Federal Trade Commission

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BEFORE

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GOVERNMENT AFFAIRS CONFERENCE

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The views expressed are those of the Chairman and do not necessarily reflect those of the Federal Trade Commission or the other Commissioners.

It is a pleasure, as usual, to meet with the Direct Marketing Association. I am happy to be here today to talk with you about issues facing both DMA and the Commission as well as some of our shared goals. You may be happy to know that I will not be talking about postal rates for third class mail.

Both DMA and the Commission are faced with the proliferation of new direct marketing techniques such as infomericals and 900-numbers. Like the Commission, DMA must attempt to address the problems associated with new technologies as they develop. The challenge for the FTC in the 1990's will be to fashion a program that provides strong national consumer protection in a changing environment without unduly interfering with dynamic and competitive market forces. As the explosion of information and marketing technology continues, it seems to me that it is imperative that your industry mount a vigilant defense against the fraud artists who would tarnish your legitimate efforts to communicate with and market to consumers.

Today I would like to talk to you about how the Commission has begun to scrutinize some of the problems associated with infomercials and 900-numbers. In addition, I will talk about our efforts in the telemarketing area, some general advertising issues and the Mail Order Rule.

One of the newest forms of direct marketing, is the "infomercial" or 30-minute commercial program. Viewed by some as the "electronic mail order" business of the future, these

seemingly ubiquitous programs have gotten the industry off to a start with a shaky reputation.

What distinguishes the 30-minute infomercials from traditional advertising is the lengths that some producers go to hide the fact that the program is an advertisement at all. That fact is what attracted so much attention to this new format. The Commission's first action against an infomercial producer was one where the complaint alleged deception in the format of the program, but did not challenge the claims made for the sunglasses, the subject of the program.[1] In subsequent cases involving a variety of products, from diet patches to baldness cures to bee pollen, the Commission has attacked the claims for the product being sold, as well as the format of the show.

In some instances infomercials are marketers using new technology to market old products. That point was brought home dramatically in the case of a company called Twin Star Productions, Inc.,[2] where the Commission obtained a cease and desist order and an agreement to make refunds of $1.5 million. The Commission learned a lot about the informercial business because of Twin Star. In an SEC registration statement for a public stock offering -- a public document, of course -- Twin Star laid out the economics of the infomercial business and gave

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[1] JS&A Group, Inc. et al., 111 FTC 522 (1989).

[2] Twin Star Productions, Inc., C-3307 (Oct. 2, 1990).

a glimpse of where the industry will have to go if it is to have a viable future in the direct marketing industry.

The potential impact of the FTC's action on Twin Star is clear from its SEC disclosure that three of the products it had to discontinue because of government actions had accounted for 78% of its sales during 1988. Twin Star disclosed that it sells many of the same products through mail order catalogs, and these sales although made at a price lower than through its infomercial programs, produce a higher gross profit margin due to the fact that the overhead for these sales does not include the cost of broadcast time. Thus, we can expect, I believe, the same old products to be marketed through catalogue sales, telemarketing efforts, and other direct marketing means. Therefore, the Commission and its staff will have to maintain the same attentive approach to marketers and products, whether marketed through infomercials or some other medium.

I emphasize, however, that the Commission has not tried to "kill" the infomercial industry. To the contrary, we have tried to bring cases and otherwise manage our work in a way that will allow legitimate infomercials to achieve whatever degree of success a free market allows.

Recently, Advertising Age announced that General Motors would be attempting a 30-minute program for its Saturn car and, in the same issue, it reports that the State of Arizona plans half-hour ads to sell visitors on Arizona. It is not surprising that neither GM nor Arizona refers to its product as an

"infomercial," using such other new terms as "documercial" to distinguish it from its less elegant ancestor. If the FTC's efforts result simultaneously in weeding out fraud and nurturing a new medium for legitimate direct marketing, the Commission and its staff will indeed have made a worthwhile contribution.

The Commission has also begun looking at another relatively new type of marketing involving the telephone -- the growing misuse of "900" telephone numbers. The 900-number phenomenon, where the consumer pays a fee for each call, is an innovative means of marketing information that can, and often does, benefit consumers. Although 900-numbers can provide valuable information and services, such as weather, sports, and opinion polls, there has been a proliferation of unscrupulous 900-number providers. Scam operators have learned that by using the 900-number service, they can make money merely by persuading consumers to place a call, rather than having to get them to provide their credit card number.

Although the Commission's jurisdiction over common carriers, is limited, it has brought several actions against some of the information providers. The targets of the Commission actions to date have involved information providers who fail to disclose in advertising that the call costs money or the full cost of the call. In addition, the Commission actions have involved situations where the consumer is induced to make the call through false promises. The product or service promoted may offer useless credit cards to persons with bad credit histories, travel

packages no one can use, or bogus employment placement information. Many people only realize after they have incurred the charge, that they have been duped.

The Commission recently announced the first settlement in a 900-number case with FTC v. Transworld Courier Service.[3] In that case, it was alleged that the defendants ran help-wanted classified advertisements for construction workers and listed a toll-free 800 telephone number for applicants to call. When consumers called the 800-number a recording instructed them to dial a 900-number if they were interested in a job. Neither the newspaper advertisement nor the tape recorded message on the 800 line disclosed that there was a charge of $15 to $18 for calling the 900-number. Moreover, the defendants routinely failed to provide any job information to those consumers who did call.

The court recently approved a settlement in this case requiring defendants to pay $1 million in consumer redress. The settlement also required that the defendants include a complete cost disclosure in future 900-number ads and to include a "preamble" at the beginning of each toll call telling callers they can hang up after hearing the preamble and thereby avoid the charge. The Commission is currently litigating three other 900-number cases in federal court and has a number of other investigations underway, so you can expect to see more in this area in the future.

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[3] FTC v. Transworld Courier Services, No. 1:90 CV-1635-JOF (N.D. Ga.)

The Commission continues to bring traditional telemarketing cases including investment frauds in such items as rare coins, art, gemstones, and gold mine interests. Almost all these scams share promises that the investment is low risk, will yield a high return, and must be acted upon quickly. Many of these scams are quite sophisticated. For example, the Commission filed a case in federal court last fall that involved what amount to a leveraged investment in precious metals.[4] The defendants represented that the investment was low risk with a high yield. In fact, it was an extremely risky investment where some consumers lost everything when they received a margin call and were unable to come up with more money to cover the margin. The Commission's telemarketing efforts also involve sellers of water purifiers, vacation packages, and the resale of timeshare or recreational property, just to name a few.

The Commission brings these fraud cases in federal court to stop the frauds and to obtain redress for consumers. Under appropriate circumstances, we are able to proceed ex parte and seek a Temporary Restraining Order and freeze the proposed defendants assets, in order to provide redress to consumers at the conclusion of the case.

You may be interested in learning about a settlement the Commission announced last week that is the largest settlement in

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[4] FTC v. Group America Inc., et al. Civil No. 90-4913 H.L.H (Ex), C.D. CA (Sept. 13, 1990).

a telemarketing fraud case in our history.[5] It illustrates that we are looking at root systems and not just individual cases. Under the terms of the agreements, more than $47 million will be distributed to more than 8,000 consumers. The settlement stems from a July 1983 Commission complaint alleging that three southern Florida companies and ten individuals engaged in false and deceptive sales practices in connection with application filing services for a federal oil and gas lottery. Consumers were falsely promised that they would win valuable oil and gas leases based on expert information and sophisticated computer analysis.

After the initial action against the primary defendants, the Commission and a court-appointed receiver learned that there were numerous parties who had aided and abetted the defendants. Separate actions were filed against some of these parties, such as accountants, lawyers, insurance companies, banks and even the Better Business Bureau of South Florida. The announcement of these settlements sends important messages to those in the financial, legal, and accounting communities who may be tempted by the profits of knowingly aiding and abetting a fraud.

The Commission recently filed a complaint alleging that a company was marketing a turn-key telemarketing business.[6]

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[5] FTC v. U.S. Oil and Gas Corp., Case No. 83-1702-CIV-HOEVELER (S.D. Fla.); and In re U.S. Oil and Gas Litigation, Case Nos. 83-1702-AL-CIV-HOEVELER and 83-1702-A2-CIV-HOEVELER (S.D. Fla.).

[6] FTC v. Listworld, Inc., CV-91-N-0979-NE (N.D. Ala.)

According to the complaint the defendant companies and individuals sold credit packages to dozens of telemarketers, who in turn sold them to consumers. The defendants were alleged to have sold to telemarketers the printed mail solicitations, the telephone scripts, the mailing lists targeting people who have credit problems, and the credit programs themselves. In addition, the complaint alleged that the defendants offered to set up 900-numbers for its telemarketer clientele to sell the packages. It appears, therefore, that there is a direct connection emerging between conventional telemarketing fraud and 900-number fraud.

Turning to national advertising issues, one of my goals at the Commission that directly affects the direct marketing industry is to improve the Commission's presence and activities in the national advertising field. Your industry, whether it solicits orders by direct mailings, catalogues, newspaper ads, magazine ads, broadcast ads, infomercials or even telemarketing, engages in national advertising.

An important development in advertising during the last few months is not a particular case or investigation, but in the improved relationship with the FTC and the State Attorneys General. Several advertising cases in the past year were brought with the cooperation of the States. I believe that the Commission's work in this area has been and will continue to be to develop fair, economically rational, predictable, and

understandable law enforcement policies and then to enforce them vigorously.

A new area for the Commission and one in which the States have a keen interest is the area of environmental advertising claims. The American public is becoming increasingly interested in the environmental effects of the products they use. A recent poll indicated that 82% of those surveyed reported changing their purchasing decisions based on concerns about the environment.[7] This consumer demand presents enormous incentives for innovation in environmental technology -- less wasteful packaging, new material, "ozone safe" products, and so forth. Not surprisingly, manufacturers have been quick to flood the market with products bearing "environmentally safe," "degradable," and other environmental claims to address this demand. However, there have been exaggerated and unsubstantiated claims as well. Deceptive or unsubstantiated claims can only reduce consumer confidence in such "green claims," reducing the incentive of producers to be innovative in this area.

The Commission is conducting over 20 active investigations in the environmental-claims area. The staff is examining the accuracy of particular product performance claims, such as "photodegradable," "biodegradable," and of more general claims, such as "environmentally friendly," and "environmentally safe." Just last month the Commission accepted for public comment a

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[7] J.W.T. Greenwatch, Vol. I, No. 2, J. Walter Thompson USA consumer survey, autumn 1990.

consent agreement settling charges that a spray cement product contains an "ecologically-safe propellant" and that use of the product will not damage the environment.[8] In that case, the Commission settled allegations that Zipatone, which sells adhesive spray cement, falsely claimed that its product was safe for the environment. It was true that the propellant in its spray was ozone safe. However, the company failed to disclose that the ingredient being propelled was itself a Class I ozone depleter as defined in the Amended Clean Air Act.

The Commission has also agreed to participate in a joint task force with the Environmental Protection Agency and the United States Office of Consumer Affairs and we will work closely with the states to discuss the federal response to deceptive environmental marketing. The Commission is planning to hold public hearings to learn more about a number of petitions and recommendation for guidelines that we have received, and about other options available for providing guidance to the public on these difficult questions.

I would now like to talk about the more traditional direct marketing business and discuss some of the Commission's more recent actions. As you are aware, the Commission accepted a consent order with Haverhills, a San Francisco company, which

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[8] Zipatone, Inc., File No. 902-3366. (Accepted for public comment Apr. 22, 1991).

disseminates a catalog under that name.[9] The Commission had begun a series of cases involving the safety of sun tanning devices several years earlier.[10] Those cases involved claims that the devices were safer than the sun, did not have any of the harmful side effects associated with the sun and did not increase the risk of skin cancer. The cases involved ads where models were using the equipment without protective eyewear. To alert consumers further about such claims, the Commission's Office of Consumer and Business Education published a "Facts For Consumers" about sun tanning devices. This was followed up by a number of other media efforts to warn consumers about such claims.

Despite these cases, the resulting publicity, and the serious health and safety risks, Haverhills continued to make the same representations that the Commission had challenged. Accordingly, the Commission brought an action against Haverhills for ads that were identical to the ads challenged in the previous cases. Specifically, the Commission's complaint charged that Haverhills misrepresented the safety of a sun tanning device as well as the efficacy of a gas savings device.

In another recent case that may have an impact on your industry, the Commission entered into a consent agreement with

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[9] Haverhills, Inc., 55 Fed. Reg. 47536 (Nov. 14, 1990)(published for comment). The Commission gave final approval to the consent order on January 25, 1991.

[10] The Silver Group, Inc., 110 F.T.C. 380 (1988); Sun Industries, Inc., 110 F.T.C. 511 (1988); and An-Mar International, Ltd., Docket No. C-3261 (1989).

United States Sales Corporation,[11] for the failure to disclose in its mail-order catalogs the geographic origin of the textile products it advertised and offered for sale, in violation of the Textile Fiber Products Identification Act.

I mention these cases because I think it is important to stress the point that consumers must be provided with truthful information. Therefore, it is necessary that advertisers and marketers make certain that the claims they make are substantiated. This includes descriptions of products in catalogues.

Finally, I would like to turn to the Mail Order Rule. As you know the Mail Order Rule has been in effect for 15 years and its requirements essentially coincide with what you know to be fundamentally good business practices. Perhaps that is why DMA and its members have long supported the Rule. I know that Lorna Christie, DMA's Vice-President for Ethics and Consumer Affairs, her staff and DMA's two ongoing committees that handle ethics issues are responsible for educating many direct marketers about the Rule and mediating disputes between businesses and consumers. For your involvement and help in achieving compliance with the Rule, I want to express my appreciation and gratitude.

Since 1985, the Commission has brought 17 enforcement actions, involving 60 individual and corporate defendants, for violating the Rule. And, we obtained nearly $2 million in civil

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[11] United States Sales Corp. C-3313 (Nov. 21, 1990).

penalties. Cases involved products ranging from computers to clothing.

To bring you up to date on the status of the rulemaking proceeding to amend the Rule to include telephone orders, the rulemaking staff has submitted its proposed Staff Report summarizing and analyzing the comments and made recommendations to the Bureau for review. There will be a comment period on staff's and the Presiding Officer's reports and then a recommendation will be made to the Commission. A final decision may not be made until the end of this year.

Conclusion

The Commission's record shows our active enforcement efforts during the past year. I hope you agree that our actions, while numerous, are sensible and set standards that are reasonable. I look forward to working with all of you as we strive to protect the widest possible consumer choice in a deception free market place.