unfair or deceptive acts or practices, in violation of the FTC Act, by: 1) understating the APR and finance charges; 2) failing to disclose or accurately disclose the payment schedule (including failing to disclose a balloon payment); and 3) failing to provide disclosures that accurately reflect the legal obligation. The complaint also alleges that defendants engaged in other deceptive or unfair practices in offering and extending credit and throughout the loans, in violation of the FTC Act, with the result that a number of borrowers were overcharged on their loans, were defaulted, and had title to their homes or other property impaired or completely lost (along with the equity). A trial date has been set for March 25, 2002.⁷

B. Other TILA Cases

A stipulated final judgment was entered against Epic Resorts, LLC and Epic Travel, LLC, and their CEO, timeshare developers that used telemarketers to sell vacation travel packages to consumers.⁸ Among other things, the complaint alleged that defendants and their telemarketers promised consumers credits on their credit cards for returned vacation travel packages, and failed to provide them. The stipulated final judgment includes a requirement that defendants refund the money of customers who returned their vacation packages within defendants’ 30-day cancellation period and requested, but did not receive, their refunds. The judgment also prohibits defendants from making various misrepresentations, and from violating the TILA and Regulation Z, by failing to provide credit card refunds within seven business days of accepting returned vacation packages.

⁶ Federal Trade Commission v. Capital City Mortgage Corp., No. 1:98CV00237 (D.D.C. filed Jan. 29, 1998).

⁷ The case is joined with a private lawsuit, Hargraves v. Capital City Mortgage Corp., No. 98CV1021 (D.D.C. filed Apr. 24, 1998).

⁸ Federal Trade Commission v. Epic Resorts, No. 6:00CV1051ORL-19-C (M.D. Fla. Sept. 5, 2001).

A consent decree was entered against Netpliance, the marketer of a device advertised as a less expensive alternative to the personal computer for Internet access and e-mail, called the “i-opener.”⁹ The complaint charges included that the company misrepresented, in violation of the FTC Act, that consumers had only thirty days to dispute a charge to their credit card accounts for services rendered by the company when federal law gives consumers sixty days to dispute such charges. The complaint also alleged that the company failed to issue promised credits to consumers’ credit card accounts within seven business days of accepting returned property, in violation of the TILA and Regulation Z. The consent decree requires the company to clearly and conspicuously disclose various terms and qualifications associated with using the i-opener or any other Internet or online access product or service and to reimburse consumers for improperly billed charges. The consent decree also prohibits the company from misrepresenting any consumer’s rights under the TILA and from failing to comply with the credit card refund requirements of Section 166 of the TILA and Section 226.12(e)(1) of Regulation Z.

C. Other Initiatives

The Commission testified before the Financial Institutions and Consumer Credit Subcommittee of the U.S. House of Representatives’ Financial Services Committee regarding rent-to-own (“RTO”) transactions.¹⁰ The Commission’s testimony presented the key findings of the Commission’s Bureau of Economics’ survey of RTO customers (“BE survey”).¹¹ The Commission’s statement noted that RTO transactions are not specifically regulated by federal laws that govern other transactions, such as the TILA and CLA, and that federal legislation that would specifically regulate RTO transactions has been proposed several times in the past decade. Based on the findings of the BE survey, the Commission’s testimony did not recommend federal legislation regarding the RTO industry at this juncture; determining whether federal legislation is needed requires information regarding RTO transactions in addition to that considered in the BE survey. Such additional information would include, for example, whether consumers currently understand the total cost of RTO transactions, what information they have available at present, and what alternatives to the RTO transaction they typically consider.

⁹ United States of America v. Netpliance, Inc., No. A-01-CA 420SS (W.D. Tex., June 27, 2001).

¹⁰ Prepared Statement of the Federal Trade Commission before the Financial Institutions and Consumer Credit Subcommittee, House Financial Services Committee on Rent-to-Own Transactions (July 12, 2001) presented by J. Howard Beales III, Director, Bureau of Consumer Protection, Federal Trade Commission.

¹¹ See Survey of Rent-to-Own Customers, Federal Trade Commission, Bureau of Economics Staff Report (April 2000). Additional information regarding the RTO survey was provided in the Commission’s Annual Report to the Board on TILA, ECOA, and EFTA for 2000 (Feb. 20, 2001).

The Commission testified before the California State Assembly Committee on Banking and Finance on predatory lending practices in the subprime mortgage market, including practices that may involve the TILA and the Home Ownership and Equity Protection Act ("HOEPA").¹² The testimony addressed various lending practices occurring with some lenders in the industry that have concerned the Commission. The testimony also noted that the Commission has increased its enforcement activities to halt lenders engaged in predatory lending, coordinating efforts with other federal and state agencies, and increasing educational activities for consumers to help them avoid potential home equity lending abuses.

D. Consumer and Business Education

The Commission continues to view consumer and business education efforts as important complements to its enforcement activities. In 2001, the Commission's Northeast Regional Office hosted a Forum on Predatory Lending that involved consumer representatives, bankers, state and federal regulators, and homeowners and senior citizens.¹³ The forum focused on various legislative, legal, and community-based initiatives to combat predatory lending practices that can exploit lower-income and minority borrowers and target elderly homeowners.

The Commission issued updates to various consumer publications to provide up-to-date information to consumers. All of the Commission's consumer protection materials were made available to the public through the Commission's website.

Equal Credit Opportunity Act

In calendar year 2001, the Commission filed one action and continued other litigation against two mortgage lenders for alleged violations of the Equal Credit Opportunity Act ("ECOA") and Regulation B. These cases seek orders awarding equitable relief and/or civil penalties. Other enforcement efforts continue.

First, the Commission's complaint against The Associates and others, discussed above, alleged, among other things, that The Associates also failed to maintain consumers' loan applications and certain related records, in violation of Regulation B.¹⁴

¹² Prepared Statement of the Federal Trade Commission before the California State Assembly Committee on Banking and Finance on Predatory Lending Practices in the Home-Equity Lending Market (Feb. 21, 2001), presented by Ronald G. Isaac, Assistant to the Director of the Federal Trade Commission's Bureau of Consumer Protection.

¹³ Commissioner Mozelle Thompson was a keynote speaker at the forum.

¹⁴ See supra note 3.

Second, the Commission's complaint against Capital City, also discussed above, alleged among other things that the company and its owner, Thomas K. Nash, violated the ECOA and Regulation B by: 1) failing to take written applications for mortgage loans; 2) failing to collect required information about the race or national origin, sex, marital status, and age of applicants; 3) failing to provide rejected applicants with written notice of adverse action; and 4) when providing notice of adverse action, failing to provide applicants with the correct name and address of the Commission, the federal agency that administers compliance with the ECOA with respect to defendants Capital City and Nash.¹⁵

The Commission continued its consumer and business education efforts, including efforts to increase awareness of and compliance with the ECOA. The Commission also continued its participation in the Interagency Task Force on Fair Lending.

Electronic Fund Transfer Act

In 2001, the Commission continued its consumer and business education efforts in this area. The Commission released a new brochure, "Electronic Check Conversion," which provides information to consumers about this important new form of electronic banking.

II. ANY SUGGESTIONS FOR CHANGES IN THE ACTS OR THEIR IMPLEMENTING REGULATIONS

In 2001, the Commission filed two comments supporting Board proposals to change Regulation Z provisions implementing HOEPA and Regulation C provisions implementing the Home Mortgage Disclosure Act ("HMDA").¹⁶

The Board is addressing issues related to the Electronic Signatures in Global and National Commerce Act ("ESIGN") in connection with various federal consumer financial requirements, including the TILA, CLA, ECOA, and EFTA. In 2001, the Commission and the U.S. Department of Commerce conducted a public workshop and released a report prepared jointly at the request of Congress regarding ESIGN.¹⁷ The ESIGN Report concerns the benefits and burdens of the

¹⁵ See supra note 6.

¹⁶ Letters from Commission to Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System: 1) Mar. 9, 2001, Re Docket No. R-1090, Regulation Z; 2) Mar. 9, 2001, Re Docket No. R-1001, Regulation C.

¹⁷ Report to Congress on The Electronic Signatures in Global and National Commerce Act: The Consumer Consent Provision in Section 101(c)(1)(C)(ii) submitted by the Federal Trade

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“reasonable demonstration” requirement of the consumer consent provision in ESIGN. The ESIGN Report states, “it is reasonable to conclude that, thus far, the benefits of the consumer consent provision of ESIGN outweigh the burdens of its implementation on electronic commerce It preserves the right of consumers to receive written information required by state and federal law. The provision also discourages deception and fraud by those who might fail to provide consumers with information the law requires that they receive.”¹⁸ The ESIGN Report also concludes that ESIGN’s reasonable demonstration requirement “appears to be working satisfactorily at this stage of the [ESIGN Act]’s implementation,” and recommends that Congress take no action at this time to amend the statute.¹⁹

The Commission hopes that the information contained in this letter responds to your inquiry and will assist in preparation of the Board’s Annual Report to Congress. If any other information would be useful or if you wish to request additional assistance, please contact Joel Winston, Acting Associate Director, Division of Financial Practices, at (202) 326-3224.

By direction of the Commission.

Donald S. Clark
Secretary

Commission (Bureau of Consumer Protection) and the Department of Commerce (National Telecommunications and Information Administration) (June 27, 2001) (ESIGN Report). The ESIGN Report is available at the Commission’s website. Information on the ESIGN Public Workshop (Apr. 27, 2001) is contained in the ESIGN Report and separately at the Commission’s website.

¹⁸ ESIGN Report at 13.

¹⁹ Id. at 14.