Commissioner MacIntyre concurred in the result but not in the opinion. Commissioner Jones dissented for the reasons set forth in her accompanying dissenting statement.

IN THE MATTER OF

UNIVERSAL CREDIT ACCEPTANCE CORPORATION, ET AL.

ORDER, ETC., IN REGARD TO THE ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 8821. Complaint, Oct. 6, 1970—Decision, Feb. 16, 1973.

Order requiring three California corporations engaged in the advertising and sale of franchises which authorize franchisees to sell memberships in a credit card program, among other things to cease deceptions and misrepresentations with respect to the "Honor All Credit Card" program. Respondents are further required to offer a 7-day cooling-off period for cancellation of future contracts with full refund rights. An individual respondent is further required to refund all payments for franchise fees within 90 days to everyone who became members of franchisees during the last seven years.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Universal Credit Acceptance Corporation, a corporation, Continental Credit Card Corporation, a corporation, and International Credit Card Corporation, a corporation, also trading as National Credit Service, and John Clifford Heater, individually and as an officer of Universal Credit Acceptance Corporation and International Credit Card Corporation, and Howard P. Gingold, individually and as an officer of Continental Credit Card Corporation, hereinafter referred to as respondents, have violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Universal Credit Acceptance Corporation is a corporation organized, existing, and doing business under and by virtue of the laws of the State of California, with

its principal office and place of business located at 218 California Drive, Burlingame, California.

Respondent Continental Credit Card Corporation is a corporation organized, existing, and doing business under and by virtue of the laws of the State of California, with its principal office and place of business located at 218 California Drive, Burlingame, California.

Respondent International Credit Card Corporation, also trading as National Credit Service, is a corporation organized, existing, and formerly doing business under and by virtue of the laws of the State of California, with its principal office and place of business formerly located at 2305 South El Camino Real, San Mateo, California.

Respondent John Clifford Heater is an individual and an officer of Universal Credit Acceptance Corporation and International Credit Card Corporation. His business address is the same as the corporate respondent, Universal Credit Acceptance Corporation. Respondent Howard P. Gingold is an individual and is an officer of Continental Credit Card Corporation, and his business address is the same as said corporate respondent.

Respondent Heater has been and is primarily responsible for establishing, supervising, directing and controlling the acts and practices of each of said corporate respondents. He originally engaged in the business activities alleged herein under the names of National Credit Service and corporate respondent International Credit Card Corporation, and said activities were transferred to and have been continued under the names of corporate respondents Universal Credit Acceptance Corporation and Continental Credit Card Corporation.

Respondent Gingold, in addition to his functions as president of respondent Continental Credit Card Corporation, also has acted as a salesman of franchises for said corporation.

The aforementioned respondents cooperate and act together in carrying out the acts and practices hereinafter set forth.

PAR. 2. Respondent International Credit Card Corporation, also trading as National Credit Service, was, and respondents Universal Credit Acceptance Corporation, Continental Credit Card Corporation, John Clifford Heater, and Howard P. Gingold were and are now engaged in the advertising and offering for sale and sale of franchises which authorize the franchisees to sell retail merchants memberships in respondents' "Honor All Credit Card" program for the use of respondents' credit card services, and in

the advertising and offering for sale, and sale of such services to retail merchants.

Respondents first sell franchises to persons who invest a substantial sum of money as a condition to being granted exclusive rights to sell memberships in respondents' "Honor All Credit Card" program (hereinafter referred to as respondents' program). Second, directly and through such franchisees, respondents sell their credit card clearing services to retail merchants (hereinafter referred to as members), who invest substantial sums of money as fees, dues and service discounts on credit sales. Respondents' program entitles members to sell their respective products and services to customers presenting any one of a large number of credit cards approved by respondents, and to submit such credit charges to respondents. Respondents collect the charges from the customers of members and remit payment to the members.

PAR. 3. In the course and conduct of their business as aforesaid, respondent International Credit Card Corporation, also trading as National Credit Service, has caused, and respondents Universal Credit Acceptance Corporation, Continental Credit Card Corporation, Heater and Gingold were and are now causing their advertising matter to be published in newspapers of interstate circulation and their promotional materials to be mailed or otherwise conveyed to various persons residing outside the State of California in each and every State of the United States and in foreign countries. Advertising matter, applications, contracts, franchise agreements, letters, checks or other written instruments and communications have been sent and have been received between the respondnts at their places of business located in California, and persons in various other States of the United States and of foreign countries. As a result of said interstate advertising and promotion and as a result of said transmission and receipt of said written instruments and communications, respondents have maintained a substantial course of trade in said franchises and credit card services in commerce, as "commerce" is defined in the Federal Trade Commission Act.

PAR. 4. In the course and conduct of their aforesaid business, respondents now engage in, and/or have engaged in, a continuing program of recruiting franchisees to sell respondents' services and of selling memberships in respondents' program.

A. SALE OF FRANCHISES

Respondents solicit the sale of their franchises in the following manner and by the following means. Respondents publish, or cause to be published, in magazines and newspapers of regional and national circulation and disseminate through the mails advertisements inviting inquiries from persons interested in becoming franchisees. To persons who respond to such invitations, respondents send through the mails advertising and promotional material containing many statements and representations regarding respondents' services and the financial and other benefits to be enjoyed by persons who become franchisee of respondents. Persons who express further interest receive a telephone sales presentation by one of respondents' sales representatives and, in most instances, are invited to visit respondents' place of business, now in Burlingame, California. Respondents also disseminate said advertisements, statements and representations through existing franchisees for the purpose of soliciting the sale of subfranchises, new franchises, and the resale of franchises.

Typical and illustrative of said representations and statements appearing in advertising and promotional material, but not all inclusive thereof, are the following:

FULL OR PART TIME BUSINESS You can have a SECURE FUTURE as a business partner with America's leading credit organization. Our unique service allows retail business firms to honor over 200 million credit cards now in use, including most major oil company cards * * * with guaranteed payment from us.

Opportunity for EXCEPTIONALLY HIGH EARNINGS. $10,000 investment required. Partial financing considered. Renewals and bonuses insure permanent security and income. No age limit. For personal interview, write Universal Credit Acceptance Corp., Box 593, Burlingame, California 94010. WRITE TODAY, while your area is still available.

DID YOU NOTICE THIS AD IN THE BUSINESS OPPORTUNITIES SECTION OF YOUR NEWSPAPER?

ARE YOU LOOKING—for a profitable addition to your present income or business? Why not diversify with a non-competitive service that offers immediate profits and a virtually unlimited opportunity for future business expansion.

NOW—YOU CAN OBTAIN THE SALES RIGHTS for the "HONOR ALL CREDIT CARD" program in your area. Through our program, any merchant, large or small, can make *instant credit sales* to more than 100 million credit card customers * * * with guaranteed payment. It is the most appealing business and sales promotion program on the market today!

FIND OUT FOR YOURSELF! Ask any merchant if he would like to be able to accept the 3 leading all-purpose credit cards plus those issued by

over 50 different oil companies—over 100 million potential customers—without risking his own money.

YOUR PROFITS ARE IMMEDIATE—THEY ARE SUBSTANTIAL—THEY ARE CONTINUOUS! This is the opportunity you've been waiting for * * * the chance to own a secure, profitable full or part-time business. Complete details can be yours at once. Simply fill out the attached card and MAIL TODAY.

B. SALE OF CREDIT CARD SERVICES

Respondents solicit the sale of their credit card services to members in the following manner and by the following means. Respondents disseminate through the mails to retail merchants advertisements and promotional material containing many statements and representations regarding respondents' services and the financial benefits to be enjoyed by persons who become members. Leads resulting from responses to said mailings are forwarded to respondents' franchise holders who also make such statements and representations directly with the aid of sales kits, and other material supplied to them by respondents.

Typical and illustrative of said representations and statements to prospective members, but not all inclusive thereof, are the following:

UNIVERSAL CREDIT ACCEPTANCE CORP * * * the nation's largest credit card clearing house, is your answer to increased business. You fill out just ONE simple form for any credit sale. You receive ONE BIG CHECK for all credit sales every month. It's fast! It's easy! It's PROFITABLE! Payment is guaranteed, non-recourse.

PAR. 5. By and through the statements and representations contained in the advertising and promotional material referred to in Paragraph Four hereof, and others similar thereto but not expressly set out herein, and in the course of oral sales presentations, respondents, their agents, representatives and employees, for the purpose of inducing the sale of franchises, memberships and credit card services, represent, and have represented, directly or by implication:

A. To prospective franchisees, that:

1. Franchisees selling memberships in respondents' program can expect to receive profitable earnings from the sale of two to five memberships per week, and can expect to remain active franchisees selling memberships for many years.

2. Respondents' program can be sold with ease to retail merchants.

3. Solicited prospective franchisees do not risk losing any expenditure of money in coming to Burlingame, California for an interview; and that respondents have authorized the reimbursement of the prospects' air fare expenses for such interviews.

4. Solicited prospective franchisees do not risk losing their deposits or downpayments submitted with applications for franchises; and that such deposits or downpayments are refundable if the applicants withdraw or otherwise do not consummate the franchise agreements.

5. Geographical areas offered to prospective franchisees have not been previously franchised; or that the areas offered have been franchised before and were profitable for the prior franchisees.

6. Respondents offer only a limited number of sales franchises to qualified individuals.

7. There is a "Regional Manager" of respondents who is interviewing other franchise applicants for the same area as each franchise prospect; and that the prospective franchisees must act immediately to be considered for a franchise.

8. Franchise holders receive substantial benefits from renewals of memberships, and from annual bonuses based on a percentage of net credit charges submitted by members in each franchisee's territory.

9. Franchise holders risk losing little or nothing in investing in a franchise; that respondents will repurchase the franchise and/or aid in its resale; and that the franchise is a vested property right which may be sold, assigned, transferred, or testated.

B. To both prospective franchisees and prospective members, that:

1. Respondents' program has received national acceptance.

2. There are thousands of members honoring all credit cards under respondents' program each and every month.

3. All credit charges submitted under respondents' program are guaranteed payable without recourse; that respondent's assume all risk of nonpayment by the members' customers; that members can expect to be successful and satisfied with the program's performance; and that members usually continue using respondents' program for two years and renew their contracts thereafter.

4. Articles used to solicit sales of franchises and memberships are unsolicited and impartial accounts about respondents' program.

5. Letters and payment checks used to attest to the success of respondents' program are representative, typical and current, and that such letters and checks reflect an unbiased evaluation.

6. Respondents' program costs members little or nothing at all; and that the program costs members half as much as trading stamps.

7. Members complete just one simple form for all credit charges; and that members receive payment for each credit charge submitted to respondents in 30 days.

8. Respondents are the largest credit card clearing house in America.

9. Respondents' program is approved or endorsed by the individual issuers of the credit cards accepted by respondents.

10. Respondents' authorized capitalization of $3,000,000 is liquid and available to provide financial resources and ability to service members.

11. Members are assured a minimum 10 percent increase in business within the first 12 months using respondents' program, and that in the event such increase does not materialize, membership dues will be waived for the second year.

12. Respondents are members in good standing of an independent organization by the name of the Fair Trade Bureau; and that the Better Business Bureau has written an uncensored, objective report on respondents' business.

C. To members, that:

1. Every credit charge submitted by members is subject to the most intensive collection procedure in the credit industry, consisting of billing, outside collection and legal action.

2. When a member becomes inactive and respondents determine his account is in arrears, respondents will institute legal action for the collection of such monies unless they are remitted by the member to respondents upon demand.

PAR. 6. In truth and in fact:

A. With respect to the representations directed to prospective franchisees:

1. Franchisees selling memberships in respondents' program have not received profitable earnings from the sale of two to five

memberships per week, and have not remained active franchisees selling memberships for many years. A substantial number of franchisees do not achieve either a return of their original investment or even one year longevity as franchisees actively pursuing sales efforts.

Further, respondents fail to disclose to prospective franchisees relevant information, which would assist such prospects in evaluating the probabilities of their success and chances of achieving longevity as franchisees, and which would lessen the potential for deception, including: the median and mean earnings from the sale of memberships by franchisees associated with respondents during the previous calendar or fiscal year; the median and mean length of time that said franchisees pursued membership sales efforts; the median and mean period of time that members associated with respondents' program during the previous calendar or fiscal year submitted payment vouchers for credit charges using respondents' program; the number of such members submitting said payment vouchers each month; the rate or degree of recoursing such credit charges back to members during the previous calendar or fiscal year; and, the full number and nature of reasons for which respondents recourse charges to members.

2. Respondents' program has not been and cannot be sold with ease to retail merchants.

3. Solicited prospective franchisees do risk losing the money they expend for air fare in coming to Burlingame, California for an interview. Respondents authorize the reimbursement of prospects' air fare expenses only upon the payment of the funds required to accompany applications.

4. Solicited prospective franchisees do risk losing their deposits or downpayments submitted with applications for franchises and such deposits or downpayments are not refundable if the applicants withdraw or otherwise do not consummate the franchise agreements.

5. In a substantial number of instances, the geographical areas offered to prospective franchisees have been previously franchised and were not profitable for the prior franchisees.

6. Respondents do not limit the number of sales franchises offered.

7. There is no "Regional Manager" of respondents who is interviewing other franchise applicants in each area, but rather all persons responding to respondents' invitation for inquiries receive

the same form letter stating that said "Regional Manager" is interviewing other interested persons for the same franchise area. In few, if any, instances need prospective franchisees act immediately to be considered for a franchise.

8. Franchise holders do not receive substantial benefits from renewals of memberships, or from annual bonuses based on a percentage of net credit charges submitted by members in each franchisee's territory.

9. Franchise holders do risk losing their investment. Respondents do not repurchase the franchise, and in those instances where respondents do aid in its resale, they retain at least half of the amount for which it is resold. The franchise is not a vested property right which may be sold, assigned, transferred or testated. If a franchise holder does not produce the sales quota set forth in his franchise agreement, the franchise may be terminated by respondents.

B. With respect to the representations directed to both prospective franchisees and prospective members:

1. Respondents' program has not received national acceptance.

2. There are not thousands of members honoring all credit cards under respondents' program each and every month.

3. Not all credit charges submitted under respondents' program are guaranteed payable without recourse. Respondents do not assume all risk of non-payment by the members' customers. A substantial number of members have been neither successful nor satisfied with the program's performance. A substantial number of members have not continued using respondents' program for even one year, and have not renewed their contracts after the expiration of two years.

Further, respondents fail to disclose to prospective members relevant information, which would assist such prospects in evaluating the probabilities of their success and chances of achieving longevity as members, and which would lessen the potential for their deception, including: the median and mean period of time that members associated with respondents' program during the previous calendar or fiscal year submitted payment vouchers for credit charges using the program; the number of such members submitting said payment vouchers each month; the rate or degree of recoursing credit charges back to members during the previous calendar or fiscal year; and, the full number and nature of reasons for which respondents recourse charges.

4. Articles used to solicit sales of franchises and memberships are not unsolicited and impartial accounts about respondents' program. Such accounts, for the most part, are prepared and placed by representatives of respondents.

5. In many instances, letters and payment checks used to attest to the success of respondents' program are unrepresentative and atypical, and are from franchisees and/or members who are no longer active with the program. Many of such letters and checks do not reflect an unbiased evaluation of respondents' program. Furthermore, respondents fail to disclose that many testimonial letters have been prepared by representatives of respondents and many are from persons who received remuneration or other beneficial consideration from respondents, so as to mislead and deceive prospective franchisees and members with respect thereto.

6. Respondents' program does not cost members little or nothing at all. The program does not cost members half as much as trading stamps. Taking into account the initial membership fee, the monthly dues, the discount rate, the total amount of charges recoursed, and the 6 percent discount fee paid even on recoursed charges, the program costs the members a substantial amount.

7. The forms which members must complete to process credit charges are not simple and are burdensome to fill out in practice. Members do not receive payment for each credit charge submitted to respondents in 30 days.

8. Respondents are not the largest credit card clearing house in America. There are other credit card operations with larger retail memberships and with larger amounts of financial resources than respondents' business.

9. Respondents' program has not been approved or endorsed by the individual issuers of the credit cards accepted by respondents.

10. Respondents' authorized capitalization of $3,000,000 is not liquid and available to provide financial resources and ability to service members. It is merely the amount selected by respondents as the sum on which the fee to be paid to the California Corporations Commissioner was determined. Further, respondents fail to disclose the relevant information that their net working capital is a deficit, so as to mislead and deceive prospective franchisees and prospective members with regard to respondents' financial condition.

11. In most instances, members have not realized a minimum 10 percent increase in business within the first 12 months using

respondents' program, and have not received a waiver of membership dues the second year.

12. Respondents are not members of an independent organization by the name of the Fair Trade Bureau. The Fair Trade Bureau is a division of respondents, having no members or function at present, other than its use as a reference in the materials disseminated by respondents. The Better Business Bureau report evaluating respondents' business is not an uncensored, objective document.

C. With respect to the representations directed to members:

1. Every credit charge submitted by members is not subject to the most intensive collection procedure in the credit industry, consisting of billing, outside collection and legal action. Respondents' collection efforts are not uniformly intensive, but are determined by the dollar amount of each individual charge. Respondents do not in practice institute legal action against delinquent customers. Further, respondents fail to disclose to members and to debtor-customers, at any time, that North American Collections, the agency to which delinquent accounts are turned over, is not an outside agency, but rather an affiliated division of respondents.

2. Respondents have not instituted legal action against inactive members whose accounts respondents have determined are in arrears.

Therefore, the statements and representations, as set forth in Paragraphs Four and Five hereof, were and are false, misleading and deceptive.

PAR. 7. Furthermore, it was and is an unfair practice and a false, misleading and deceptive act and practice for respondents to seek to sell their franchises, memberships and credit card services in the manner set forth in Paragraphs Four and Five hereof, while they knew or, as reasonably prudent businessmen, should have known, that their "Honor All Credit Card" program would not operate and produce results as represented.

Moreover, it was and is an unfair practice and a false, misleading and deceptive act and practice for respondents to seek to sell franchises in the manner aforesaid when respondents knew or, as reasonably prudent businessmen, should have known that the realization of profit by franchisees contemplates, and is necessarily predicated upon, the exploitation of member

retailers who must be induced to participate in respondents' program by misrepresentations.

At no time did respondents notify any persons who expended money in reliance upon respondents' statements and representations that their money would be refunded if respondents knew or, as reasonably prudent businessmen, should have known that respondents' program would not operate and produce results as represented, and if in fact such persons found in practice that the program did not operate and produce results as represented. Meanwhile, the operations and practices of respondents alleged herein were and are perpetuated for an indeterminate period of time with the monies obtained from such persons who expended sums in reliance upon respondents' statements and representations.

Therefore, the aforesaid failure of respondents to notify and refund to persons who acted in reliance upon said statements and representations set forth in Paragraphs Four and Five hereof, all monies expended by such persons, was and is inherently and unconscionably unfair and deceptive.

PAR. 8. In the course and conduct of their aforesaid business, and at all times mentioned herein, respondents International Credit Card Corporation, also trading as National Credit Service, has been, and respondents Universal Credit Acceptance Corporation, Continental Credit Card Corporation, Heater and Gingold have been, and now are, in substantial competition, in commerce, with corporations, firms and individuals in the sale of franchises or distributorships to persons interested in establishing their own businesses, and with corporations, firms and individuals in the sale of credit card services.

PAR. 9. The use by respondents of the aforesaid unfair acts and false, misleading and deceptive statements, representations and practices, has had and now has, the capacity and tendency to mislead members of the purchasing public into the erroneous and mistaken belief that said statements and representations were and are true and into investing substantial sums of money in becoming franchisees to sell respondents' services, and into investing substantial sums of money in becoming members of respondents' program for the use of respondents' services, and into the payment of substantial sums of money by reason of said erroneous and mistaken belief.

PAR. 10. The aforesaid acts and practices of respondents, including their failure to refund all monies expended by persons who

acted in reliance upon respondents' statements and representations, as herein alleged, were and are all to the prejudice and injury of the public and of respondents' competitors and constituted, and now constitute, unfair methods of competition in commerce and unfair and deceptive acts and practices in commerce in violation of Section 5 of the Federal Trade Commission Act.

Mr. Alfred Lindeman, William A. Arbitman, and *William T. Mitchell* supporting the complaint.

Young and Gush, San Mateo, Ca., by *Mr. Alfred L. Young,* counsel for respondents.

INITIAL DECISION

BY RAYMOND J. LYNCH, HEARING EXAMINER

FEBRUARY 29, 1972

PRELIMINARY STATEMENT

The complaint in this proceeding was issued on October 6, 1970, charging the corporate and individual respondents with violations of Section 5 of the Federal Trade Commission Act through the use of unfair or deceptive acts and practices and unfair methods of competition in commerce in the sale of "franchises" and "memberships" in their "Honor All Credit Card" program.

Respondents filed an answer to the complaint on December 17, 1970. A prehearing conference was held on February 10, 1971 in San Francisco, California, at which time the examiner set the matter for formal hearings on May 18, 1971. Subsequent thereto on April 19, 1971, counsel supporting the complaint filed a motion to amend the complaint which was denied by the Commission on July 21, 1971.

The matter finally came on for hearing before the undersigned examiner on November 2, 1971, and concluded on November 11, 1971. Pursuant to an order issued by the Commission granting the respondents an extension of time in which to file proposed findings, they were filed on January 17, 1972.

Respective counsel were afforded full opportunity to be heard, to examine and cross-examine all witnesses and to introduce such evidence as is provided for under Section 3.43(b) of the Commission's Rules of Practice for Adjudicative Proceedings. Proposed findings of fact and conclusions submitted and not adopted in substance or form as herein found and concluded are hereby rejected. After carefully reviewing the entire record in this proceeding and based on such record and the observation of the witnesses testify-

ing herein, the following Findings of Fact and Conclusions therefrom are made, and the following Order issued.

Nature of Respondents' Business and Business Methods

Respondents in this proceeding are promoting an "Honor All Credit Card" program. The primary basis of the program is the sale by respondents of franchises to individuals which permits them to act as salesmen for memberships in respondents' program. Member merchants can extend credit to holders of selected credit cards (including the cards issued by the major banks, oil companies and other issuers such as American Express, Diner's Club, and Carte Blanche) and send the charge tickets to respondents who bill the customer and remit payments to the merchant. Advertised and promoted as a nonrecourse program, *i.e.*, the merchant gets paid by respondents whether or not the latter collect, and one under which the merchant is guaranteed payment in 30 days, it has great surface appeal. It opens up a vast market of customers to whom merchants can ostensibly extend credit without risk of loss and without the administrative problems connected with handling accounts receivable. Furthermore, since respondents portray themselves as a large, well-respected financial institution ($3,000,000), any concern about their reliability and financial dependability is dispelled.

Beneath the surface of this program, however, lies something entirely different. After having paid, or obligated themselves to pay, a $240 membership fee, $240 in dues, and a 6 percent discount fee on all charges submitted, members soon discover that respondents avoid paying charges which they can't collect by citing one or more of *at least* 18 different reasons why they are not obligated to pay. Members also discover that, rather than receiving payment for charges within 30 days from the date they are submitted, payment is not received until anywhere from 45 to 75 days later. As a result of this treatment and despite the fact that they signed a two-year contract, member merchants give up in despair and, swallowing their losses, stop using the program after about seven to eight months on the average. Typically, in addition to having paid what is not an insignificant sum for a service that was never delivered, members have, in fact, risked and lost money for charges recoursed by respondents.

Since the program as administered has no merit and results in financial loss and aggravation to merchants, franchisees who

purchase the rights to sell it are also destined to fail and have failed miserably.

What the record establishes is that these respondents have perpetrated a scheme fraught with misrepresentations from which they try to insulate themselves by using devious contractual language, not intended or likely to be read and not clearly understandable, even if actually read. Respondents have cleverly calculated the program to enrich only themselves at the expense of innocent small businessmen lured into it as members and franchisees.

FINDINGS OF FACT

1. Respondent Universal Credit Acceptance Corporation is a corporation organized, existing, and doing business under and by virtue of the laws of the State of California,[1] with its principal office and place of business located at 218 California Drive, Burlingame, California (deemed admitted by respondents' Answer).

2. Respondent Continental Credit Card Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of California, with its principal office and place of business located at 218 California Drive,[2] Burlingame, California (deemed admitted by respondents' Answer; see also CX 6 A–D).

3. Respondent International Credit Card Corporation, also trading as National Credit Service, is a corporation organized, existing, and formerly doing business under and by virtue of the laws of the State of California,[3] with its principal office and place of business formerly located at 2305 South El Camino Real, San Mateo, California (deemed admitted by respondents' Answer; see also CX 1 A–L). Said corporation, though dormant, has never been dissolved (Heater, Tr. 765).

4. Respondent John Clifford Heater is an individual and an officer of Universal Credit Acceptance Corporation and International Credit Card Corporation. His business address is the same as the corporate respondent Universal Credit Acceptance Corporation. Respondent Howard P. Gingold is an individual and

[1] Universal Credit Acceptance Corporation has apparently also been incorporated in the State of Nevada on March 1, 1971 (Cerino, Tr. 680–682).

[2] Although the address used on letterheads by Continental Credit Card Corporation is 216 California Drive, Burlingame, California, there is ample evidence in the record to the effect that both 216 and 218 California Drive are in fact the same entrance to the same building (Fish, Tr. 172; MacDonald, Tr. 540).

[3] International Credit Card Corporation was apparently also incorporated in the State of Nevada (Heater, Tr. 763).

is an officer of Continental Credit Card Corporation, and his business address is the same as said corporate respondent (deemed admitted by respondents' Answer).

5. Respondents' "Honor All Credit Card" program entitles merchant members to sell their respective products and services to customers presenting any one of a large number of credit cards approved by respondents, and to submit such credit charges to respondents. Respondents collect the charges from customers of members and remit payment to the members (deemed admitted by respondents' Answer). Members are initially sold by home office membership salesmen or by franchisees. The membership contracts are between the retail merchant and Continental Credit Card Corporation (CX 136 A–B, CX 179 Z–88, CX 181 A–B, CX 218 A–B). There is then a paper transfer of the contracts to Universal Credit Acceptance Corporation (Fish, Tr. 84; Cerino, Tr. 692). Universal Credit Acceptance Corporation handles the collections from customers of members as well as all subsequent payments and dealings with the members themselves after the membership is sold (CX 45 H, CX 46 H).

6. Respondent Heater has been and is primarily responsible for establishing, supervising, directing and controlling the acts and practices of each of said corporate respondents. The "Honor All Credit Cards" program and concept was started by him in 1953 (CX 45 B–C). During the time period pertinent to this complaint, respondent Heater or his family held all issued stock and respondent Heater himself was the responsible official of all the respondent corporation.[4] He was an incorporator and director of International Credit Card Corporation (CX 1 A–L); he and his father were the only stockholders; and respondent Heater was its president (Heater, Tr. 764–65). Respondent Heater also hired and trained salesmen for National Credit Service and International Credit Card Corporation (Heater, Tr. 766). Respondent Heater has owned all of the outstanding stock of Universal Credit Acceptance Corporation throughout the period pertinent to this proceeding (Heater, Tr. 759).

7. Respondent Heater has been president and the controlling, directing and dominating influence of Universal Credit Acceptance Corporation throughout the period pertinent to this proceeding (CX 45 D–E). Respondent Heater is similarly the primary individual responsible for establishing, supervising, directing and

[4] The nominal president of Continental describes his title as "ceremonial" (Gingold, Tr. 703–04, 734).

controlling the acts and practices of Continential Credit Card Corporation during the period pertinent to this proceeding (Heater, Tr. 753, 771). Recent ex-employees identified him as the functioning, operating head of both Universal Credit Acceptance Corporation and Continental Credit Card Corporation (Fish, Tr. 78; O'Flaherty, Tr. 411–12; MacDonald, Tr. 541). Also, respondent Heater admitted his role in providing sales instructions to Continental Credit Card Corporation's franchise salesmen (Heater, Tr. 895). Although Heater has nominally stepped down as president of Universal Credit Acceptance Corporation as of June 1971, he, the new president, Lawrence Cerino, and the president of Continental Credit Card Corporation all acknowledge Heater's clear responsibility prior to June 1971 (Heater, Tr. 758–59; Cerino, Tr. 683–84; Gingold, Tr. 704).

8. Respondent Gingold, in addition to his functions as president of respondent Continental Credit Card Corporation, also acts and has acted as a salesman of franchises for said corporation (deemed admitted by respondents' Answer; Gingold, Tr. 703). In addition, respondent Gingold is in part personally responsible for many of the advertising claims that are the subject of the instant complaint (Gingold, Tr. 705–06; O'Flaherty, Tr. 478), although the approval of the copy for same came from John Heater (Gingold, Tr. 707).

9. United Credit Card Corporation, although not named as a respondent in this proceeding, was incorporated in both the State of California and Nevada in February and March of 1971 (CX 7 A–C, CX 8 E).

A representative of the State of California Corporations Commissioner's Office appeared as a witness and testified that in March of 1971, an application was filed under the California Franchise Investment Law in behalf of United Credit Card Corporation, a California corporation, intending to operate an "Honor All Credit Cards" business. Under the applicable procedures, information was received regarding the address, officers and salesmen of United Credit Card Corporation, as well as samples of the franchise agreements and advertising to be used. This information indicates that United Credit Card Corporation was to operate at the *identical address* as the respondents herein, and that while the officers were to be different than the named officers of the corporate respondents during the time period pertinent to this complaint, the *franchise salesmen* included John Kadwell and Howard Gingold, both of whose participation in the operation of the corporate respondents is fully documented in the record

(Davidson, Tr. 290–94; Winstead, Tr. 360–62; Tronca, Tr. 663–66). The *shareholders* to whom stock is to be issued in United Credit Card Corporation include Mae Heater, the wife of respondent John Heater. The *franchise agreements* to be used by United Credit Card Corporation are identical in every respect, except for the corporate name, to those of the respondents, and the direct mail *advertisements* to be used by United Credit Card Corporation are similarly identical to those of the respondents (Olcomendy, Tr. 902–04; CX 20 A–B, CX 21 A–B, CX 22, CX 127, CX 128, CX 129 A–B, CX 237–39).

United Credit Card Corporation was formed after the complaint was filed in this proceeding.

10. Despite many name changes occurring since the inception of the "Honor All Credit Cards" program, the operation has remained essentially a continuation of the concept begun by respondent Heater in 1953. It was operated under the name National Credit Service from 1953 until 1959, when International Credit Card Corporation was formed (CX 1 A–L); the operation thereafter was conducted under the name National Credit Service, a division of International Credit Card Corporation (Heater, Tr. 764–65). International Credit Card Corporation sold memberships in the "Honor All Credit Cards" program throughout the United States and Canada, employing from 10 to 20 salesmen (Heater, Tr. 766–67). Universal Credit Acceptance Corporation was incorporated in 1964 (CX 5 A–F) and Continental Credit Card Corporation in 1965 (CX 6 A–D). Whereas previously memberships in the program were sold only by company salesmen, in 1963 respondent Heater began to sell franchises to individuals who would in turn sell memberships in the program to merchants in their respective areas (Heater, Tr. 767). Eventually, Continental Credit Card Corporation took over the function of the sale of franchises and memberships from International Credit Card Corporation, operating as a "sales affiliate" of Universal Credit Acceptance Corporation (Heater, Tr. 770–71). Respondent Heater admitted that International Credit Card Corporation was "essentially the same business of (sic) Continental Credit Card Corporation" (Heater, Tr. 765).

11. For all intents and purposes Universal Credit Acceptance Corporation and Continental Credit Card Corporation constitute one operation.

Raleigh Fish, who was respondents' director of member rela-

tions for 18 months from August 28, 1969 to February 20, 1971, testified that:

> Contipental Credit Card Corporation is the sales arm of Universal Credit Acceptance Corporation. They sell the document and make whatever other initial contacts are made to the prospective member merchants. Upon receiving a signature on the document, it is forwarded to the offices which in this case happen to be the same, and it is then accepted by Universal Credit Acceptance Corporation, which, I guess, is the signee (Fish, Tr. 84).

Joseph N. O'Flaherty who was sales promotion manager and head of the franchise relations department, employed by respondents from February 1969 until August 1971, testified as follows:

> A. I worked for Continental Credit Card Corporation, and Universal Credit Acceptance Corporation.
> Q. You worked for both corporations?
> A. Technically, yes.
> Q. What do you mean by technically?
>
> * * * * * * *
>
> THE WITNESS: I was paid, actually by Universal Credit Acceptance Corporation, however, I worked with franchisees, which was Continental Credit Card Corporation. So, since there was no definitive separation, I actually worked for both companies. I suppose one could argue it, as to which one I was working for, I really don't know. I was paid by Universal, I worked for Continental (O'Flaherty, Tr. 411–12).

Brian MacDonald, who was technically employed by Universal Credit Acceptance Corporation, testified that he had daily contact with people who worked for Continental Credit Card Corporation, namely the franchise sales force; and although Universal and Continental did not have the same street address, in reality both addresses were actually the same entrance to the same building, in which there were no separate offices designated for Universal and Continental (MacDonald, Tr. 539–40).

12. Respondent John Clifford Heater made a disingenuous effort to remove himself from his position of responsibility as of March 1971.

On March 1, 1971, Lawrence Cerino was made president of Universal Credit Acceptance Corporation (Cerino, Tr. 677, 680). Although Cerino was also named president of United Credit Card Corporation, it is apparent that respondent Heater is still in a sub rosa position of control and responsibility (Olcomendy, Tr. 902–03). The agent for service of process for the corporation in Nevada is his wife, Mae Heater (CX 8 B), and she is to be a stockholder of the California corporation using joint funds for

this investment (Olcomendy, Tr. 903–04; Heater, Tr. 785). In any event, respondent Heater acknowledged that he gave approval for having the new corporation organized (Heater, Tr. 783), and he was knowledgeable about the current operations at the time of the hearing (Heater, Tr. 798).

Respondent Heater is still in control of the corporate respondents. When Mr. O'Flaherty left the company, respondent Heater remained active in the day-to-day operations of the company without having diminished his activities in any respect, even though the presidency of Universal had been transferred to Lawrence Cerino (O'Flaherty, Tr. 444). Heater is paid a higher salary than Cerino (Cerino, Tr. 688), who does not even know who owns the stock in Universal (Cerino, Tr. 687), or in fact whether he is president of the California or the Nevada corporations (Cerino, Tr. 680–83).

13. Respondent International Credit Card Corporation, also trading as National Credit Service, was, and respondents Universal Credit Acceptance Corporation, Continental Credit Card Corporation, John Clifford Heater, and Howard P. Gingold were, and are now, engaged in the advertising and offering for sale and sale of franchises which authorize the franchisees to sell retail merchants memberships in respondents' "Honor All Credit Cards" program (hereinafter referred to as respondents' program), for the use of respondents' credit card services, and in the advertising and offering for sale, and sale of such services to retail merchants (deemed admitted by respondents' Answer).

14. Respondents sell franchises to persons who invest a substantial sum of money as a condition to being granted exclusive rights to sell memberships in respondents' program.

An investigation of respondents' records resulted in a tabulation of all franchises sold by Continental Credit Card Corporation from January 1, 1967 to October 1969 (CX 190 A–Q). Said exhibit discloses that 172 franchises were sold and the total amount actually paid or invested for such franchises was $1,291,703.90 or an average of $7,509.91 per franchise. Respondents' consolidated income statements for the years ending June 1969, 1968 and 1967 reflect income from "franchise rights" in the amounts of $475,632, $570,552, and $149,286 respectively (CXs 122–124).

15. Directly and through franchisees, respondents sell their credit card clearing services to retail merchants (hereinafter referred to as members) (deemed admitted by respondents' Answer).

16. Retail merchants purchasing respondents' program invest substantial sums of money as fees, dues and service discounts on credit sales (CXs 122–124):

	Year Ended June 30, 1969	Year Ended June 30, 1968	Year Ended June 30, 1967
Member Fees	$257,633	$353,028	$226,509
Member Dues	301,900	235,976	131,190
Discounts	135,693	105,371	99,485
Totals	$695,226	$694,375	$457,184

17. Respondents' total annual volume of business for the years ended June 30, 1969 and June 30, 1968, was in excess of $1.25 million (CXs 122–23).

18. In the course and conduct of their business as aforesaid, respondent International Credit Card Corporation, also trading as National Credit Service, has caused, and respondents Universal Credit Acceptance Corporation, Continental Credit Card Corporation, Heater and Gingold were, and are now, causing their advertising matter to be published in newspapers of interstate circulation and their promotional materials to be mailed or otherwise conveyed to various persons residing outside the State of California, in each and every State of the United States and in foreign countries (CXs 23–44). Advertising matter, applications, contracts, franchise agreements, letters, checks and other communications have been sent and have been received between the respondents at their places of business located in California, and persons in various other States of the United States and in foreign countries (deemed admitted by respondents' Answer; see also Krieger, Tr. 179–81; Davidson, Tr. 252–53, 255; Winstead, Tr. 328; Clay, Tr. 564–65; Lynema, Tr. 589–90).

The franchises sold by respondents and the members sold by said franchisees (members actually contract with respondents) are located throughout the United States and Canada, the vast majority of which are located outside the State of California (CX 190 A–Q; see also CX 193 A–E, CX 194 A–E).

19. As a result of said interstate advertising and promotion and as a result of said transmission and receipt of said written instruments and communications, respondents have maintained a substantial course of trade in said franchises and credit card services in commerce, as "commerce" is defined in the Federal Trade Commission Act.

20. In the course and conduct of their business, respondents now engage in, and/or have engaged in, a continuing program of recruiting franchisees to sell respondents' services and of selling memberships in respondents' program (CX 45 B, CX 46 B).

21. Respondents solicit the sale of their franchises in the following manner and by the following means. Respondents publish, or cause to be published, in magazines and newspapers of regional and national circulation and disseminate through the mails advertisements inviting inquiries from persons interested in becoming franchisees (CXs 24–27, CX 43, CX 44; MacDonald Tr. 541–46, 549). To persons who respond to such invitations, respondents send through the mail advertising and promotional material containing many statements and representations regarding respondents' services and the financial and other benefits to be enjoyed by persons who become franchisees of respondents (CX 45, CX 46, CXs 47–59). Persons who express further interest receive a telephone sales presentation by one of respondents' sales representatives and, in most instances, are invited to visit respondents' place of business, now in Burlingame, California (Gingold, Tr. 715–718, 723–728; see also Davidson, Tr. 252–53, 255; Winstead, Tr. 328–335; Krieger, Tr. 179–81; Clay, Tr. 564–65; Lynema, Tr. 589–90; England, CX 234 at pp. 2–3; McKinnon, CX 234 at pp. 3–4; Smith, CX 234 at p. 5; Hawkins, CX 234 at p. 6).

22. Respondents also disseminate said advertisements, statements and representations through existing franchisees for the purpose of soliciting the sale of subfranchises, new franchises, and the resale of franchises. Respondents have a policy of attempting to elicit sales of additional franchises and subfranchises through their existing franchisees (Lynema, Tr. 617–21; Heater, Tr. 883–85).

23. Typical and illustrative of said representations and statement to prospective franchisees appearing in advertising and promotional material, but not all inclusive thereof, are the following:

FULL OR PART TIME BUSINESS

You can have a SECURE FUTURE as a business partner with America's leading credit organization. Our unique service allows retail business firms to honor over 200 million credit cards now in use, including most major oil company cards * * * with guaranteed payment from us.

Opportunity for EXCEPTIONALLY HIGH EARNINGS. $10,000 investment required. Partial financing considered. Renewals and bonuses insure

permanent security and income. No age limit. For personal interview, write Universal Credit Acceptance Corp., Box 593, Burlingame, California 94010. WRITE TODAY, while your area is still available.

DID YOU NOTICE THIS AD IN THE BUSINESS OPPORTUNITIES SECTION OF YOUR NEWSPAPER?

ARE YOU LOOKING—for a profitable addition to your present income or business? Why not diversify with a non-competitive service that offers immediate profits and a virtually unlimited opportunity for future business expansion.

NOW—YOU CAN OBTAIN THE SALES RIGHTS for the "HONOR ALL CREDIT CARDS" program in your area. Through our program, any merchant, large or small, can make instant credit sales to more than 100 million credit card customers * * * with guaranteed payment. It is the most appealing business and sales promotion program on the market today!

FIND OUT FOR YOURSELF! Ask any merchant if he would like to be able to accept the 3 leading all-purpose credit cards plus those issued by over 50 different oil companies—over 100 million potential customers—without risking his own money.

YOUR PROFITS ARE IMMEDIATE—THEY ARE SUBSTANTIAL—THEY ARE CONTINUOUS! This is the opportunity you've been waiting for * * * the chance to own a secure, profitable full or part-time business. Complete details can be yours at once. Simply fill out the attached card and MAIL TODAY (CX 24 A–B; CX 25 A–B; CX 26 A–B; CX 46 A–L).

24. Respondents solicit the sale of their credit card services to members in the following manner and by the following means. Respondents disseminate through the mails to retail merchants advertisements and promotional material containing many statements and representations regarding respondents' services and the financial benefits to be enjoyed by persons who become members (CXs 28–41). Leads resulting from responses to said mailings are forwarded to respondents' franchise holders who also make such statements and respresentations directly with the aid of sales kits, and other material supplied to them by respondents (CX 45 I, CX 16 A, CX 17 A, CX 18 A, and CX 179 A–Z88).

25. Typical and illustrative of said representations and statements to prospective members, but not all inclusive thereof, is the following:

UNIVERSAL CREDIT ACCEPTANCE CORP., the nation's largest credit card clearing house, is your answer to increased business. You fill out just ONE simple form for any credit sale. You receive ONE BIG CHECK for all credit sales every month. It's fast! It's easy! It's PROFITABLE! Pay-

ment is guaranteed, non-resource (CX 38 B, copyright 1965; CX 39 B, copyright 1969).

26. By and through the above-quoted statements and representations, and others similar thereto but not expressly set out herein, and in the course of oral sales presentations, respondents, their agents, representatives and employees, for the purpose of inducing the sale of franchises, memberships and credit card services, represent, and have represented, directly or by implication to prospective franchisees, that franchisees selling memberships in respondents' program can expect to receive profitable earnings (from the sale of two to five memberships per week), and can expect to remain active franchisees selling memberships for many years.

The earnings projection sheets used by respondents (CXs 47–59) project income on a year-by-year basis over a four-year period based upon from two to five membership sales per week, showing total annual earnings mushrooming upward. These sheets also claim in footnotes that "changes of ownership among member firms and new businesses starting, as well as other economic factors, make market saturation impossible into the indefinite future."

The advertisements employed by respondents refer to such things as a "secure future," "exceptionally high earnings," "renewals and bonuses insure permanent security and income," "profitable addition to your present income or business" (on a full or part-time basis), "immediate profits," "your profits are immediate—they are substantial—they are continuous!," "secure, profitable full or part-time business" (CX 24 A and CX 25 A); "expand your present earnings," "guarantee your future," "your profits are immediate * * * they are substantial * * * and they are continous * * * on a full or part-time basis," "a highly profitable business" (CX 26 A–B); and "financial success," "opportunity," "secure future" (CX 27 A).

The "Franchise Proposal" of respondents refers to "a franchise opportunity without parallel!," "immediate income," "residual earnings," "participation in credit sales volume," "insure immediate success," "unlimited opportunity to expand the scope of his sales activities and income," "security with a promising future," "you can expect immediate and continuing success," "no experience necessary," "you can become successful * * * on a full or part-time basis," "virtually insure an exceptional income

for you," "vested renewal will create an evergrowing fund of residual profit for you" (CX 45 A–L, CX 46 A–L).

In addition to the written representations enumerated above, numerous witnesses testified as to the specific earnings representations made to them. Arnold Krieger was told that there was a "great deal" of money to be made from his franchise, in the neighborhood of $50,000 to $75,000 a year (Krieger, Tr. 181), that there was no failure rate among existing franchisees (Krieger, Tr. 182–83), and that there was no risk involved in his investing in a franchise, since his franchise was worth an estimated $25,000 (Krieger, Tr. 191). Respondent Howard Gingold told Clayton Davidson that his present $12,000 to $15,000 salary as a manager of a Stuckeys store in Las Vegas would be "peanuts" (Davidson, Tr. 299–300).

An ex-employee who had worked for respondents in franchising processing and control testified that he frequently witnessed respondent Gingold making telephone presentations to franchise prospects in which he would mention that there were franchisees earning up to and including $80,000 per year (MacDonald, Tr. 548). The earnings claims attributed to Gingold by Davidson and MacDonald were not denied by Gingold at the hearing.

Harold Jerome Winstead was told that "eight out of nine franchisees got rich" and that within five years as a franchisee he would be a millionnaire, even working on a part-time basis (Winstead, Tr. 330-32). Richard Colfels testified that the sales pitch he received led him to think he could generate the same income he had been earning at General Motors, namely $30,000 a year (Colfels, Tr. 507–08, 511). Joe Clay, who in fact failed to consummate a franchise agreement, testified that the sales presentation given to him indicated that he could make a "ton of money" as a franchisee (Clay, Tr. 566–67). Leonard Lynema was convinced by the earnings projection sheets indicating the amount he could make as a master franchisee based on five sales per week, *i.e.*, $32,130 to $48,295 a year (Lynema, Tr. 604; CX 47).

Neil G. Labrum, who was sold an International Credit Card Corporation franchise, was told that he could earn $1,200 per month (CX 234, at pp. 1–2). Mahlon J. England received the earnings projection sheets (CXs 47–59) as well as representations that he could expect to earn at least $20,000 a year and that there was no limit to what he could earn as a franchisee (CX 234, at p. 2). Roy S. McKinnon received a document entitled "An Opportunity Without Parallel" (CX 188 A–B), the predecessor to

the "Franchise Proposal" brochure (CX 45 A–L), and earnings projection sheets, as well as representations that he could earn $25,000 per year, even on a part-time basis (CX 234, at pp. 3–4). Mark Smith received the "Franchise Proposal" (CX 45 A–L), the earnings projection sheets (CXs 47–59) and oral representations that he could reasonably expect to earn from $14,000 to $28,000 per year operating a franchise on a part-time basis (CX 234, at p. 5). Sam A. Hawkins was sold a franchise on the basis of the "Franchise Proposal" (CX 45 A–L), and the oral representations of the large amounts of money he could expect to make operating a franchise even on a part-time basis (CX 234, at p. 6). Albert G. Peek, after responding to an advertisement of respondents in the March 1966 TV Guide, was sold by a representative of respondents who used earnings projection sheets and verbally represented that Peek would "make a million" (CX 234, at p. 6).

27. In truth and in fact, franchisees selling memberships in respondents' program have not received profitable earnings from the sale of two to five memberships per week, and have not remained active franchisees selling memberships for many years. The overwhelming majority of franchisees do not achieve either a return of their original investment or even one year longevity as franchisees actively pursuing sales efforts.

The substantial lack of earnings and of longevity of franchisees is clearly demonstrated from the tabulation of all franchises sold by Continental Credit Card Corporation from January 1, 1967 to October 1969 (CX 190 A–Q). This evidence demonstrates that only 5 out of 172 franchisees earned even a return of their initial investment. That is, 97 percent failed to earn back their initial investment; 100 percent failed to earn the amounts projected in respondents' earnings projection sheets (CXs 47–59). The following is a summary of the results of the 172 franchises [5] referred to:

Total franchise fees	$1,893,879.70
Average franchise fee	11,010.93
Total amounts paid	1,291,703.90
Average amount paid	7,509.91
Total earnings	249,211.66

[5] It is noted that some of the 172 franchises actually operated under more than one franchise contract. The tabulation shows that the 172 franchises actually operated under a total of 206 franchise contracts.

Average earnings	1,448.91
Average percentage of investment lost	81%
Average elapsed time from agreement date to date of last earnings statement [6]	8.61 months

An examination of the number of the foregoing franchisees whose total earnings from selling memberships fell into various categories also reveals a clear pattern of failure:

Earnings	*Number of Franchisees Who Attained Such Earnings*
$0 to $999	103
$1,000 to $4,999	60
$5,000 to $9,999	6
$10,000 to $19,999	2
$20,000 or more	1
	172

It is noted that these earnings were not even necessarily attained in one year. For instance, the *one* franchisee who earned $20,099.80 took 23 months to do so (CX 190 A, #2), and the *two* franchisees who earned between $10,000 and $20,000 needed 43 months and 21 months, respectively, to do so (CX 190 D, #47; CX 190 E, #59).

CX 190 (A–Q) demonstrates the length of time franchisees actually operated their franchisees compared to the various periods of time used by respondents in their earnings projection sheets (CXs 47–59):

Number of franchise operations with longevity of one, two, three, and four years

0 to 12 months	140
13 to 24 months	27
25 to 36 months	3
37 to 48 months	2
	172

By definition, CX 190 A–Q is limited to the period January 1, 1967 through December 31, 1970, which would therefore only

[6] Elapsed time was measured by rounding off to the nearest whole month.

allow for a maximum longevity of four years. However, respondents' "flow chart" of all franchisees active as of October 1969 shows that there was absolutely no franchisee whose franchise predated January 1, 1967 (CX 189 A–C).

Most franchisees were able to sell very few memberships and some couldn't or didn't sell any (CX 190 A–Q).[7] With respect to the franchisees who were at first able to sell any significant number of memberships, it was not long before the fruits of their labors came back to haunt them. For instance, Harold Jerome Winstead testified that only four of the 64 memberships he sold were still active when he checked back with them at a later date; their use of the program averaged about 3 to 6 months, and their average loss was $400 to $500 (Winstead, Tr. 354–55). After buying his franchise upon the representation he would be a rich man in five years, he poignantly summarized his nine months' experience as follows:

Q. Why did you stop trying to sell the program?

A. * * * I guess the main one was I had a wife and three kids I was trying to feed and I went broke. * * * (Winstead, Tr. 355).

* * * * * * *

Q. What do you figure your participation in this whole franchise cost you personally?

A. It cost me a life's savings and about 35 years' work. I lost two businesses. I had one of them paid for and the other one partly paid for. I had 10 years paid on my home at 4½ per cent interest. I lost both of those businesses, I lost my home. I sold it for what I had in it with no profit. I sold the station at a losss to make a fast turnover because it looked like I had a real deal here. I put everything I had in one basket and that basket just didn't go (Winstead, Tr. 363).

Arnold Krieger testified that after selling ten memberships, the complaints he received from members caused him to quit the program (Krieger, Tr. 200, 206–08). Richard Colfels testified that after giving up his $30,000 a year job he had with General Motors, he sold about 30 to 40 memberships, but the aggravation and complaints he and his wife received from these members, including one murder threat, not only made him give up the project but also caused him a severe medical problem (Colfels, Tr. 518, 520–21, 522).

Clayton Davidson testified that after giving up a job as a manager of a local store and selling 32 or 33 memberships, the

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[7] The normal commission to a master territory franchisee for the sale of each membership is $108.00.

resulting feedback, problems and dissatisfaction of members caused him to lose his investment (he earned between $2,300 and $2,500 after investing $6,000; (Davidson, Tr. 296, 300). Furthermore, the experience literally forced Davidson to move out of Las Vegas, where his reputation had been so injured that he was unable to find work (Davidson, Tr. 290, 297, 307–08, 316). As he summarized it:

Q. How long a period of time were you making these sales over?

A. I was afraid to go out after the first of March.

Q. So you started in October. Why were you afraid to go out after the first of March?

A. You take people in business like in Vegas particularly, it's a nasty place to live if people don't like you.

Q. Did you fear for your life, sir?

A. Certainly, I'm cheating people, I'm dead in Vegas. I can't get a job in Vegas because they know I'm a crook.

Q. Did you cheat them or were you aware?

A. No, I didn't cheat them, I had nothing to do with the collection or recourses of this.

Q. Am I to understand that they felt you were cheating them?

A. Certainly, I'm the one that they blame, not the company that guaranteed they collect their money.

Q. How long have you known these people that some of them you began to fear?

A. Some of them seven, eight year business associates.

Q. Did you sell the program the way you had been taught in the seminar?

A. I sure did, that's the way I believed in it.

Q. Did you deviate in any way?

A. No (Davidson, Tr. 287–88).

Neil G. Labrum was a franchisee for International Credit Card Corporation, whose testimony includes the following:

I and my members had unfavorable experiences with International (see CX 176). I experienced considerable trouble and embarrassment caused me by my association with International, including financial injury and adverse reflection on my honesty and integrity in the community (CX 234, at p. 2).

Roy S. McKinnon's testimony was that:

My subsequent operation of my franchise was unsuccessful and I experienced adverse effects to my business reputation in the community resulting from my association with respondents (CX 234, at p. 4).

Leonard Lynema sold out an interest in an insurance agency in order to invest over $24,000 with respondents, for which he

received about $2,800 in earnings; and after he was used by respondents to bring them $50,000 from selling territorial franchises to others, respondents failed to pay him his commissions (CX 190 N; Lynema, Tr. 626, 629, 648). Albert Peek invested $15,000 for two franchises and lost his retirement income as a result of his association with respondents (CX 234, at p. 6).

The results indicated in CX 190 A–Q were not atypical as compared with other time periods. Joseph O'Flaherty, who was head of respondents' franchise relations department until the middle of 1971, testified that only 5 or 6 out of a total of 49 to 55 franchisees at any given time were ever actually producing sales of memberships (O'Flaherty, Tr. 418). He testified further that a study he had conducted in March of 1970 covering the sales activity of franchisees for the prior 3 years showed that the average franchisee made a total of 5 membership sales a year; and that the overwhelming majority of franchisees lose their money (O'Flaherty, Tr. 419–20, 421). Brian MacDonald, who worked for respondents in "franchise processing and control," testified that there were many franchise areas that were turned over and over (MacDonald, Tr. 552), which would tend to indicate a repeated incidence of failure to achieve satisfactory earnings.

Finally, in this regard, respondent Heater was able to identify only four "successful" franchisees (Heater, Tr. 860). The earnings from the sale of memberships by three[8] of those he identified is as follows:

Schwelling	—$ 5,642.68	(CX 190 F)
Soli	—$ 2,217.75	(CX 190 D)
Rothwell	—$13,221.86	(CX 190 D)

It is noted that Schwelling, the *only* franchisee cited by respondent Heater as making $30,000 a year made most of it from selling franchises, not memberships (Heater, Tr. 861–62). It must be emphasized that respondents' earnings projection sheets (CXs 47–59) and the oral earnings representations discussed, are based exclusively upon earnings from the sale of memberships. Yet, respondent Heater acknowledged that his criterion for "success" was earnings from $10,000 to $30,000; and that the individuals

[8] The record does not indicate the earnings of the fourth franchisee, John Kadwell. He purchased his franchise from another franchisee rather than from Continental Credit Card Corporation. Nevertheless, his business ethics, or lack thereof, is clearly established from the testimony of witnesses (Tronca, Tr. 663–64, 665–66; Davidson, Tr. 290–94; and Winstead, Tr. 360–62).

cited received earnings from the sale of subfranchises in addition to earnings from membership sales (Heater, Tr. 860, 862).

Respondents' Failure To Disclose Relevant Information

28. Further, respondents fail to disclose to prospective franchisees relevant information, which would assist such prospects in evaluating the probabilities of their success and chances of achieving longevity as franchisees, and which would lessen the potential for deception, including: the median and mean earnings from the sale of memberships by franchisees associated with respondents during the previous calendar or fiscal year; the median and mean length of time that said franchisees pursued membership sales efforts; the median and mean period of time that members associated with respondents' program during the previous calendar or fiscal year submitted payment vouchers for credit charges using respondents' program; the number of such members submitting said payment vouchers each month; the rate or degree of recoursing such credit charges back to members during the previous calendar or fiscal year; and the full number and nature of reasons for which respondents recourse charges to members.

It is clear from the record that none of respondents' sales presentations to prospective franchisees make the foregoing disclosures. To the contrary, it is evident that the sales materials contain the capacity to deceive prospects into believing that there are great probabilities of success as franchisees based on the earnings from the sale of memberships, and that the members sold would be satisfied, successful, and long-lasting in respondents' "non-recourse" program. Moreover, respondent Gingold, who operates mainly as a franchise salesman, testified as to the materials he and the other franchise salesmen use. His testimony indicated that the disclosures referred to herein were not made (Gingold, Tr. 705, 741–43).

29. Respondents represented that their program could be sold with ease to retail merchants but the record is clear that this representation was false. Sam A. Hawkins was told by a franchise salesman that "memberships were easy to sell" (CX 234, at p. 6); Mahlon England was told the program "would sell itself" (CX 234, at p. 3); and Arnold Krieger was told "the only thing you had to do was make your calls and see people * * * that the demand was fantastic * * *" (Krieger, Tr. 182).

In this regard, respondent Heater's testimony is as follows:

Q. As far as Continental is concerned, are any representations made to franchisees that the program can be sold with ease to merchants?

A. It is explained to them if they learned their sales presentation, if they present it properly to the merchant, if they manage their time effectively and if they make sure when they get through with the presentation that the merchant understands the value of the program, the merchant should buy the program, therefore, it should be sold with ease if you know how to present it properly * * * (Heater, Tr. 798–99).

30. In truth and in fact, respondents' program has not been and cannot be sold with ease to retail merchants.

This fact is not only the natural inference to be drawn from the abundant evidence of the failure rate and lack of success of franchisees, but there is also ample direct testimony in the record to this effect. Arnold Krieger testified that he encountered great sales resistance from prospective members who compared respondents' program unfavorably with bank credit card programs, which did not cost as much and which did not have any limit on the amount which could be charged on a nonrecourse basis (Krieger, Tr. 199–200). Harold Winstead testified that despite working long, hard hours, the program was very difficult to sell, again because prospective members felt it cost too much, and because it compared unfavorably with the credit card programs of BankAmericard and Master Charge (Winstead, Tr. 352–53). Leonard Lynemia referred to the saleability of the program by stating:

* * * it was impossible to sell the program once you got on the road with it because people told us this program had been tried before, and the merchants had been solicited for this kind of thing before and had horrible experience with it and warnings from newspapers on what it was, that these things had not paid them the charges * * * (Lynema, Tr. 629A).

As a result, the 23 salesmen that he had working for him at one time or another were only able to sell a total of about 20 memberships (Lynema, Tr. 619, 631). The testimony of Sam A. Hawkins indicates that he and his sales organization in New York City had great difficulty in selling the program (CX 234, at p. 6).

31. Respondents' representation that solicited prospective franchisees do not risk losing any expenditure of money in coming to Burlingame, California, for an interview and that respondents have authorized the reimbursement of the prospects' air fare expenses for such interviews is false.

This representation results from the combined use of a "Personal History Statement and Qualification Form" (CX 60, CX 62 A–B), a series of form telegrams and letters used by respondents to invite interested prospects for a home office interview in Burlingame, California (CX 80, CXs 92–109), and oral representations made by the franchise salesmen. Of the two versions of the personal history statement referred to, one, bearing a copyright date of 1965, has no statement on the reverse side whatsoever (CX 60), while the other, bearing a 1967 copyright date, has a paragraph on the reverse side describing the interview procedure, without any disclosure that a deposit of any kind must accompany a "bona fide franchise application" in order to qualify for reimbursement of air fare (CX 62 B). The letters and telegrams referred to contain statements that upon receiving a completed personal history statement from the prospect, an attempt will be made to get authorization for an interview "at our expense," or, after receiving the completed personal history statement from the prospect, the franchise salesman states that he has "received authorization from the franchise committee to reimburse your air fare for home office interview upon your submitting a franchise application, whether or not you are selected."

In July 1966, after Mr. Roy S. McKinnon received a telegram (CX 168) inviting him to telephone a franchise salesman of respondents, he was invited for an interview at Continental's expense (his air fare and expenses would be reimbursed) even should he decide not to submit an application for a franchise. Mr. McKinnon did not know before leaving Tacoma, Washington, that a substantial amount was required as a deposit to accompany an application in order to get reimbursement and he would not have come for the interview if the foregoing had been disclosed (CX 234, at pp. 3–4). Mr. Mahlon J. England was invited to come for an interview from Idaho in September 1966 upon the understanding his air fare and expenses would be reimbursed, even if after the interview he were to decide not to submit an application for a franchise. He was not told before he left Idaho to go to Burlingame that a $1,000 deposit was required to accompany his application. He would not have come for the interview had he known this beforehand (CX 234, at pp. 2–3).

In July or August of 1968, Mr. Sam A. Hawkins was promised by Continental's franchise sales manager that the company would

pay his expenses in flying to Burlingame from New York City for an interview even if he didn't commit himself to the proposition (CX 234, at p. 6). Mr. Joe Clay testified as follows, relating the proposition made to him by a franchise salesman of Continental in June 1969:

Q. What was the full nature of your call?
A. Yes, to come out and look at the program to see what they had to offer me. He said I could make a lot of money, make a ton of money. I think that was his words; and if I didn't like the program, they would still pay my ticket back and forth and pay my hotel room and what have you, so I agreed to that (Clay, Tr. 566).

This promise was the overriding consideration in getting Mr. Clay to Burlingame, because notwithstanding a telegram confirming that reimbursement would be made "upon your submitting a franchise application whether or not you are selected" (CX 108), and notwithstanding the fact that Mr. Clay had even been directed to bring $1,000 with him, he was reassured he was not risking anything if he didn't like the program (Clay, Tr. 568).

Since Messrs. England, McKinnon, Hawkins and Clay did ultimately submit franchise applications, according to company policy they were entitled to receive air fare "reimbursement," either by deducting the amount from their deposit or by actual refund. Clearly, the payment of such reimbursement does not cure the deception of having lured those who would not have come for the interviews had they known about the deposit requirement in advance. Moreover, there is evidence that other prospects were not so fortunate. They truly expected they would receive reimbursement whether or not they submitted franchise applications, when such was not the case (MacDonald, Tr. 550).

32. In truth and in fact, solicited prospective franchisees do risk losing the money they expend for air fare in coming to Burlingame, California, for an interview. Respondents authorize the reimbursement of prospects' air fare expenses only upon the payment of the funds required to accompany applications (admitted by respondents' Answer, p. 3).

33. Respondents' representations that solicited prospective franchisees do not risk losing their deposits or downpayments submitted with applications for franchises and that such deposits or downpayments are refundable if the applicants withdraw or otherwise do not consummate the franchise agreement are false.

In addition to oral representations to this effect (Davidson, Tr.

257; Clay, Tr. 569), the two relevant documents placed before prospects at the time of the interview have the capacity to deceive with regard to the refundability of deposits, especially if the prospects are only given an opportunity to review the documents in cursory fashion. That such is the case is established from the evidence that there is a high-pressure approach applied by the franchise salesmen,[9] who are paid on a commission basis (Gingold, Tr. 704).

Respondents' Franchise Application (CX 19 and CX 174) states "IN THE EVENT THIS APPLICATION IS REJECTED, THE DOWN PAYMENT ENCLOSED HEREWITH SHALL BE REFUNDED" in large boldface type, while in smaller type, there is another statement by which the prospect acknowledges that the downpayment shall be retained as liquidated damages, if he should fail to pay the balance due after acceptance by the company. Respondents' Franchise Agreements (CX 3, CX 4, CXs 16–18) state in boldface type at the bottom: "ALL MONEY WILL BE RETURNED IMMEDIATELY, IF APPLICATION IS NOT ACCEPTED." What the prospects don't know is that it is normal procedure for the company to "accept" virtually all applicants, and to do it within a matter of days (MacDonald, Tr. 553–54; Winstead, Tr. 340–41; McKinnon, CX 234, at p. 4; Smith, CX 234, at p. 5). In fact, it is company policy to interview only one prospect at a time for a particular franchise area, so that if one buys, it is not necessary to interview another (MacDonald, Tr. 548–49).

The franchise application not only contains the foregoing statements which have the capacity to deceive, but respondents have relief upon the "liquidated damages" provision to withhold or refuse to refund a deposit, even though language had been added to the application which completely negated the "liquidated damages" statement. For example, the franchise application of Joe Clay (CX 174 contains the following statement under the heading "remarks:"

> Deposit includes $171.66 credit for visit to home office interview, including air transportation and motel bill and cash in the amount of $828.34, making a total deposit of $1,000, as indicated below. If Mrs. Clay doesn't agree to transaction by 6–11–69 the $828.34 is to be refunded in full.

[9] Clay, Tr. 567–71; Labrum, CX 234, at p. 1; England, CX 234, at p. 3; McKinnon, CX 234, at p. 4; Smith, CX 234, at p. 5; Hawkins, CX 234, at p. 6.

Despite the fact that Mr. Clay understood the added language to constitute confirmation of the oral promises made to him and notwithstanding the fact that Mrs. Clay did not agree to the transaction by June 11, 1969, Mr. Clay had not received a refund of the deposit up to, and through, the time he testified at the hearing (Clay, Tr. 571–73).

34. In truth and in fact, solicited prospective franchisees do risk losing their deposits or downpayments submitted with applications for franchises and such deposits or downpayments are not refundable if the applicants withdraw or otherwise do not consummate the franchise agreements (admitted by respondents' Answer, p. 3).

False Representation Concerning Franchise Sales

35. Representations that geographical areas offered to prospective franchisees have not been previously franchised or that the areas offered have been franchised before and were profitable for the prior franchisee were false.

Arnold Krieger testified that respondents' franchise salesman orally represented that the area of Rochester, New York, was "just released" by the franchise committee, and that the nearest franchisee to Rochester, New York, was in the State of Virginia since the entire States of New York, Pennsylvania, and Ohio had never been franchised (Krieger, Tr. 184). He was also told that only 25 percent of the country remained unfranchised (Krieger, Tr. 191). Harold Winstead was told on two occasions, first when he applied for the franchise for the area of Corpus Christi, Texas, and later when he was sold an additional franchise for Houston, Texas, that both areas were "virgin territory," never before franchised, and that the whole State of Texas had never been franchised (Winstead, Tr. 337 and 350). Leonard Lynema testified that he was told the entire State of Indiana had never been franchised before (Lynema, Tr. 592). Mahlon J. England was told by a representative of respondents that his area was "virgin territory," never franchised before (England, CX 234, at pp. 2–3). Roy S. McKinnon was told that the area in which he was interested, Tacoma, Washington, was "virgin territory" (McKinnon, CX 234, at pp. 3–4). Mark Smith, when being interviewed at a later date for a franchise covering the same Tacoma, Washington, area previously held by McKinnon was told that the State of Washington was "virgin territory" (Smith, CX 234, at p.

5). Sam A. Hawkins was told that respondents' program had never been sold before in his area, New York City (Hawkins, CX 234, at p. 6).

The record also demonstrates that respondents represented that some areas offered had been franchised before and were profitable for the prior franchisees (on occasions when it appeared to be advantageous to do so). For instance, when Mahlon England, who had been sold a Continental franchise for the eastern half of the State of Idaho, was attending his seminar, respondent Heater orally represented that there was a franchisee named Labrum in Boise, Idaho, who was "doing great" (England, CX 234, at pp. 2–3). In fact, Labrum had previously been sold a franchise which included the exact area covered by England's Continental franchise, as well as the western half of Idaho (Labrum, CX 234, at pp. 1–2). Also, when Bruce Tronca was solicited to buy 51 percent stock interest in the franchise of John Kadwell covering various portions of the State of Wisconsin, Kadwell represented that a prior franchisee had been successful in accumulating a "great" number of very successful and satisfied members in those areas (Tronca, Tr. 657). The sale of stock referred to had to be approved by John Heater (Tronca, Tr. 659).

36. In truth and in fact, in a substantial number of instances, the geographical areas offered to prospective franchisees have been previously franchised and were not profitable for the prior franchisees (respondents' Answer, p. 3, admits that in "some" instances, the geographical areas offered have been previously franchised and were not profitable).

The evidence in the record showing the falsity of the "never franchised before" claim is of two kinds. First, specific individuals to whom the representation was made were negotiating for franchises in areas which actually had been franchised before. Such was the case in the State of Washington when Roy S. McKinnon was told that his area had not been franchised before (CX 234, at p. 4), when in fact he later discovered that there had been a prior franchisee in the same town of Tacoma (CX 166 A–B; CX 167). McKinnon was unsuccessful with his franchise. Respondents thereafter sold the same territory to Mark Smith upon the representation that the State of Washington was virgin territory (CX 234, at p. 5), when in fact the specific area Smith was contracting for had been franchised at least twice before. In the case of Mahlon England, the area of his Continental Credit

Card Corporation franchise (CX 234, at pp. 2–3) had in fact been previously franchised to Neil G. Labrum under his International Credit Card Corporation franchise (CX 234, at pp. 1–2), and the franchise was not profitable for Labrum.

Second, there have been instances of flagrant misrepresentation wherein franchise prospects were told that whole states had just been released from the "franchise committee" or had never been franchised before, when in fact there were many prior and current franchisees in the respective states, whose lack of success was manifest. Specifically, when Arnold Krieger was sold a franchise for Rochester, New York, in March 1970, he was told that the States of New York, Pennsylvania, and Ohio had never been franchised before. In fact, the following franchisees existed in those respective states prior to March 1970:

Franchisees in New York Prior to March 1970

Kaufman, Feldman (CX 190, #29)
St. Claire (CX 190 E, #52)
Summers (CX 190 E, #54)
Hawkins (CX 190 G, #75)
Agresti (CX 190 I, #94)
Donnelly (CX 190 M, #137)
Kunicky (CX 190 M, #146)
Schwartz, Barone (CX 190 O, #156)
Stratton (CX 190 O, #162)

Franchisees in Pennsylvania Prior to March 1970

Bly, Steigler, Hasso (CX 190 A, #4)
Peticca (CX 190 D, #40)
Thompson (CX 190 H, #88)
Pollock (CX 190 K, #119)
Peck (CX 190 N, #151)
Chern (CX 190 P, #166)

Franchisees in Ohio Prior to March 1970

Fleck (CX 190 B, #17)
Gajzer (CX 190 B, #20)
Handel (CX 190 B, #25)
Hubbard (CX 190 C, #27)
Lavy (CX 190 C, #32)
Stein (CX 190 E, #53)
Travis (CX 190 E, #57)

Youssef (CX 190 E, #63)
Headley (CX 190 F, #65)
Myers (CX 190 G, #86)
Frizzell (CX 190 H, #91)
Bolce (CX 190 L, #130)
Ochs (CX 186 A–B)

Similarly, Harold Jerome Winstead was solicited for the purchase of two franchises in the State of Texas in August of 1969, at which time he was told that the State of Texas had never been franchised before. In fact, the following franchisees existed in *Texas* prior to that time:

Mercer (CX 190 C, #35)
Kane (CX 190 G, #76)
Jones (CX 190 J, #108)
Pattilo (CX 190 K, #126)
Tompkins (CX 190 K, #126)
Carver (CX 190 L, #133)
Landreth, Cree (CX 190 N, #147)
Smith, Hatchet (CX 190 O, #160)

In addition, the testimony of former employees O'Flaherty and MacDonald confirms the frequent turnover and resale of franchised areas, making it highly unlikely that any area franchised by respondents in the last several years has not been franchised before (O'Flaherty, Tr. 434–35; MacDonald, Tr. 552). Respondents themselves make such a statement in seminar questionnaires, which franchisees must complete and acknowledge, wherein it is indicated that there is no place in the United States or Canada that respondents' program has not been introduced (CX 227, p. 2, #11; see also Heater, Tr. 805–06).

37. Respondents' representations that they offer only a limited number of sales franchises to qualified individuals and that respondents have a franchise committee which screens the qualifications of franchise applicants were false.

Arnold Krieger testified that he was told that there were four other applications for his area, which would have to be weighed by the "franchise committee" before making the choice as to whom the franchise for Rochester, New York, would be sold (Krieger, Tr. 186 and 190). Clayton Davidson testified he was told by respondent Gingold that Davidson and other franchisees would be

screened by a "franchise committee" before making the choice of a franchisee for the State of Nevada (Davidson, Tr. 277). Harold Winstead testified that the franchise salesman he dealt with stated two others had already been interviewed for the Houston, Texas, area, but that respondents always interviewed three before they sell a franchise and, therefore, they wanted to get him interviewed before they made up their minds which one of the three they were going to pick (Winstead, Tr. 335).

Neil G. Labrum was told that International Credit Card Corporation definitely limited the number of sales franchises to qualified individuals only, and that his application would have to be submitted to and screened by a "franchise committee" (Labrum, CX 234, at p. 1). Mahlon J. England was told that the company limited the sale of franchises to qualified persons and that his application would have to be examined and approved by the "franchise committee" (England, CX 234, at p. 3). Mark Smith was subjected to high pressure and told there were three or four more applicants for his area (Smith, CX 234, at p. 5).

This representation is also made by way of inference from the form letters and oral statements that a "regional manager" is interviewing other people for each area. The effect and purpose of these is obviously to give the impression that respondents check the qualifications of a number of persons before choosing franchisees and that obviously only one will be chosen. Furthermore, respondents' "Franchise Application" even states in part: "* * * the Company, at its expense, must make an extensive investigation of the Applicant * * *" (CX 19).

38. In truth and in fact, respondents do not limit the number of sales franchises offered. Respondents do not have a functioning franchise committee which screens franchise applicants' qualifications.

The testimony of Brian MacDonald, whose function was to process franchise applications for respondents, stated that *no applications were ever rejected during the time he performed such duties* (MacDonald, Tr. 554). He merely checked the incoming papers "to make sure there was an application, an agreement and a deposit" (MacDonald, Tr. 551). Respondents would not check any of the references called for on the applicant's "Personal History Statement and Questionnaire" form. There were never any meetings by company executives to see if the applicant "qualified" (MacDonald, Tr. 552). Once MacDonald had checked

the franchise applicant's papers, he would have the application "approved" and a telegram sent "on the date the salesman requested that the franchise committee was supposed to meet" (MacDonald, Tr. 553). The fact is that the "franchise committee" was nothing more than a paper creation, a list of names that never met or functioned (MacDonald, Tr. 553). Some of the people named on the list of "franchise committee" members were not even working for the company any longer (MacDonald, Tr. 559).

Mr. MacDonald's testimony is reinforced by that of Joseph O'Flaherty, former head of respondents' Franchise Relations Department. The *complete* files on all franchisees would be sent to him after the franchisees had completed the training session. From these files, he could attest to the fact that there was no report of a "franchise committee" or any attempt to screen out unqualified people before accepting them as franchisees (O'Flaherty, Tr. 430–31, 473, 475, 481). He also testified "there was no actual franchise committee that I ever knew of or met, or was familiar with" (O'Flaherty, Tr. 431), despite the fact that "in two and one half years, with a company of this size you get to know exactly what's going on" (O'Flaherty, Tr. 468). Stated differently, O'Flaherty also testified: "I knew there was no such thing. But when it came time to terminate the fellow, I told them the franchise committee has decided that you must go" (O'Flaherty, Tr. 481).

39. Respondents' representation that there is a "Regional Manager" of respondents who is interviewing other franchise applicants for the same area as each franchise prospect and that the prospective franchisees must act immediately to be considered for a franchise is false.

40. In truth and in fact, there was no "Regional Manager" of respondents interviewing other franchise applicants in each area, but rather all persons responding to respondents' invitation for inquiries received the same form letter stating that said "Regional Manager" is interviewing other interested persons for the same franchise area. The record indicates that the "Regional Manager" was nonexistent during the time of Brian MacDonald's employment from February 24, 1969 to November 1970 (Tr. 539, 546). The president of Continental Credit Card Corporation testified that he did not know who performed the function of "Regional Manager" in 1969, 1968, 1967 or 1966 (Gingold, Tr. 711–12).

41. Representations that franchise holders receive substantial

benefits from renewals of memberships and from annual bonuses based on a percentage of net credit charges submitted by members in each franchisee's territory were false.

42. In truth and in fact, franchise holders do not receive substantial benefits from renewals of memberships or from annual bonuses based on a percentage of net credit charges submitted by members in each franchisee's territory.

Benefits from renewals of memberships only occur if a member sold by a franchisee lasts for two years and decides to renew his contract hereafter. Accordingly, both the member and the franchisee must still be active at a point in time two years in the future for any franchisee to receive such benefits. The vast majority of franchisees do not last for a period of even one year, let alone two (140 out of 172 franchises lasted one year or less). Moreover, not only do very few members renew their contracts after two years, but the average longevity of a substantial number of respondents' members is on the order of 5 months (CX 192 A–C, 193 A–E).

Similarly, for a franchisee to receive the benefits of annual bonuses based on the charge volume submitted by his members, both he and the member must still be active at the end of each year, at which time such bonuses are due and owing (see paragraph #10 in respondents' franchise agreements, CXs 16 A and 18 A). Respondents' own "flow chart" of all active franchisees as of October 1969 discloses the extraordinary lack of membership sales, which emphatically indicates that no substantial benefits in the form of either renewals or bonuses could possibly occur (CX 189 A–C).

43. Representations by respondents that franchise holders risk losing little or nothing in investing in a franchise; that respondents will repurchase the franchise and/or aid in its resale; and that the franchise is a vested property right which may be sold, assigned, transferred, or testated were false.

The representation that respondents will repurchase the franchise was made to witnesses Krieger (Tr. 192) and Lynema (Tr. 621 and 629); and witness Winstead testified that when he attended his training seminar the whole class of franchisees was told respondents would aid in reselling the franchise for any unsuccessful franchisee (Winstead, Tr. 362–63).

The representation that the franchise is a vested property right which may be sold, assigned, transferred or testated is clearly made in the "Franchise Proposals:"

* * * No one in the world can take the Franchise away from you * * * THIS FRANCHISE MAY BE SOLD, ASSIGNED OR TRANSFERRED WITH APPROVAL OF THE COMPANY AND INURES TO THE BENEFIT OF THE ESTATE OR HEIRS OF THE FRANCHISE HOLDER (CX 45 I, #9 and CX 46 I, #9).

The use and effect of this assurance in the "Franchise Proposals" is demonstrated by the testimony of Mr. Winstead relating the oral statement made to him by the franchise salesman: "When you buy this, you can will it to your family, your kids, it is yours for a lifetime and their lifetime" (Winstead, Tr. 339).

44. In truth and in fact, franchise holders do risk losing their investment. Respondents do not repurchase the franchise, and in those instances where respondents do aid in its resale, they retain at least half of the amount for which it is resold (admitted by respondents' Answer, p. 4). The franchise is not a vested property right which may be sold, assigned, transferred, or testated. If a franchise holder does not produce the sales quota set forth in his franchise agreement, the franchise may be, and usually is, terminated by respondents (admitted by respondents' Answer, p. 4).

That a vast majority of franchises ultimately end in termination is evident from CX 190 A–Q. In essence, the quota requirements so limits and qualifies the right to sell, assign, transfer, or devise the franchise as to render it deceptive and meaningless, where virtually every franchisee cannot and does not meet the quota.

45. Representations that respondents' program has received national acceptance are false.

46. In truth and in fact, respondents' program has not received national acceptance.

"National acceptance" connotes large numbers of members who have used the program *approvingly*. Neither the sales of memberships in respondents' program nor the longevity of members has been such that the program could by any stretch of the imagination be deemed to have achieved "national acceptance." Joseph O'Flaherty, whose function was to stimulate and oversee the sales of each franchisee, testified that the average franchisee over a period of three years made a total of five sales per year (O'Flaherty, Tr. 419–20). Raleigh Fish, whose function it was to deal with members during their entire association with respondents after their contract was received, testified that there was considerable turnover amongst members, with 30 to 50 quitting each month (Fish, Tr. 122).

Respondents' "flow chart" showing the membership sales of all franchisees active as of October 1969 discloses that prospects for memberships were *rejecting* the program nationally, judging from the lack of sales results indicated therein (CX 189 A–C). This result is confirmed for the period from January 1, 1967 through October 1969, during which time 172 franchises were able to achieve membership sales amounting to an average of $1,449 earnings per franchise (CX 190 A–Q).

Significantly, of the 803 members participating in respondents' program in October of 1969 (CX 191 C), only 24 predated January 1967 (CX 192 A–C).[10]

The lack of "national acceptance" is not limited to respondents' program as operated under the more recent names Universal Credit Acceptance Corporation and Continental Credit Card Corporation. It was also a shoddy program when it was operated under the name National Credit Service (Winstead, Tr. 337–38, 357; Lynema, Tr. 629).

47. Claims that there are thousands of members honoring all credit cards under respondents' program each and every month were false.

This representation is made directly in respondents' "sales presentation" manual: "We have members all over the country. *Thousands* of merchants Honoring All Credit Cards, and increasing their business *each and every month*" (CX 130, at p. 10) (emphasis added).

There are many examples of oral representations used by franchise salesmen and franchisees regarding the size of respondents' membership. Arnold Krieger was told there were over 10,000 members in the program (Krieger, Tr. 189). Leland McBride was told that "practically 2/3 of all gas stations in the United States were using the program" (CX 234, at p. 7). Russell Sheldon received the impression that "there were thousands and thousands of members using the program (CX 234, at p. 10). William P. Brooks was told that respondents "had thousands of members" (CX 234, at p. 11). Marino Manicucci was told that respondents "had a membership in the thousands" (CX 234, at p. 13).

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[10] Of the 24 members referred to, all but 11 received one or more special considerations, *e.g.*, a preferred discount rate of 5 percent as compared with the normal 6 percent rate; no initial membership fee; no monthly dues or $6 monthly dues as compared with the normal $10; a lifetime membership which by definition means that no subsequent membership fee could be charged; at least two of these members were owned by respondent Heater (CX 192 A–C).

48. In truth and in fact, there are not thousands of members honoring all credit cards under respondents' program each and every month.

The number of members in the program can be determined by observing the number of members receiving checks or statements from respondents each month. From January 1968 through October 1969 said sources indicated that the memberships averaged 781 per month, and there was never any month in which there were as many as even *one* thousand members (CX 191 A–C). Raleigh Fish testified that there were approximately 1,100 members *under contract* at any given time, *though not all would actually be using the program* in terms of submitting charges (Fish, Tr. 121). The foregoing was confirmed by respondent Heater, who reluctantly acknowledged that there are only some 800 active members (Heater, Tr. 816).

Credit Charges

49. Claims that all credit charges submitted under respondents' program are guaranteed payable without recourse; that respondents assume all risk of nonpayment by the members' customers; that members can expect to be successful and satisfied with the program's performance; and that members usually continue using respondents' program for two years and renew their contracts thereafter were false.

That all credit charges submitted under the program are guaranteed payable without recourse is respondents' most widely expressed and fundamentally deceptive claim. The mailers used to attract prospects for both franchises and memberships contain this claim:

Through our program any merchant, large or small, can make instant credit sales * * * with guaranteed payment (CX 24 A and CX 25 A);

Payment is guaranteed, non-recourse (CX 31 A and CX 32 A);

* * * receive one check for all credit transactions * * * on a guaranteed non-recourse basis (CX 34 A);

GUARANTEED PAYMENT * * * eliminate bad debts * * * (CX 37 A);

* * * ONE BIG CHECK for all credit sales every month * * * payment is guaranteed non-recourse (CX 38 B, copyright 1965; CX 39 B, copyright 1969);

GUARANTEED NON-RECOURSE PAYMENT (CX 41 B).

Advertisements appearing in magazines have contained this claim:

Our unique service allows retail business firms to honor over 200 million credit cards—including major oil company cards—with guaranteed payment (CX 43, at p. 90 and CX 44, at p. 56).

Also, the Better Business Bureau reports on respondents, which have been used as sales tools, contain the "non-recourse" claim (MacDonald, Tr. 551; Lynema, Tr. 596–97, 600, 602):

These charges are accepted on the without recourse basis (CX 120 A and CX 121).

The "Franchise Proposal" states:

All valid credit transactions are payable without recourse (CX 45 F and CX 46 F).

The basic sales kit employed by franchise salesmen to sell franchises and ultimately by franchisees (as well as home office membership salesmen) to sell memberships to retail merchants begins with a resume of the respondents' "Background" and a "Synopsis of Operation." In the latter paragraph it is stated: "the Members are paid for all properly completed credit charges on a guaranteed non-recourse basis" (CX 23 B, International Credit Card Corporation; CX 132 B, Universal Credit Acceptance Corporation; and CX 179 D, Continental Credit Card Corporation). The sales kit also contains further claims as to the "non-recourse" feature of the program:

The firm permits its member-merchants to accept any of more than fifty different credit cards with a maximum guaranteed payment by Universal (CX 179 R);

Charges are paid on a guaranteed NON-RECOURSE basis (CX 179 Z83);

NON-RECOURSE: THE COMPANY AGREES TO PAY MEMBER WITHOUT RECOURSE, except where otherwise provided, for all valid credit charges extended in accordance with the provisions of this agreement * * * (CX 179 Z88).

A "sales presentation" manual with which respondents train their franchisees and home office membership salesmen contains the following references to the alleged nonrecourse feature of the program (copyright 1965 with some 1967 revisions):

This means that a customer can walk into your place of business today and use * * * credit cards on a guaranteed non-recourse basis (CX 180 D);[11]

* * * we can bring it to you without recourse—without any risk to you! (CX 180 O, approach No. 3);

Charges are paid on a guaranteed, non-recourse basis (CX 180 Z13, #5).

Another "sales presentation" manual, dated February 10, 1969, includes the following representations:

We guarantee those charges up to $150 per transaction, whether we collect from the customer or not (CX 130, at p. 8);

Besides, you're issuing credit cards with guaranteed payment back to you on a non-recourse basis (CX 130, at p. 22);

Because, we're going to guarantee the charges to you and pay you whether we collect from the customer or not, you realize of course, there is a cost and a risk involved and we're taking that risk (CX 130, at p. 25);

I want to go over this membership application in detail * * * it says the maximum credit charge here is $150 per transaction * * * and of course, it's non-recourse to you (CX 130, at p. 26).

The foregoing include not only the representation that respondents' program is "guaranteed non-recourse," but also the claim that respondents *assume the risk* of nonpayment by the members' customers. For example, the older "sales presentation" manual (CX 180 O, approach No. 3) clearly states: "we can bring it to you without recourse—*without any risk to you!*" (emphasis added). The current "sales presentation" manual also clearly states: "* * * there is a cost and a risk involved, and *we're taking that risk*" (CX 130, at p. 25) (emphasis added). In addition, the sales kit also contains what purports to be a newspaper article about respondent Heater, the contents of which describes the program by stating: "*The firm assumes the risk* of collecting payment. It, in turn, pays the merchant" (CX 179 R) (emphasis added).

The effect of the written materials containing the deceptive description of respondents' program as "non-recourse," with the risk to be borne by respondents, is evident from the testimony. Virtually every franchisee and member prospect regarded said

[11] Footnote at bottom of "sales presentation" manual page states: "*Please note*—Those persons attending the home office Membership Sales Training Seminar are required to memorize the above introduction."

representations as constituting the essence of the service to be provided by respondents.[12]

The representation that members can expect to be successful and satisfied with the program's performance and that members usually continue using respondents' program for two years and renew their contracts thereafter is made indirectly to franchisees and prospective franchisees from the earnings projection sheets (CXs 47–59). Said projections infer that 50 percent of the memberships sold can be expected to renew their contracts after the initial two-year contracts expire. Further, these representations are made directly in the reprints of articles included in the sales kits of franchise salesmen and franchisees. One such article in Business Digest, entitled "The Credit Card Revolution," contains the statement: "Mr. Heater's plan has become so successful and requests for membership so numerous, he says, that it has been necessary to restrict membership * * *" (CX 179 P and CX 110 C).

The deceptive effect of the aforesaid articles and the accompanying representations made by franchisees and home office membership salesmen is apparent from the testimony of members. Russell Sheldon, a member in Reno, Nevada, understood that the "thousands and thousands of members using the program * * * were extremely happy and renewed their contracts repeatedly" (CX 234, at p. 10); William P. Brooks, a member in Napa, California, believed that it was normal for members to renew their contracts repeatedly due to their extreme satisfaction with the program (CX 234, at p. 11); and another member from Nevada, Marino Manicucci, believed that respondents' members were all successfully using the program and renewing their contracts after their first two year contracts expired (CX 234, at p. 13).

In addition, respondents' "sales presentation" manuals instruct both franchisees and membership salesmen to show prospects appropriate testimonial letters and payment checks as an indicator of the success of the program, and many of such success letters and checks bear dates extending back substantially more than two

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[12] Krieger, Tr. 188, 204, 243–44; Davidson, Tr. 261–62, 271, 281; Winstead, Tr. 338, 342; Lynema, Tr. 609–11, 616; Tronca, Tr. 655; Clay, Tr. 574–75; Labrum, CX 234, at p. 2; England, CX 234, at p. 3; McKinnon, CX 234, at p. 4; Smith, CX 234, at p. 5; Hawkins, CX 234, at p. 6; McBride, CX 234, at p. 7; Ferre, CX 234, at p. 8; Dee, CX 234, at p. 8; Sheldon, CX 234, at p. 10; Brooks, CX 234, at p. 11; Padgett, CX 234, at p. 11; Kiefert, CX 234, at p. 12; Manicucci, CX 234, at p. 13; Dorigo, CX 234, at p. 13; Liebowitz, CX 234, at p. 14.

years (CX 180 F and G; Lynema, Tr. 612–13; CX 179 Z7–37, CX 179 Z41–65).

50. In truth and in fact, not all credit charges submitted under respondents' program are guaranteed payable without recourse. Respondents do not assume all risk of nonpayment by the members' customers. A substantial number of members have been neither successful nor satisfied with the program's performance. Most members have not continued using respondents' program for even one year, and have not renewed their contracts after the expiration of two years.

Respondents' contract obligates them to pay only "valid" charges on a nonrecourse basis. *However, there are at least 18 reasons for which respondents consider a charge "invalid" and therefore subject to recourse.* The disclosure of the fact that there are 18 reasons for recoursing is not made to either franchisees or members until a point in time after they have paid their money for a franchise or a membership. Eighteen of the reasons for recoursing are set forth on the back of a document called a "Debit/Credit/Memo" (CX 139 B). No franchisees saw such document or knew the full nature and number of reasons for recoursing until well into the operation of their franchise when members they had sold would tell them that recourses had occurred for one of the reasons enumerated on the back of said "Debit/Credit/Memo." [13]

It is evident that in view of the respondents' failure to apprise franchisees and home office salesmen of the full number and nature of reasons for recoursing, members commonly experienced unexpected recoursing for a multitude of reasons (Clay, Tr. 575–76, 580, 581–83; McBride, CX 234, at p. 7; Ferre, CX 234, at pp. 7–8; Dee, CX 234, at pp. 8–9; Leeper, CX 234, at pp. 9–10; Sheldon, CX 234, at p. 10; Brooks CX 234, at p. 11; Padgett, CX 234, at pp. 11–12; Kiefert, CX 234, at p. 12; Manicucci, CX 234, at pp. 12–13; Dorigo, CX 234, at pp. 13–14; Liebowitz, CX 234, at pp. 14–15).

Members complained at a rate of 20 to 30 per week for 3 weeks of each month (Fish, Tr. 97–98). Recoursing was one of the two major reasons for such complaints. In actual practice, *the only valid credit charge is one that has been paid by the customer*

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[13] Krieger, Tr. 193–95, 197, 212; Davidson, Tr. 258–59, 271, 282–83, 323; Winstead, Tr. 343, 344; Lynema, Tr. 612, 614, 616; Colfels, Tr. 513; Labrum, CX 234, at p. 1; England, CX 234, at p. 3; McKinnon, CX 234, at p. 4; Smith, CX 234, at p. 5.

(Fish, Tr. 102). This completely contravenes the nature of the bargain that members and franchisees thought they made.

The incidence or the frequency of recoursing has been such that the program cannot be considered "non-recourse." By a simple mathematical computation using the information in CX 125 and respondents' income statements covering the same periods of time (CXs 122–124), it is possible to determine the net percentage of total charges that were recoursed:

July 1968 through June 1969	
6% credit charge discount income	$ 135,693
Total credit charges submitted [14]	2,261,650
Net recourses	211,100
Recourse rate as percentage of total charges submitted	9%

July 1967 through June 1968	
6% credit charge discount income	$ 105,371
Total credit charges submitted	1,756,183
Net recourses	233,960
Recourse rate as percentage of total charges submitted	13%

July 1966 through June 1967	
6% credit charge discount income	$ 99,485
Total credit charges submitted	1,658,083
Net recourses	339,178
Recourse rate as percentage of total charges submitted	20%

56. Respondents' respresentations that the program costs members little or nothing at all and that the program costs members half as much as trading stamps were false.

The representation that the program costs little or nothing at all is made in respondents' direct mailers (CX 29 A, CX 30 B, CX 34 A, CX 41 A, CX 42 B), "Franchise Proposal" (CX 45 F and CX 46 F), and in various sales presentation manuals employed:

[14] Respondent Heater confirmed that the credit charge discount income figures represented in CXs 122 through 124 do in fact constitute 6 percent of the total credit charges submitted in the respective years indicated, so that by performing the mathematical computation, the total credit charges submitted can be ascertained (Heater, Tr. 774).

(Higher unit sales *eliminates all cost.*) (CX 180 G, #14);

This fact alone eliminates the complete cost of our program (CX 180 J);

* * * Since credit customers spend some 53% to 200% more than cash customers, the extra profit you make on these larger sales more than eliminates any cost of Honoring All Credit Cards (CX 180 Z32);

So, this in itself, eliminates any cost to the All Credit Card program (CX 130, at p. 6);

In fact, once you join us, it's very painless. From then on, we'll be sending you money and the program is going to pay for itself and pay for everything else (CX 130, at p. 28); and

Tell him that, within 30 days he can pay for the service and pay himself a profit beside, and pay his bills with the money we send him (CX 130, at pp. 36–37).

Another instructional document, entitled "Membership Sales Presentation—Subject: Positive Statements (Command Phrases that Sell)," includes the following statements:

You will pay for the program and pay yourself a profit besides in less than 30 days (CX 131 A, #4);

It doesn't cost you money; it will make you money! (CX 131 A, #13); and

The profit you make on the higher unit sales more than eliminates any cost of the program (CX 131 B, #20).

Such "command phrases" do reach prospects (Kiefert, CX 234, at p. 2; Sheldon, CX 234, at p. 10).

That respondents' program costs members half as much as trading stamps is a claim that is made directly in direct mailers (CX 29 A, CX 30 B, and CX 42 A), as well as in the list of "Positive Statements (Command Phrases that Sell)," which includes: "Honoring All Credit Cards costs less than half the cost of green stamps because we only charge you for the extra business we bring you" (CX 131 B, #30).

57. In truth and in fact, respondents' program does not cost members little or nothing at all. The program does not cost members half as much as trading stamps. Taking into account the initial membership fee, the monthly dues, the discount rate, the total amount of charges recoursed, and the 6 percent *discount fee paid even on recoursed charges*, the program costs the members a substantial amount.

The falsity of this claim is obvious. Raleigh Fish, former director of member relations, testified that the claim that the cost of the program is 7 percent is based upon the assumption that the member submits $1,000 credit charges each month and receives no

recourses. The computation is as follows: the $240 membership fee prorated over a 24-month period would be $10 per month. The member dues are an additional $10 per month. The 6 percent discount rate on $1,000 worth of charges is reduced so that it is 5 percent, or $50. The total of $50 discount, plus $10 dues, plus $10 membership fee would be $70 per month as the cost to produce $1,000 worth of business, or 7 percent (Fish, Tr. 127–28).

However, in actual practice the average member at best lasts about 8 months and sends in only $200 per month in charges. This means that the cost involved to produce that $200 in charges is a fantastically high percentage. The $240 membership fee prorated over only 8 months of program usage would be $30 per month. Similarly, the monthly dues, which must be paid regardless of whether or not the program is used after the 8 months, would be $30 per month on a prorated basis. And the 6 percent discount rate on his $200 volume would be $12. *Accordingly, the total cost for the average member would be $30 membership fee, plus $30 dues, plus $12 discount for a total of $72, or 36 percent* (Fish, Tr. 128–29). In addition, the average member can expect to be recoursed at a rate of from 12 percent to 15 percent of the total amount of the charges he submits (CX 125). For the average member, therefore, the cost of the program rapidly approaches 50 percent.

61. Claims that respondents are the largest credit card clearing house in America were false.

Respondents state that they are "the largest credit card clearing house in the world" (CX 29 B, CX 34 A, CX 28 B, CX 42 B, CX 45 B and G, CX 46 B and G, CX 186 A). The deception is evident from the testimony of persons who believed such claims indicated the respondents were "bigger than American Express" (Lynema, Tr. 602), persons who were led to believe that respondents' financial resources were such that they had $3 million in the bank (Krieger, Tr. 187; Winstead, Tr. 334), as well as from persons who merely accepted the representations at face value, thereby believing respondents' size was comparable to that of the large, well-known credit card operations (Manicucci, CX 234, at p. 13; Brooks, CX 234, at p. 11).

By definition, a "clearing house" is "an institution or establishment for carrying on the business of clearing," which in turn is defined as:

a method adopted by banks and bankers for making an exchange of checks, etc., held by each against the others, and settling differences of accounts with each other (Webster's New International Dictionary, 2nd edition, pp. 499–500).

Literally, therefore, respondents' representation has the tendency to imply a relationship with all of the individual credit card issuers, whose cards respondents "approve." In truth and in fact, respondents act merely as a collection agency.

62. In truth and in fact, respondents are not the largest credit card clearing house in America. There are other credit card operations with larger retail memberships and with larger amounts of financial resources than respondents' business.

The representation is clearly false under the literal interpretation of "clearing house," because as even respondent Heater admitted, respondents do not really clear anything with any other credit card companies (Heater, Tr. 872). Furthermore, respondents' size as compared with the size of other credit card issuers makes the claim false.

Respondents' total active membership during the period January 1968 through October 1969 averaged 781 (CX 191 A–D), with about 1,100 members under contract (Fish, Tr. 121). The BankAmericard system had contracts with some 509,000 merchants in the United States as of December 31, 1970, which merchants had approximately 680,000 outlets (CX 216). The Master Charge system had contracts with some 628,000 merchants representing a total of some 840,000 outlets as of December 31, 1970 (CX 217). Respondents' total revenues produced from their program was in the neighborhood of $1 million a year from July 1966 through June 1969 (CXs 123–125). And respondents' net working capital as of January 1969 was actually a deficit of almost $26,000 (CX 126 A–B). It is clear, therefore, that other credit card programs, particularly those backed by banking institutions, have substantially larger retail memberships and larger amounts of financial resources than do respondents.

63. Representations that respondents' program is approved or endorsed by the individual issuers of the credit cards accepted by respondents were false.

This representation results from the publication and dissemination by respondents of a direct mailer (CX 42 B) and sales kits (CX 179 L), containing a list of the individual credit cards which are acceptable references under respondents' program. Said lists are entitled "Approved Credit Card List." Following the title there

is a list of some 90 individual credit cards. Although respondents footnote or asterisk reference the list with a disclosure that "credit cards are accepted as a credit reference only, customers are billed direct by Universal Credit Acceptance Corporation," such disclosure does not prevent readers from believing that the issuers of the credit cards listed somehow have knowledge of and approve of the use of their cards in respondents' program (Sheldon, CX 234, at p. 10; Brooks, CX 234, at p. 11; Kiefert, CX 234, at p. 12; and Manicucci, CX 234, at p. 13).

64. In truth and in fact, respondents' program has not been approved or endorsed by the individual issuers of the credit cards accepted by respondents (admitted by respondents' Answer).

65. Representations by respondents that authorized capitalization of $3,000,00 is liquid and available to provide financial resources and ability to service members were false.

The resume containing the background and synopsis of respondents' operation includes the statement that: "The contractual obligations with member firms are backed by the resources of Universal Credit Acceptance Corporation, with an authorized capitalization of 3 million dollars" (CX 179 D). The same statement was made in the resume of the background and synopsis of operation of International Credit Card Corporation (CX 23 B). The "Franchise Proposals" (CX 45 B and CX 46 B) state that Universal Credit Acceptance Corporation is "a multi-million dollar national firm doing business from border to border and overseas, employing a large staff of general office, accounting, sales and executive personnel." The Better Business Bureau report on Universal Credit Acceptance Corporation (CX 121) repeats that Universal has "an authorized capitalization of $3,000,000," and said report often was used by respondents for sales soliciting purposes (Winstead, Tr. 333; MacDonald, Tr. 551; Lynema, Tr. 596–97, 600, 602). The foregoing language taken alone or accompanied by oral representations has led both franchise and member-prospects to believe that the amounts represented reflected the amount of money respondents actually had on hand at any given time to honor their commitments (Sheldon, CX 234, at p. 10; Brooks, CX 234, at p. 11; Krieger, Tr. 187, 189; Lynema, Tr. 602–04; Winstead, Tr. 334; MacDonald, Tr. 548; Tronca, Tr. 655).

66. In truth and in fact, respondents' authorized capitalization of $3,000,000 is not liquid and available to provide financial resources and ability to service members. It is merely the amount

selected by respondents as the sum on which the fee to be paid to the California Corporations Commissioner was determined. Further, respondents fail to disclose the relevant information that their net working capital is a deficit, so as to mislead and deceive prospective franchisees and prospective members with regard to respondents' financial condition.

During the period pertinent to this proceeding, the only bank accounts maintained by respondents were those at the local branches of the Bank of America and the Hibernia Bank (Cerino, Tr. 690–91). By stipulation, respondents admitted that the total amounts on deposit in said banks during the time period January 1, 1965 to November 1971 ranged from $10,000 to $99,000 (Tr. 697).

Moreover, according to the Dun and Bradstreet reports written on respondents from a financial statement submitted by respondent Heater, respondents had a *net working capital deficit* of $25,619 as of January 1969 (CX 128 A–B, CX 235 A–B). The testimony of all franchisees and member witnesses reveals that the sales solicitation made to them failed to disclose that fact, which is very material since respondents are obligated to pay charges submitted by members.

67. Claims and representations that members are assured a minimum 10 percent increase in business within the first 12 months using respondents' program and that, in the event such increase does not materialize, membership dues will be waived for the second year were false.

These claims are made in direct mailers (CX 29 A, CX 30 B, CX 41 B and CX 42 A), in respondents' sales kit (CX 179 Z86), in their "Sales Presentation" manuals (CX 130, at pp. 7 and 26; CX 180 G, #17; CX 180 L; CX 180 Y; CX 180 Z12, Z30, Z33), and in respondents' list of "Positive Statements (Command Phrases that Sell)" (CX 131 B, #18).

68. In truth and in fact, in most instances, members have not realized a minimum 10 percent increase in business within the first 12 months using respondents' program and have not received a waiver of membership dues the second year (respondents' Answer, p. 4, admits "some" members failed to realize a minimum 10 percent increase in business within the first 12 months using respondents' program).

CX 193 A–E discloses that a sampling of 101 members terminated the program in approximately 5 months' time. The

reasonable inference to be drawn from this lack of longevity is that said members failed to receive the represented benefits from it, notably a 10 percent increase in business. In addition, Mr. Fish noted that the so-called guarantee is deceptive because the guarantee only permits the member to continue using the program (Fish, Tr. 130). In other words, the member would have to send in more charges and chance more recoursing to receive the "benefits" of this guarantee, when he was already fed up with the program.

The testimony of respondents' members was specific in this regard. Joe Clay did not receive any increase in business from using respondents' program (Clay, Tr. 575). Similarly, members McBride (CX 234, at p. 7), Ferre (CX 234, at p. 8), Sheldon (CX 234, at p. 10), Brooks (CX 234, at p. 11), Kiefert (CX 234, at p. 12), Manicucci (CX 234, at p. 13), and Dorigo (CX 234, at pp. 13–14), all indicated that they failed to experience the assured results. Likewise, the testimony of franchisee witnesses Lynema, Colfels, Krieger, Tronca, Davidson and Winstead demonstrates that the members they sold the program to failed to receive the benefits contracted for, and therefore dropped it in a short period of time (Lynema, Tr. 631; Colfels, Tr. 520–21; Krieger, Tr. 198, 200, 206–07, 208, 225–26; Tronca, Tr. 663–66; Davidson, Tr. 286–87, 295; Winstead, Tr. 354–55).

69. Representations that respondents are members in good standing of an independent organization by the name of the Fair Trade Bureau and that the Better Business Bureau has written an uncensored, objective report on respondents' business were false.

70. In truth and in fact, respondents are not members of an independent organization by the name of the Fair Trade Bureau. The Fair Trade Bureau is a division of respondents, having no members or function other than its use as a reference in the materials disseminated by respondents.

Respodent Heater indicated that the Fair Trade Bureau is part of a corporation called "National Professional and Businessmens Association," of which he is president; there are no stockholders; and Universal and Continental are the only "members" of the Association after five or six years of "operation" (Heater, Tr. 774–78).

71. In truth and in fact, the Better Business Bureau reports evaluating respondents' businesses are not uncensored, objective documents.

By letter dated February 26, 1969, the Better Business Bureau of San Mateo County, Inc., advised respondent Heater:

Dear John:

I an enclosing reports the Bureau is sending out on your organization. These reports are dated September 1967 and I was wondering whether there should be any additions or deletions to make the report current.

If you feel it necessary to redo the reports, I would appreciate having approximately 500 copies for distribution to Bureaus and inquirers. If no changes are necessary, I would appreciate being so informed (CX 196, CX 120, CX 121).

In addition to the foregoing opportunity to censor the Better Business Bureau reports, the reports themselves, CX 120 and CX 121, reveal that the contents are taken almost *in toto* from respondents' literature. In view of this, the reports are more subjective accounts, repeating respondents' own advertising claims. The reports are later used by respondents as sales aids which have a new aura of respectability by virtue of the Better Business Bureau name accompanying them. Consequently, they serve to thwart even the most diligent attempts of both able businessmen and less experienced members of the public to ascertain the legitimacy of respondents' program before investing in it (Lynema, Tr. 588–606).

72. Every credit charge submitted by members is subject to the most intensive collection procedure in the credit industry, consisting of billing, outside collection, and legal action (CX 179 Z82) is a false representation.

Members (and franchisees) are led to believe respondents use such effective collection procedures that virtually all charges are collected, thereby minimizing the incidence of recoursing.

73. In truth and in fact, every credit charge submitted by members is not subject to the most intensive collection procedure in the credit industry, consisting of billing, outside collection, and legal action.

Little effort is made by respondents to collect certain charges, namely the smaller charges, whereas there is more attention given to collecting the larger ones. The collection supervisor had accounts over six months' old which hadn't even been worked on (Fish, Tr. 136). Respondents' collection efforts are not uniformly intensive but are determined by the dollar amount of each individual charge (admitted by respondents' Answer, p. 4; see also CX 179 Z82). Respondents do not in practice institute legal action

against delinquent customers (see respondents' Answer, p. 5), and they fail to disclose to members and to debtor-customers, at any time, that North American Collections, the agency to which delinquent accounts are turned over, is not an outside agency, but rather an affiliated division of respondents. Respondent Heater testified that "North American Collections is designed to accelerate collections by an apparent change of name so people will think we are getting serious and want to collect these charges." He also admitted North American Collections does not collect bills for any company other than Universal, of which it is a part (Heater, Tr. 778–79; CX 144, CX 145, CX 146 A–B).

78. In truth and in fact, respondents have not instituted legal action against inactive members whose accounts respondents have determined are in arrears (admitted by respondents' Answer, p. 5; see also testimony of witness Fish to this effect, Tr. 126).

Respondents Knew Their Program Was A Failure But Continued To Victimize The Franchisees Regardless

Joseph O'Flaherty testified directly about respondents' knowledge that the program was a failure:

Q. Are you saying that the company knew that the franchisees would fall flat on their face going out and selling the program if they knew?

A. I would say so, yes.

HEARING EXAMINER LYNCH: What do you base that belief on?

THE WITNESS: In the first place, one has to assume that the company knew how the program worked. The history of the fatality rate of members and the procedures with regards to recoursing. Quite obviously, the company knew that. Therefore, if you know that, you know exactly what's going to happen out in the field, and there is only two ways the program can be sold. You're either going to lie about it, or you're not going to sell it at all. This is just plain, common sense * * * (O'Flaherty, Tr. 426–27).

Another indication of respondents' knowledge and expectation that franchisees would fail is the steps taken in advance to attempt to insulate respondents from accountability. In this connection, Mr. O'Flaherty testified:

Q. Were the franchisees required to take a test at the conclusion of the seminar?

A. Yes.

Q. Why was the test given?

* * * * * * *

A. It was given to eliminate problems in the future when it came time

to terminate the franchise. It was designed to get him acknowledge facts so that when we came around to terminate him, we could always relate to this test and say on so and so date, you acknowledged the fact that this was so, and therefore, you didn't have much to stand on (O'Flaherty, Tr. 429–30).

That respondent Heater was aware of the actual sales, or rather the lack of sales, of franchisees is manifest from the testimony of Mr. O'Flaherty. His department conducted a study which was submitted to Heater in March of 1970, covering the period of the preceding three years. It covered the average number of sales per franchise, the general life expectancy of franchisees. The results were that franchisees were able to produce an average of only five sales each per year (O'Flaherty, Tr. 419–20). When O'Flaherty was questioned as to whether or not he brought this knowledge of franchisees' failure to the attention of Heater, he testified as follows:

A. Verbally. I think we would have discussed it periodically, but, quite obviously, that was unnecessary.

Q. What were the nature of your discussions with Mr. Heater concerning inability of franchisees to make money on their franchises?

A. Mr. Heater had indicated to me, had many conversations with me, regarding the franchisee and his ability to produce sales, etc. And, of course, he did stress in conversations, that it was an ability franchise. And, quite obviously, it rested on the franchisee to make sales on his investment. He also indicated that they didn't have to make money on their investments, they were getting an education basically, and they would never invest again in any of this manner after they got through this experience. That it was an education for them. * * * And if we had not taken the money, someone else would (O'Flaherty, Tr. 421–22).

* * * * * * *

Q. Did Mr. Heater ever relate to you his opinion about the qualifications and abilities of a franchisee of the company?

A. Mr. Heater talked to me many times about the franchisees. He took exception to the fact, as far as I was concerned, that I was attempting to relate to them on an "intelligent basis." And, his feeling was that they should not be related to as intelligent people, they were, basically, children. For instance, as an example, Mr. Heater indicated to me in many cases, that the word "pursuant" would not be understood by 90% of the franchisees, and therefore I should talk to them in simple language.

Q. Did the company have a fixed procedure for canceling franchisees who did not produce membership sales?

* * * * * * *

A. Yes, we did. This fluctuated from time to time depending how we were going as far as franchise sales were concerned. But, on several occasions,

Mr. Heater indicated to me that 120 days should be the magic number. That is to say, if a franchisee was not producing sales within 120 days, he should be in and out. He should be terminated within that period of time, if he was not producing sales. The situation fluctuated as far as the termination of franchisees. At times, it would go full blast, and at other times it would ease off. If we were having a lot of legal problems, generally, we would ease off. At other times, I got the word that I was to accelerate the terminations because we were running out of areas to sell (O'Flaherty, Tr. 432–33).

Mr. O'Flaherty's testimony about respondents' policy of employing form letters whenever possible reveals respondents' cynicism and consciousness with regard to the ultimate failure of their victims:

Q. Did you receive any instructions from anybody as to what manner you were to respond to franchisee problems and questions?

A. There was an elaborate system of form letters used within the company. It was company policy, as related by Mr. Heater, that these form letters and form paragraphs for insertion in form letters were to be used whenever possible. And it was told to me on several occcasions that we should try to avoid directly answering problems and questions if a franchisee had a particular question, why don't you do this, this is happening to me, you don't answer them. You send them out a form letter and ask them a question, so that you put him on the defense (O'Flaherty, Tr. 414–15).

* * * * * * *

A. The form letters consist of the statement of Mr. Heater to me was, the purpose of form letters is to drive the franchisee into apathy. By continually sending a flow of form letters, he would stop communicating with you (O'Flaherty, Tr. 453).

Furthermore, Mr. O'Flaherty referred to a certain form letter questionnaire entitled "Activity Report and Summary" (CX 214) as follows:

Q. What was the purpose of sending that form to franchisees?

A. There were two purposes. The intended purpose, really, was—again, all of our forms, quite frankly, were designed with the purpose of eventually entrapping the franchisee. Making statements that would commit him.

* * * * * * *

THE WITNESS: The purpose of the form is to find out what he is doing with regards to his franchise. That is to say, how many hours he is spending in the operation of his franchise, how many sales calls he is making, total number of hours he is spending on his franchise, how many leads he's received, how many he's worked, and this type of thing.

BY MR. ARBITMAN:

Q. Why did the company want that information?

* * * * * * *

A. Normally, what we do, we would review the form and look for glaring areas of omission on his part generally speaking. For instance, question #6 asks the question "How many hours would you estimate you have spent making membership presentations?" Well, if he only indicated that he spent two hours, and he wasn't making any sales, generally, he was complaining to us in previous letters that I can't sell, because the program's no good. Then, we would simply write back, the reason you're not selling is you're not making calls, and it's just a question of making calls. We follow the company procedure on that. It should be understood that in my work with the department, at all times, I followed basically what I was supposed to be doing as per instructions from Mr. Heater. So, if he said send out form letters and ask these questions, that's exactly what I did (O'Flaherty, Tr. 439–42).

In this connection, Mr. O'Flaherty testified further:

Q. Did you try to truthfully answer them [franchisees] to the best of your ability?

A. I would. Well, no, that's not accurately correct. That's not the truth. You're asking me for an honest evaluation of the thing, I did not answer them truthfully.

Q. You did not answer them truthfully?

A. I would have to say no. That is to say, I followed company policy. If I were to answer them truthfully, I couldn't answer them, so I followed company policy.

Q. Did you try and solve their problems?

A. I many times did, because my conscience got the better of me, and if it weren't for my conscience, just purely business ethics, if one writes in and asks a question with regards to a subject, one normally expects an answer on it. Now, I realize of course, full well, that the use of form letters is in vogue and has been for some time by large corporate corporations. But we weren't that large, and we could, I think, have afforded the luxury of replying individually to people, but we generally did not. Now, I many times, did reply, and attempted to keep the answer at least somewhat in the same area that he was asking the question. But they generally reflected company policy and company statements (O'Flaherty, Tr. 461–62).

As a result of his experiences, Mr. O'Flaherty submitted an 88-page proposal to Heater containing suggestions and recommendations, which O'Flaherty characterized as "everything conceivable that a normal company would use in its sales promotion activities." As was the case with Mr. Fish's recommendations,

Heater never responded to or acted upon any of his proposals (O'Flaherty, Tr. 422–23).

When Brian MacDonald, who worked in respondents' franchise processing and control department, realized the nature of the deceptive practices being conducted, he decided he "couldn't stomach" what he saw (MacDonald, Tr. 555). He brought to Heater's attention the fact that the company's operation was quite different that what he was told when he was hired. Mr. MacDonald received the following response: "I was told, that one time, not to ask what we could do for the franchisees but to see what they could do for us" (MacDonald, Tr. 556). *Heater never denied having made the statements attributed to him by Fish, O'Flaherty, and MacDonald.*

79. In the regular course of their business, respondents ambiguously utilize terms and phrases, material to a determination of the nature and value of the program, which ordinarily convey a meaning to potential franchisees and members that is contrary to fact.

Respondent Heater admitted some of said terms and phrases do in fact rely upon technicalities and semantics and that "largest credit card clearing house" is used in a misleading fashion (Heater, Tr. 828, 830, 872). He acknowledged that respondents' "earnings projections" were really only "hypotheticals" (Heater, Tr. 796, CXs 47–59): and that representations of "profitable earnings" and urgings to franchise prospects to "act immediately" were in fact made by indirection rather than directly (Heater, Tr. 796, 798, 810).

80. In the course and conduct of their aforesaid business, and at all times mentioned herein, respondent International Credit Card Corporation, also trading as National Credit Service, has been, and respondents Universal Credit Acceptance Corporation, Continental Credit Card Corporation, Heater and Gingold have been, and now are, in substantial competition, in commerce, with corporations, firms, and individuals in the sale of franchises or distributorships to persons interested in establishing their own businesses, and with corporations, firms, and individuals in the sale of credit card services.

Under an expansive definition of "competition" respondents compete with other businesses engaged in the sale of franchises or distributorships to persons interested in establishing their own businesses. The May/June 1969 issue of Franchise Journal lists

81 other advertisers in addition to Continental Credit Card Corporation (CX 43, p. 76), and the July/August 1969 issue of Franchise Journal lists 91 other advertisers in addition to Continental Credit Card Corporation (CX 44, p. 92). More specifically, the testimony of both franchisees and members indicates that respondents are in competition with other credit card operations, such as those of banks (BankAmericard and Master Charge) and other credit operations (American Express, Diner's Club, and Carte Blanche) (Lynema, Tr. 602; Winstead, Tr. 352–53; Krieger, Tr. 200, 225, 226; Tronca, Tr. 655; Labrum, CX 234, at p. 2; Dee, CX 234, at p. 9; Brooks, CX 234, at p. 11; Dorigo, CX 234, at p. 14).

81. The use by respondents of the aforesaid unfair acts and false, misleading and deceptive statements, representations and practices, has had and now has, the capacity and tendency to mislead members of the purchasing public into the erroneous and mistaken belief that said statements and representations were and are true, and into investing substantial sums of money in becoming franchisees to sell respondents' services, and into investing substantial sums of money in becoming members of respondents' program for the use of respondents' services, and into the payment of substantial sums of money by reason of said erroneous and mistaken belief.

CONCLUSIONS

1. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents.

2. Respondent International Credit Card Corporation, also trading as National Credit Service, has been, and respondents Universal Credit Acceptance Corporation, Continental Credit Card Corporation, Heater and Gingold have been, at all times relevant hereto, engaged in interstate commerce within the intent and meaning of Section 5 of the Federal Trade Commission Act.

3. The failure of respondents to notify and refund to persons who acted in reliance upon the statements and misrepresentations, as herein found, all monies expended by such persons, was and is, inherently and unconscionably unfair and deceptive.

4. The retention of funds obtained pursuant to the unlawful scheme disclosed by this record itself constitutes a violation of Section 5 of the Federal Trade Commission Act.

5. The aforesaid acts and practices of respondents, as herein found, including their failure to refund all monies expended by persons who acted in reliance upon respondents' statements and representations, as herein found, were, and are, all to the prejudice and injury of the public, and of respondents' competitors, and constituted, and now constitute, unfair methods of competition in commerce and unfair and deceptive acts and practices in commerce in violation of Section 5 of the Federal Trade Commission Act.

PROPOSED ORDER

Counsel supporting the complaint's proposed order differs from the order issued with the complaint in certain respects, but is within the scope of the original order. The respondents in their proposed findings and order have recommended that in the event the examiner finds the respondents in violation of Section 5 of the Federal Trade Commission Act, that he issue an order in most respects following that proposed by the Commission when it issued the complaint. However, the respondents contend, and submit a lengthy brief in support of their position, that the Commission lacks the power and authority under Section 5 of the Federal Trade Commission Act to issue an order that would direct the payment of, in effect, a money judgment against the respondents. While the respondents are unable to cite any cases to substantiate their position, they attempt to construe counsel supporting the complaint's legal justification in a manner contrary to the position taken by the Commission in *Curtis Publishing Company,* Docket No. 8800, decided June 30, 1971 [78 F.T.C. 1472], wherein the Commission outlined some of the circumstances which could lead to the conclusion that retention by a seller of funds secured through misrepresentation constitutes an unfair act or practice within the meaning of the Act:

> An order granting restitutionary relief could also operate prospectively if it were issued on the basis of a finding by the Commission that a seller's retention of its customers' money or property was an unfair trade practice in and of itself. Such a situation could conceivably occur, for example, where * * * the consumer, as a result of deception or fraud on the part of the seller, pays for a product or service but receives nothing of value in return or receives something that is *either worthless or of only token value.* In such instances the retention of the money or property of consumers may be deemed to be a continuing violation of Section 5, separate and apart from any misrepresentation or deceptive sales scheme which may be utilized by the seller. *And to terminate such a practice an order would of necessity*

require restitution of the money or property unjustly held by the seller. Curtis Publishing Company, F.T.C. Dkt. No. 8800, decided June 30, 1971 (emphasis added). [78 F.T.C. 1472, 1516]

The examiner has difficulty interpreting the Federal Trade Commission Act to be broad enough to permit an order requiring restitution by a respondent where the circumstances are such that there are no procedures of any kind provided for by the Act for the adjudication of just or unjust claims. However, the Commission has stated very broadly in *Curtis* that they have the power to issue this type of order. Therefore, the examiner feels compelled to follow the policy established by the Commission in *Curtis* as a precedent governing the disposition of this proceeding.

ORDER

It is ordered, That respondents Universal Credit Acceptance Corporation, Continental Credit Card Corporation, International Credit Card Corporation, also trading as National Credit Service, corporations, and their officers, and John Clifford Heater, individually and as an officer of Universal Credit Acceptance Corporation and International Credit Card Corporation, and Howard P. Gingold, individually and as an officer of Continental Credit Card Corporation, and respondents' franchisees, agents, representatives, employees, successors and assigns, directly or through any corporate or other device, in connection with the advertising, offering for sale or sale of franchises or credit card services, or any other products or services, or in the operation of any credit card service or other business in commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from directly or by implication:

1. (A) Representing that franchisees will earn or can reasonably expect to earn or receive any stated or gross or net amount of earnings or profits; or representing, in any manner, the past earnings of franchisees unless in fact the past earnings represented are those of a substantial number of franchisees in the geographical area about which such representations are made and accurately reflect the average earnings of said franchisees under circumstances similar to those of the person to whom the representation is made.

(B) Representing that franchisees can expect to remain active franchisees for many years; or representing, in any manner, the longevity or tenure of past or existing fran-

chisees unless in fact the periods of time represented are those for which a substantial number of franchisees actively pursued membership sales efforts.

(C) Selling, or offering franchises for sale, in any manner, without disclosing clearly and conspicuously in writing at or before the time of the first oral sales presentation, or in the event no oral sales presentation is made, reasonably prior to the execution of a franchise application, agreement or contract:

(i) the median and mean gross earnings from the sale of memberships in respondents' program by franchisees in the most recent calendar year (who were active for the entire year) preceding the year in which such sale or offer is made;

(ii) the total number of franchisees in the most recent calendar year preceding the year in which the sale or offer is made;

(iii) the total number of franchisees in subparagraph (ii) above who had earnings from the sale of memberships during the designated year in the following dollar amounts:

a. $1,000 or less
b. over $1,000 but not over $5,000
c. over $5,000 but not over $10,000
d. over $10,000 but not over $20,000
e. over $20,000

(iv) the number of franchisees referred to in subparagraph (ii) above who sold memberships for the following periods of time:

a. 1 year or less
b. over 1 year but not over 2 years
c. over 2 years but not over 3 years
d. over 3 years but not over 4 years
e. over 4 years

(v) the total number of members submitting credit charges in respondents' program during the most recent calendar year preceding the year in which the sale or offer is made;

(vi) the number of members referred to in subparagraph (v) above who submitted credit charges under respondents' program for the following periods of time:

a. 1 year or less
b. over 1 year but not over 2 years
c. over 2 years but not over 3 years
d. over 3 years but not over 4 years
e. over 4 years

(vii) the percentage of credit charges recoursed to members during the most recent calendar year and the full number and nature of reasons for which respondents may recourse charges;

(viii) the name and current address of each of respondents' franchisees in the most recent calendar year preceding the year in which such sale or offer is made;

(ix) a financial statement reflecting respondents' assets and liabilities (stating separately fixed assets and liquid assets) for the most recent calendar year;

(D) Selling, or offering memberships for sale, in any manner, without disclosing clearly and conspicuously in writing at or before the time of the first oral sales presentation, or in the event no oral sales presentation is made, reasonably prior to the execution of any application, agreement or contract:

(i) the percentage of credit charges recoursed to members during the most recent calendar year preceding the year in which the sale or offer is made and the full number and nature of reasons for which respondents may recourse charges;

(ii) the total number of members submitting credit charges in respondents' program during the most recent calendar year preceding the year in which the sale or offer is made;

(iii) the number of members referred to in sub-paragraph (ii) above who participated for the following periods of time:

a. 1 year or less
b. over 1 year but not over 2 years
c. over 2 years but not over 3 years
d. over 3 years but not over 4 years
e. over 4 years

(iv) a financial statement reflecting respondents' assets and liabilities (stating separately fixed assets and liquid assets) for the most recent calendar year.

Provided, however, That in the event respondents operated or used any corporate or trade name for a period of less than five years, the disclosures called for in this paragraph shall reflect the operations of the last preceding business entity used by respondents to sell and administer franchises and memberships.

2. Selling, or offering franchises for sale, in any manner, without furnishing to each prospective purchaser reasonably prior to the execution of a franchise application or agreement, a copy of the Federal Trade Commission Consumer Bulletin No. 4, "ADVICE FOR PERSONS WHO ARE CONSIDERING AN INVESTMENT IN A FRANCHISE BUSINESS."

3. (A) Representing that persons do not risk any loss of money in coming to respondents' offices, or any other place, for a franchise interview, or that respondents authorize the reimbursement of air fare expenses for such interviews, without disclosing clearly and conspicuously in writing prior to the expenditure of any funds by such persons, all conditions which must be met to receive reimbursement, including the exact amount of any deposit or downpayment required.

(B) Failing to reimburse travel expenses to any person respondents have promised such reimbursement.

4. Representing that persons do not risk losing the deposits or downpayments submitted with applications for franchises; or that such deposits or downpayments are refundable when such deposits or downpayments may be forfeited if the applicants withdraw or fail to pay the balance due after acceptance of their applications by respondents, or for any other reason;

Provided, however, That respondents may make such representations if they do in fact refund such deposits.

5. Misrepresenting that any geographical area offered as a franchise has not been previously franchised by respondents or misrepresenting that such area has been franchised before by respondents and was profitable for the prior franchise holder.

6. Misrepresenting that respondents have a franchise committee which actually checks the qualifications of prospective franchisees, or misrepresenting, in any manner, that respondents check, or have checked the qualifications of a prospective franchisee.

7. Misrepresenting that respondents have a regional man-

ager who will interview, or has interviewed, prospective franchisees for a particular geographical area; or that respondents have applications pending for a particular area; or that any person must act immediately to be considered for a franchise; or misrepresenting, in any manner, the nature and extent of interest of others in any particular franchise, or franchises in general.

8. Representing that franchise holders receive substantial benefits from renewals of memberships or from annual bonuses based on a percentage of net credit charges submitted by members; or representing, in any manner, benefits to franchisees which are dependent upon the actions of members, unless the benefits represented are those received by a substantial number of franchise holders.

9. (A) Representing that persons risk losing little or nothing in investing in a franchise; or that respondents will repurchase any franchise.

(B) Representing that respondents will aid or assist in the resale of franchises without contemporaneously, clearly and conspicuously disclosing the nature of such assistance and the amount of the resale purchase price which respondents will retain.

(C) Representing that respondents' franchises are vested property rights which may be sold, assigned, transferred or testated, without contemporaneously, clearly and conspicuously disclosing that franchises are subject to termination by respondents if a franchise holder does not produce a prescribed sales quota.

10. Representing, in any manner, that respondents' program has received national acceptance, or that respondents' program can be sold with ease; or misrepresenting in any manner, the salability or degree of acceptance or approval of respondents' program.

11. (A) Representing that credit charges submitted under respondents' program are guaranteed payable or are payable without recourse; or that respondents assume the risk of nonpayment by members' customers in any manner including, but not limited to, using the terms "we honor all approved major credit cards," "honor all credit cards," "non-recourse," "without recourse" or any other terms or words of similar import or meaning.

(B) Representing that all members can expect to be successful or satisfied with the performance of respondents' program; or that members usually continue using respondents' program for two years and renew their contracts thereafter.

12. Using or disseminating any article written or prepared by respondents and published substantially verbatim in any newspaper, magazine, or other publication.

13. Using any letter, payment check, or other materials which purport to represent the satisfaction or success of any franchisee or member unless,

(A) such franchisee or member is actively selling or using respondents' program or service at the time such letter, payment check, or other materials are used;

(B) the full name and current address of the franchisee or member and the existence of any remuneration are disclosed clearly and conspicuously in conjunction with the use of such letter, payment check or other materials;

Provided, however, That respondents shall not obtain or use any such letter, payment check or other material relating to any franchisee or member who has not sold or participated in respondents' program or service for at least six (6) months.

14. Representing that respondents' program costs members little or nothing at all; or that the program costs members half as much as trading stamps; or misrepresenting, in any manner, the cost of respondents' program to members.

15. Representing that members complete just one simple form for all credit charges; or misrepresenting, in any manner, the procedures necessary to process credit charges and receive payment therefor; or failing to disclose contemporaneously, clearly and conspicuously any and all reasons which will preclude receipt of full payment of credit charges submitted by members.

16. Representing that members receive payment for each credit charge submitted to respondents in 30 days; or misrepresenting, in any manner, the period of time in which members will receive payment for credit charges submitted to respondents.

17. Failing to disclose clearly and conspicuously that re-

spondents' program or service is not approved or endorsed by the individual issuers of the credit cards approved by respondents.

18. Representing that members are assured or can achieve a minimum 10 percent or any other percentage or amount of increase in business using respondents' program, without disclosing the number of members who have actually received said increase and offering to identify such members on request, and without maintaining verified statements from said members that they have received said increases.

19. (A) Using the name Fair Trade Bureau or any other name which represents that respondents' operations and activities have been endorsed by any independent or governmental organization.

(B) Writing, preparing, or disseminating any Better Business Bureau reports concerning respondents' business.

20. (A) Representing that every credit charge submitted by members is subject to the most intensive collection procedure in the credit industry; or misrepresenting, in any manner, the intensity or nature of respondents' collection activities.

(B) Using the name North American Collections or any other trade name or collection agency similarly related to respondents without disclosing contemporaneously, clearly and conspicuously that such name or agency is owned, operated or controlled by respondents.

21. Representing that respondents will institute legal action against inactive members whose accounts respondents claim are in arrears, unless respondents do intend to pursue such remedies and have in practice pursued such remedies against substantial numbers of members.

22. Furnishing, or otherwise placing in the hands of others, the means or instrumentalities by or through which the public may be misled or deceived in the manner or as to the things prohibited by this order.

It is further ordered, That respondents incident to selling their franchises and credit card services:

a. Inform orally all persons to whom solicitations are made and provide in writing in all applications and contracts in at least ten-point bold type that the application or contract may

be cancelled for any reason by notification to respondents in writing within seven days from the date of execution.

b. Refund immediately all monies to (1) all persons who have requested cancellation of the application or contract within seven days from the execution thereof, and (2) all persons who paid any monies for franchise fees, deposits or downpayments on franchises, air fare or other expenses for a home office interview, and for membership fees, membership dues and discount fees, who show that any of respondents' solicitations, applications, contracts or performance were attended by or involved any violation of any of the provisions of this order.

It is further ordered, That respondents herein shall within 30 days of the effective date of this order:

a. Mail or deliver a confirmed, return receipt requested copy of this order to cease and desist to all persons from whom respondents obtained any monies for the actual or prospective sale of any franchise or membership and all persons who incurred travel expenses pursuant to respondents' solications from January 1, 1967, until the effective date of this order. Furthermore, respondents shall send with each aforementioned copy of this order a letter or other written statement which effectively notifies such persons of their rights and obligations under section (b) of this paragraph.

b. Refund immediately to all persons described in section (a) of this paragraph filing a written and documented claim therefor with respondents within 30 days of their receipt of this order as set forth in section (a) of this paragraph, who show that respondents' solicitations, applications, agreements, contracts or performance were attended by or involved any of the practices, including, but not limited to, deceptive nondisclosure, which are now prohibited by this order, all monies paid: (1) for air fare or other expenses for a home office interview; (2) for a deposit or down payment on a franchise; (3) for a franchise fee (with any monies earned by franchisees from commissions on the sale of memberships to be deducted after respondents refund to any members sold by such franchisees all monies as set forth in part (4) of this section); and (4) for membership fees, membership dues, and members' discount fees.

It is further ordered, That the respondents shall forthwith deliver a copy of this order to cease and desist to all present and future salesmen and franchisees or other persons engaged in the sale of respondents' franchises and services, and secure from each such salesmen, franchisee or person a signed statement acknowledging receipt of said order.

It is further ordered, That the respondent corporations shall forthwith distribute a copy of this order to each of their operating divisions.

It is further ordered, That the respondents notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondents such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of the order.

It is further ordered, That the respondents herein shall, within sixty (60) days after service upon them of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have compiled with this order.

OPINION OF THE COMMISSION

BY JONES, *Commissioner:*

I.

In a complaint issued on October 6, 1970 [1] respondents Universal Credit Acceptance Corporation (Universal), Continental Credit Card Corporation (Continental), International Credit Card Corporation (International),[2] also trading as National Credit Service (National), John Clifford Heater, individually and as an officer of Universal and International and Howard P. Gingold, individu-

[1] For the purposes of this opinion the following abbreviated citations will be used:

Transcript of Hearing	Tr.
Complaint Counsel's Exhibits	CX.
Respondents' Hearing Brief	R.H.B.
Initial Decision	I.D.
Appeal Brief of Counsel Supporting the Complaint	C.C.B.
Appeal Brief of Counsel Opposing the Complaint	R.B.
Addendum to Appeal Brief of Counsel Opposing the Complaint	R.Ad.B.
Answering Brief of Counsel Supporting the Complaint	C.C.A.B.
Transcript of Oral Argument	T.O.

[2] Universal, Continental and International are each incorporated under the laws of the State of California. (I.D. 1-3 [p. 582 herein]).

ally and as an officer of Continental, were charged with violating Section 5 of the Federal Trade Commission Act.

The complaint charged respondents with having engaged in unfair methods of competition and unfair and deceptive acts and practices in the marketing and operation of their "Honor All Credit Card" program.

The administrative law judge found that respondents represented they would honor all credit cards used by the customers of their retail merchant program members "on a guaranteed nonrecourse basis" and that members would be paid within thirty days whether or not the customers paid respondents.[3] In fact, respondents' program was fully recoursable and respondents' retail members were not paid until and unless their customers paid respondents and then only after 45 days and sometimes not until 75 days later.[4] Additionally, the law judge found that respondents guaranteed their members a 10 percent increase in business within 12 months of becoming a member. (I.D. 67 [p. 624 herein]) However, this guarantee turned out to be simply a promise to waive membership dues for the second year. (I.D. 67) In fact, the average member remained active in the program for only 7–8 months despite the fact that they had paid a two-year membership fee. (I.D. p. 3 [p. 583 herein], I.D. 57 [p. 620 herein], I.D. 68 [p. 624 herein]).

Respondents also represented that their program was operated by substantial businessmen who could rely on corporate assets in excess of three million dollars, that it was backed by an efficient and intensive collection agency and that it was nationally accepted. (I.D. 45 [p. 612 herein], I.D. 65 [p. 623 herein], I.D. 72 [p. 626 herein]) The administrative law judge found, however, that respondents' collection procedures were at best haphazard, that in January 1969 respondents had a net working capital deficit of more than $25,000 and that respondents' bank accounts never exceeded $99,000 between January 1965 and November 1971. (I.D. 66 [p. 623 herein], I.D. 73 [p. 626 herein]) The law judge further found that there was no national acceptance for the program, that

[3] I.D. 49 [p. 614 herein] and I.D. p. 3 [p. 583 herein]. At page 3 of his initial decision, the administrative law judge included a section entitled "Nature of Respondents' Business and Business Methods." While he did not denominate this section specifically as a part of his findings of fact, nevertheless, the facts recited in this section are fully supported by the record. Some of the facts recited by the law judge in this section are reiterated in his findings and others are documented in complaint counsel's proposed findings which we are adding to the law judge's findings. See, *infra*, p. 7 note 7 [p. 646 herein].

[4] I.D. 50 [p. 618 herein] and I.D. p. 3; see note 3 *supra*.

the members failed to remain active in the program for the period covered by their contracts and that the bulk of respondents' substantiating data purporting to prove the worth of the program were in fact written by respondents and merely repeated respondents' advertising claims. (I.D. 46 [p. 612 herein], I.D. 70 [p. 625 herein], I.D. 71 [p. 625 herein]).

Representations made by respondents to prospective franchisees, in addition to those about the operation and benefits of the program, were found by the administrative law judge to be equally false. (I.D. 21 [p. 591 herein], I.D. 23 [p. 591 herein], I.D. 81 [p. 632 herein]). The administrative law judge found that prospective franchisees were induced to visit respondents' California headquarters to review the program on the belief their air fare expenses would be reimbursed whether or not they decided to submit a franchise application. (I.D. 31 [p. 601 herein]). Further, he found that air fare reimbursement was in fact contingent upon submitting a franchise application and that franchisees were otherwise pressured into submitting franchise applications quickly for consideration by respondents' franchise committee together with their deposit of $1,000 on the belief their deposit was refundable. (I.D. 32, I.D. 33 [pp. 603–05 herein], I.D. 37, I.D. 39 [pp. 608, 610 herein]). In fact, the administrative law judge found that respondents only bound themselves to refund deposits if applications were rejected, that respondents did not have an operating franchise committee, that no franchise application was ever rejected and consequently no deposits were ever refunded. (I.D. 31–34 [pp. 601–05 herein], I.D. 38 [pp. 609–10 herein]). Franchisees were further led to believe that the program was easy to sell, that they could earn as much as $80,000 a year and that each would receive either an exclusive and wholly-unworked territory or one which had been profitable for a prior franchisee. (I.D. 26 [p. 593 herein], I.D. 35 [p. 605 herein]). In fact respondents' records establish that no franchisee earned the amounts indicated on the earning projection sheets shown to prospective franchisees and that the same franchise territories were often resold to as many as 8 franchisees. (I.D. 27 [p. 595 herein], I.D. 35, I.D. 36 [pp. 605–08 herein]).

On the basis of these findings, the administrative law judge concluded that each of the respondents was liable for the deceptions as alleged and that the deceptions constituted unfair methods of competition and unfair and deceptive acts and practices in viola-

tion of Section 5 of the Federal Trade Commission Act. He also concluded that the deceptions prejudice and injured the public and respondents' competitors and that respondents' retention of funds gained through their deceptions and misrepresentations also constituted a violation of Section 5 of the Federal Trade Commission Act. The administrative law judge entered an order prohibiting each of the respondents from engaging in specified deceptive acts and practices in the future, requiring respondents in the future to provide each of their franchisees and members with a seven-day cooling-off period within which to cancel any franchise application or membership contract, requiring respondents in the future to refund monies obtained as a result of a violation of the order and directing respondents to refund all monies paid to respondents by its franchisees and retail merchant members for franchisee fees, downpayments or travel expenses incurred in connection with franchise applications and membership fees, dues and discount fees during the period from January 1, 1967, to the effective date of this order.

Both complaint counsel and respondents have appealed from the initial decision. Complaint counsel appeal from the law judge's failure to make certain findings which complaint counsel contend were necessary to support his proposed order.[5] Respondents' appeal was limited to the single issue of the propriety of the provisions of the law judge's order which required a refund of monies which they retained.[6]

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[5] These additional proposed findings are to be found at pp. 6–25 of complaint counsel's initial appeal brief. Requested findings numbered 1 through 9 relate to the failure of the respondents to disclose to their members certain material facts which were essential in order to evaluate respondents' representations about the worth of the program and to understand the procedures for submitting credit charges, the deceptiveness of respondents' purportedly objective and unbiased items of promotional material such as articles and payment checks, respondents' misrepresentations of the length of time in which members would be paid and respondents' indiscriminate threats of legal action against members whose accounts were in arrears. The other findings (Nos. 10–15) are designed to make explicit facts which are implicit in the law judge's opinion; that respondents were responsible for the acts of their franchisees whom they exploited to further their own devious purposes, that respondents were fully aware of the deceptive nature of the representations made about their worthless program and indeed framed their membership contracts and franchise agreements deliberately to mislead and deceive and that respondents have never refunded any monies obtained through their deceptions.

[6] Respondents' appeal as outlined in their appeal brief was confined to two arguments in support of their contention as to the propriety of the refund provision, namely that the Commission lacks the power to order refunds and that it would be inappropriate to order the individuals to make refunds as they received no income in their individual capacities. At the oral argument respondents raised new contentions, not discussed in their appeal briefs or raised below before the law judge, that the order was inappropriate because of pending court proceedings which rendered the relief moot and unnecessary because of respondent Heater's alleged psychological incapacitation. The Commission granted respondents permission to file certified copies of pertinent papers to support the various factual assertions they were making

We have carefully reviewed the record in this case which is not contested by the respondents on this appeal.[7] We conclude that the administrative law judge's findings and conclusions on the substantive liability of each of the respondents is fully supported by the evidence. We also conclude that the 15 additional findings contended for by complaint counsel, and also not contested by respondents on their appeal, are supported by substantial evidence, provide further support for the proposed order and should, therefore, be added to the findings already made by the law judge.[8]

We agree with the provisions of the law judge's order prohibiting respondents from engaging in future deceptions or misrepresentations with respect to the program, requiring respondents to provide members and franchisees with a cooling-off period and requiring respondents in the future to refund monies obtained in violation of the order. These order provisions are not challenged by respondents and we agree with the law judge that they are essential relief to ensure that the unfair and deceptive acts and practices of respondents are to be terminated effectively.

The sole issue for discussion on this appeal concerns respondents' contentions that an order requiring respondents to refund the monies which the law judge found they had illegally retained in violation of Section 5 is beyond the power of the Commission to order, rendered moot because of intervening court proceedings seeking relief against the same activities and the adjudgment of bankruptcy against the corporate respondents and unnecessary and unjust as respects the individual respondents. We will consider these arguments *seriatim*.

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on oral argument. Respondents filed such papers together with an additional brief to support their contentions and complaint counsel filed a response. For the purposes of this opinion these post oral argument materials will be referred to in the following manner:

Respondents' Post Argument Filings	R.F.
Response to Respondents' Filings	C.C.R.
Response to Counsel for Federal Trade Commission Response	R.A.

[7] The brief which respondents submitted to the administrative law judge stated that argument was "limited to the issue of refunds or restitution only, as respondents are now and always have been, ready, willing and anxious to correct any written or oral statement which may tend to mislead a prospective franchisee or member." (R.H.B. p. 17) Similarly, argument in respondents' appellate briefs were limited to the provisions of the order requiring a refund of monies respondents retain. During oral argument respondents' counsel stated: "Now, I don't want to concede the other issues but that [restitution] is the only one I want to address myself to." (T.O. p. 14) No statement was made challenging any other provision of the law judge's order nor was there any challenge to any of the findings of fact made by the law judge or any of the additional findings of fact proposed by complaint counsel. Beyond the issue raised by respondents' retention of certain funds, respondents have failed to indicate any "other issues" which are before us on this appeal.

[8] Counsel supporting the complaint contended these factual findings provide additional support for paragraphs 1(D) (i-iii), 12, 13, 15, 16 and 21 of the law judge's proposed order. (C.C.B. pp. 6–25)

II.

The Need For Restitutionary Relief

Central to the propriety of the restitutionary relief being challenged here is the law judge's findings and conclusions—which respondents did not challenge—that respondents' retention of the monies procured from the victims of their fraudulent credit card program constituted a violation of Section 5 of the Federal Trade Commission Act. (I.D. pp. 55–56 [pp. 632–33 herein]) In his discussion of the propriety of the refund relief which he ordered, the law judge summarized his views of respondents' program in these words:

> What the record establishes is that these respondents have perpetrated a scheme fraught with misrepresentations from which they try to insulate themselves by using devious contractual language, not intended or likely to be read and not clearly understandable, even if actually read. Respondents have cleverly calculated the program to enrich only themselves at the expense of innocent small businessmen lured into it as members and franchisees. (I.D. p. 3 [p. 584 herein])

Discussing the fraudulent and worthless nature of the services which the program purportedly offered its members and franchisees, the law judge pointed out that instead of being protected from the risk of loss and avoiding the administrative problems connected with handling the accounts receivable of their credit card customers as represented,

> Members soon discover that respondents avoid paying charges which they can't collect by citing one or more of *at least* 18 different reasons why they are not obligated to pay. Members also discover that, rather than receiving payment for charges within 30 days from the date they are submitted, payment is not received until anywhere from 45 to 75 days later. As a result of this treatment and despite the fact that they signed a two-year contract, member merchants give up in despair and, swallowing their losses, stop using the program after about seven or eight months on the average. Typically, in addition to having paid what is not an insignificant sum for a service that was never delivered members have, in fact, risked and lost money for charges recoursed by respondents. (Emphasis in original) (I.D. p. 3[p. 583 herein])

The law judge concluded that respondents' failure to refund all monies expended by such members and franchisees was "inherently and unconscionably unfair and deceptive" and together with respondents' retention of such monies violated Section 5 of the Federal Trade Commission Act. (I.D. pp. 55–56 [pp. 632–

33 herein]) His proposed order directed respondents, among other things, to refund monies thus illegally received and retained.

We have no doubt as to the correctness of the law judge's conclusion that the respondents' retention of the monies secured through their unconscionable practices and misrepresentations and their failure to refund these monies constituted violations of Section 5 of the Federal Trade Commission Act.

A fundamental and centrally important feature of the Federal Trade Commission Act is the broad power which Congress intentionally conferred on the Commission to define the specified trade practices which were to be prohibited under its generalized proscription against unfair and deceptive acts and practices.[9]

The courts have consistently recognized and approved the intentional design of Congress to delegate to the Commission broad powers to develop the term "unfair" rather than define itself "the many and variable unfair practices which prevail in commerce * * * ." [10] The Supreme Court has described the nature of this broad Congressional mandate in these words:

> Neither the language nor the history of the [Federal Trade Commission] Act suggests that Congress intended to confine the forbidden methods to fixed and unyielding categories.
>
> Congress, in defining the powers of the Commission, thus advisedly adopted a phrase [unfair methods of competition] which, as this Court has said, does not "admit of precise definition but the meaning and application of which must be arrived at by what this Court elsewhere has called the 'gradual process of judicial inclusion and exclusion'." [11]

In a later case the Supreme Court again observed: "In thus divining that there is no limit to business ingenuity and legal gymnastics, the Congress displayed much foresight." [12]

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[9] The House Report recommending the enactment of the original FTC Act was explicit on this point. As the Report pointed out:

"It is impossible to frame definitions which embrace all unfair practices. There is no limit to human inventiveness in this field. Even if all known unfair practices were specifically defined and prohibited, it would be at once necessary to begin over again. If Congress were to adopt the method of definition, it would be an endless task." H.R. Rep. No. 1142, 63rd Cong. 2d Sess. 18–19 (1914)

[10] *Atlantic Rfg. Co.*, 381 U.S. 357, 367 (1965) (citations omitted). See also, *Sears, Roebuck & Co.* v. *F.T.C.*, 258 Fed. 307, 311 (1919) in which the Seventh Circuit early observed about the Federal Trade Commission Act:

"This statute is remedial, and orders to cease and desist are civil; but even in criminal law, convictions are upheld on statutory prohibitions of 'rebates or concessions' or of 'schemes to defraud' without any schedule of acts or specific definition of prohibited conduct, thus leaving the courts free to condemn new and ingenious ways that were unknown when the statutes were enacted."

[11] *F.T.C.* v. *Keppel & Bros.*, 291 U.S. 304, 310–312 (1934).

[12] *Atlantic Rfg. Co., supra*, 381 U.S. at 367; see also, *F.T.C.* v. *Motion Picture Advertising Service Co., Inc.*, 344 U.S. 392, 394 (1953).

Most recently, the Supreme Court has again underscored this essential feature of the Commission's powers with respect to unfair or deceptive practices. Thus in *F.T.C.* v. *Sperry & Hutchinson Co.*, 405 U.S. 233 (1972), the Supreme Court observed that:

> legislative and judicial authorities alike convince us that the Federal Trade Commission does not arrogate excessive power to itself if, in measuring a practice against the elusive, but congressionally mandated standard of fairness, it, like a court of equity, considers public values beyond simply those enshrined in the letter or encompassed in the spirit of the antitrust laws. 405 U.S. at 244.[13]

In the instant case, respondents' program which was entirely fraudulent in every aspect and which was competitive with the credit card issuance business generally, has been systematically promoted since 1953. (I.D. 7 [p. 585 herein])[14] Minimally some 600 franchisees[15] and 6500 retail member merchants[16] were victimized by respondents' program. Each of these franchisees paid approximately $7500 for the franchise and the retail merchant program members each paid $240 for a two year membership in addition to monthly dues of $10 and a 6 percent discount to respondents on sales made under the program. (I.D. 14 [p. 589 herein], 57 [p. 620 herein]) For the fiscal years ending June, 1967, 1968 and 1969 alone respondents received some $3,042,255 from their franchisees and members while the overwhelming

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[13] *F.T.C.* v. *Colgate-Palmolive Co.*, 380 U.S. 374, 385 (1965); *F.T.C.* v. *Brown Shoe Co.*, 384 U.S. 316, 320–21 (1966); *F.T.C.* v. *Texaco*, 393 U.S. 223, 225–26 (1968).

[14] The administrative law judge found that the testimony of both franchisees and members indicated that respondents were in competition with other credit card operations such as those of banks and other credit operations. (I.D. 80 [p. 631 herein]) He also found that Continental advertised in a magazine entitled Franchise Journal in an effort to attract franchises. (I.D. 80) Additionally, the law judge found that from January 1, 1967 to October 1969 respondents received $1,291,703.90 for the sale of franchises. (I.D. 27 [p. 595 herein]) Income from membership fees, dues and members' discounts from June 1966 to June 1969 totaled $1,846,785. (I.D. 16 [p. 590 herein])

[15] *See, Headley* v. *Continental*, No. C–70–457 SW (N.D. Cal. August 1972), discussed *infra* at p. 30 [p. 659 herein], n. 29.

[16] Between August 1969 and February 1971 there were at least 1,100 members under contract at a given time; there was a membership turnover during this period of at least 30 a month; and the program has operated in substantially the same form and manner since 1953. (Tr. 121–122, I.D. 6 [p. 585 herein]) A rough computation based on these facts would place the total number of members since 1953 until the issuance of the complaint at about 6500 merchants.

majority of these franchisees [17] and members [18] suffered substantial losses by reason of their participation in the program. (CXs 122–124) As the law judge put it:

* * * Respondents have cleverly calculated the program to enrich only themselves at the expense of innocent small businessmen lured into it as members and franchisees. (I.D. p. 3 [p. 584 herein])

Respondents here are not in the situation where they were engaged in the business of offering a service or product of some intrinsic value but which they were promoting through unfair or deceptive means. The essence of the unfairness and deception which they perpetrated inheres in the program which they offered. To take monies under false pretenses and to retain these monies under color of law, while casting the fraud in the form of a legitimate business operation purporting to offer the participants an opportunity to make money or to improve their own business opportunities is the height of unfairness and deception. To offer a virtually worthless service to small businessmen and individuals desiring to go into business, however, is to adopt a cloak of legitimacy designed to take advantage of the free enterprise culture and create an impression on the part of their victims that that which they lost was simply a normal business risk or the

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[17] A review of respondents' business records from January 1, 1967 to October 1969, (CX 190 A–Q) indicates that there were 172 franchisees during these months and that they remained active in the program for 8 to 9 months. (Activity was measured from the date of the franchise agreement to the date of the last earnings statement submitted to respondents). The average amount paid for the franchise was $7,509.91 while the average earnings of each franchisee was $1,448.91. Thus, franchisees lost approximately 81 percent of their earnings. (I.D. 27 [p. 595 herein]) Additionally, 97 percent of these franchisees failed to earn back their initial investment and no franchisee earned the amounts shown on respondents' franchisee earning projection sheets. (I.D. 27 [p. 595 herein]) Only 3 out of these 172 franchisees made any profit at all. (CX 190E #59, CX 190D #47, CX 190A #2) In contrast, for the fiscal years ending June, 1967, 1968 and 1969 respondents earned from the sale of franchise rights $149,286, $570,572 and $475,632 respectively. (CXs 122–124)

[18] Members remained active in the program approximately 8 months although each had paid for a two-year membership. (Tr. 127–128) Between July of 1966 and June 1969 the small independent retailers who were members sustained recourses on sales made under the program of approximately 14 percent. Thus, for very $100 in sales made under the program, the member would suffer an outright loss of $14. (CXs 122–125) This same retailer would simultaneously have to pay respondents a 6 percent discount on all sales made under the program and $10 monthly dues beyond the $240 already paid for a two-year membership. (I.D. 57 [p. 620 herein]) Accordingly, over 40 percent of the members who received either checks or financial statements from respondents between January 1968 and October 1969 were informed that they were indebted to respondents. (CX 191) During the hearing, one franchisee testified that in a written survey of the retailers to whom he had sold memberships 58 answered a question as to how much money they had lost; their responses totaled $26,126.30. (Tr. 666) One other franchisee testified that of the 64 memberships he had sold, retailers, on the average, lost $400 to $500. (Tr. 353–355) In contrast for the fiscal years ending June, 1967, 1968 and 1969 respondents earned by way of membership dues, fees and members discounts $457,184, $694,375 and $695,226 respectively. (CXs 122–124)

product of their own ineptitude or lack of astuteness rather than the consequences of a fraud against which they might have had a cause of action.

We agree with the law judge, therefore, that respondents' retention of these monies which they had obtained solely as a result of their offering of a virtually worthless service and their failure to refund the monies which they took from their members and franchisees is a substantive violation of Section 5.

We believe that the law judge was entirely correct in ordering respondents to refund these monies and that indeed such remedy is essential if adequate relief is to be secured here to protect the public from possible continuation or recurrence of the perpetration of such frauds on the public by any of these respondents.

In our opinion in *Curtis Publishing Co.*, 3 CCH Trade Regulation Reporter ¶19,719 (June 30, 1971) [78 F.T.C. 1472, we described the circumstances under which an order requiring restitution would be required by Section 5. We noted that:

> [i]t may well be that in some situations injury to competition resulting from the deceptive practice cannot be adequately remedied by an order which merely enjoins the practice. In such a case refunding of the money obtained by illegal means may be the only effective method of restoring the competitive *status quo* which was disrupted by the deceptive practices. (3 CCH T.R.R. at page 21, 758 [78 F.T.C. 1472, 1515])

Additionally, we stated that:

> a seller's retention of its customers' money or property * * * [may be] an unfair trade practice in and of itself. Such a situation could conceivably occur * * * where the consumer, as a result of deception or fraud on the part of the seller, pays for a product or service but receives nothing of value in return or receives something that is either worthless or of only token value. In such instances the retention of the money or property of consumers may be deemed to be a continuing violation of Section 5, separate and apart from any misrepresentation or deceptive sales scheme which may be utilized by the seller. (3 CCH T.R.R. at page 21,758 [78 F.T.C. 1472, 1516])

The law judge found that respondents' credit card program competed with those firms engaged in the business of issuing credit cards. There is little doubt that a service purporting in effect to guarantee all credit cards is essentially competitive with the service offered by credit card issuers themselves. Thus credit card issuers compete among themselves for the merchants' business through the service fees charged, the speed with which they pay

the merchant, their recourse provisions and other like provisions. Obviously any company offering to put itself, in effect, in the place of the card issuer *vis-a-vis* the merchant is competing with the card issuers themselves. Any differences in services offered by different credit card issuers which would otherwise be of competitive significance are nullified and cancelled out by a program which purports to honor all credit cards on a non-recourse basis, make immediate payments to the merchants and perform all necessary collection services as well.

It is a universally recognized principle of relief in restraint of trade cases to require the respondent wherever possible to restore the competitive balance which existed prior to his illegal practices. Thus companies which make illegal acquisitions are typically required to divest themselves of the illegally acquired assets. See, *e.g., L. G. Balfour* v. *F.T.C.*, 442 F.2d, 1 (7th Cir. 1971); *F.T.C.* v. *Procter & Gamble Co.*, 386 U.S. 568 (1967).

That basic thrust of relief is just as applicable to distortions of competitive balance which result from the type of deceptive or unfair practice involved in the instant case as it is to similar competitive imbalances resulting from more traditional restraints of trade activities. If the businessman who has engaged in the deceptive or unfair practices has been so successful as to significantly disrupt the balance of competition, an order which merely prohibited future deceptions or misrepresentations would permit him the use of funds to further his fraudulently obtained competitive advantage. Similarly, if the businessman is permitted to retain substantial funds obtained as a result of deception or fraud, the consuming public will have been deprived of the opportunity to place these funds in legitimate competitive activities and the businessman will be able to utilize these funds for further ventures. Thus a mere order to "sin no more" would be as ineffective in the circumstances of the types of deceptions found here as it would in the case of an illegal acquisition. It is therefore evident that under these circumstances restitution is the singularly appropriate—and essential—remedy to vindicate the public injury which is the direct consequence of respondents' violation of Section 5.

The instant case, however, provides additional grounds for ordering restitutionary relief against these respondents. The record in this case is replete with evidence of the consistent and conscious efforts which respondents made to clothe their program with an apparent legitimacy and truthfulness while at the same

time building into the program all of the escape hatches necessary to enable respondents to avoid performing on their promises. Thus respondent Heater carefully instructed his salesman that:

> The best way to handle most of the "sticky" phrases in our membership agreements, is to tell the prospect that normally they are not important and are only designed to protect us against members or their employees who sometimes try to take advantage of us. Tell them: "Certainly, our contract or even our all credit card program is not perfect in *all* respects. However, lets not be looking at the hole in the doughnut." (CX 186A) (Emphasis in original)

It is difficult to conceive that an order which simply prohibited respondents from engaging in similar frauds in the future could have any real effect on preventing respondents from devising another illegal business venture to bilk another group of unsuspecting members of the public. If the presence of the Act was not sufficient to prevent respondents from engaging in these blatant violations on this occasion, we can have very little certainty that simply repeating the Act's prohibitions against fraud and deception is slightly more specific language will have any greater restraining effect on respondents' conduct in the future. If, on the other hand, respondents know that they cannot retain the sums of monies which they receive as a result of their violations, they are far less likely in the future to once again flaunt these law's proscriptions in the planning of their next business venture.

At common law equitable remedies for fraud attempted to go to the root of the injury to prevent the defrauder from retaining the fruits of his illegal conduct. (3 Pomeroy's Equity Jurisprudence, 419–20 (5th Ed. Symons, 1941))

The FTC's remedial powers have frequently been likened to those of a court of equity [19] and indeed the administrative process in general is designed to ensure a more flexible approach to law enforcement both as to matters of substantive law definition as well as to matters of devising remedy.[20]

The courts have made it abundantly clear that the Commission is duty bound to devise an appropriate and reasonable remedy to

[19] *Cf., Pan American World Airways* v. *United States*, 371 U.S. 296, 312 n. 17 (1963); *F.T.C.* v. *Sperry & Hutchinson Co.*, 405 U.S. 233, 244 (1972).

[20] It is an established principle of equity jurisdiction that:

"In the administration of remedies, an equity court is not bound by the strict or rigid rules of the common law; on the contrary, the court adapts its relief and molds its decrees to satisfy the requirements of the case * * * It is said that equity has always preserved the elements of flexibility and expensiveness so that the new remedies may be invented or old ones modified * * * to satisfy the needs of a progressive social condition." 27 Am. Jour. 2d—Equity, at 624–25 (1966)

cure violations found to exist and to prevent their recurrence. The central purpose of relief is "to prevent violations of the Act, the threat of which is indicated by past conduct of the petitioners" *Feitler* v. *F.T.C.*, 201 F.2d 790, 794 (9th Cir.), *cert. den.*, 346 U.S. 814 (1953)

Moreover, the Commission through its order "cannot be required to confine its road block to the narrow lane the transgressor has traveled; it must be allowed effectively to close all roads to the prohibited goal, so that its order may not be by-passed with impunity." *F.T.C.* v. *Ruberoid,* 343 U.S. 470, 473 (1952), *F.T.C.* v. *National Lead Co.*, 352 U.S. 419, 431 (1957). Once a violation is found the Commission must "frame its order broadly enough to prevent respondents from engaging in similarly illegal practices in [the] future * * * ." *F.T.C.* v. *Colgate Palmolive Co.*, 380 U.S. 374, 395 (1965); *Atlantic Rfg. Co.* v. *F.T.C.*, 381 U.S. 357, 367 (1965); *F.T.C.* v. *Henry Broch & Co.*, 368 U.S. 360, 364 (1962). Through these orders the Commission is required "to develop that enforcement policy best calculated to achieve the ends contemplated by Congress. * * * " *Moog Industries, Inc.* v. *F.T.C.*, 355 U.S. 411, 413 (1958). We conclude, therefore, that restitutionary relief is essential in this case in order to redress the competitive balance disrupted by respondents' fraudulent program and prevent repetition of these practices in the future.

We turn now to the specific contentions raised by respondents that this form of relief is beyond the power of the Commission to order and in any event inappropriate and unnecessary.

III.

Respondents' Contentions With Respect To The Propriety of a Refund Order

A. *The Commission's Power to Order Refunds*

Respondents argue that whatever may be the need for a refund order, it is beyond the Commission's power to order because such a relief provision is essentially compensatory in nature, operates to redress private rather than public wrongs and is in fact an award of money damages which is generally conceded to be beyond the Commission's power to issue.

We have already discussed at length in our opinion in *Curtis, supra,* the legal basis for the Commission's power to order restitutionary relief. Respondents' contentions with respect to the

impropriety of this relief do not in any way cast any doubt on the legal and factual bases for our conclusion in *Curtis* as to the existence of this power. Respondents argue in their briefs that *Curtis* is wrong since restitutionary relief redresses private wrongs and constitutes an award of money damages and hence is beyond the reach of the Commission's remedial jurisdiction. We disagree.

The cases are clear that the remedy of restitution is an appropriate remedy to redress a public wrong and as thus conceived and used will not be regarded either as a penal measure, an adjudication of a mass tort or as redress of private injury. Thus in *Virginia Electric Co.* v. *Board,* 319 U.S. 533 (1943), the Supreme Court sustained an N.L.R.B. order requiring restitution of dues and assessments after its finding that the company had committed an unfair labor practice through its domination of the union. The court held, despite the company's claim that the union had rendered its members some minimal benefits, that the Board could properly find that the services rendered by the union were, in effect, virtually worthless since a company dominated union was by its nature contrary to the interest of employees and the policies underlying the National Labor Relations Act. Further, the court held that restitution was neither a redress for a private wrong nor penal since the Board was merely vindicating public policy by ordering the company to return money which it retained in its treasury. 319 U.S. at 543–44.[21] Similarly, in *Porter* v. *Warner Co.,* 328 U.S. 395 (1946), the Supreme Court again sustained an order of restitution as an appropriate remedy to redress a public wrong committed by a landlord who had violated the Emergency Price Control Act of 1942. The thrust of the Supreme Court's opinion was that the order of restitution, even though it directed repayment of rent to individual tenants, did not constitute an attempt to redress private injury caused by impermissible rent payments and was not an award of penalties for damages suffered. As the Supreme Court noted:

[21] See also, *Wirtz* v. *Malther, Inc.,* 391 F.2d 1 (9th Cir. 1968), in which the court, in comparing the power of the Secretary of Labor to order employers to pay certain monies due their employees under the Fair Labor Standards Act to the right of the employees to individually recover these funds, stated:

"It must be remembered that restraining appellees from withholding the minimum wages and overtime compensation is meant to vindicate a public rather than a private, right, and that the withholding of the money due is considered a 'continuing public offense.' " (citations omitted) 391 F.2d at page 3.

Cf., McComb v. *Frank Scerbo & Sons,* 177 F.2d 137, 138–139 (2d Cir. 1949); *Walling* v. *O'Grady,* 146 F.2d 422, 423 (2d, Cir. 1944).

Restitution, which lies within that equitable jurisdiction [of a federal district court], is consistent with and differs greatly from the damages and penalties which may be awarded under §205(e). [Citation omittted] When the Administrator seeks restitution under §205(a), he does not request the court to award statutory damages to the purchaser or tenant or to pay to such person part of the penalties which go to the United States Treasury in a suit by the Administrator and §205(e). Rather he asks the court to act in the public interest by restoring the status quo and ordering the return of that which rightfully belongs to the purchaser or tenant. 328 U.S. at 402.[22]

These cases make clear that an order of restitution, simply because it requires that refunds be made to persons from whom the illegally retained monies were originally secured, does not exceed the Commission's power as a redress of private injuries or as an award of damages.[23]

We, therefore, reaffirm our opinion in *Curtis* that the Commission has full power in an appropriate case to order restitution wherever it is clear that such relief is necessary in order to further the public policies which are the foundation of Section 5. The refund order in issue here seeks only to disgorge monies which respondents received and makes no efforts to compensate all persons who may have expended monies in reliance on respondents' spurious claims respecting the value of the program.[24] The

[22] See also, *Bowles* v. *Skaggs*, 151 F.2d 817 (6th Cir. 1945) in which the court in discussing the Emergency Price Control Act of 1942 stated:
"An order of restitution is not a judgment for damages or for penalties. It compels compliance and is restoration of the status quo which falls within the recognized power of a court of equity * * *. The Administrator acts in the public interest—the purchaser in his own. The remedies are not irreconcilable. There are undoubtedly many instances where the relationship of buyer and seller is such that the buyer is deterred from vindicating his own and therefore also the public right. To deny to the Administrator power to act in cases where, as here, restitution rather than a prohibitory injunction is the only practical remedy, would be to subvert the purposes of this Act." 151 F.2d at 821.

[23] Respondents also contended in their brief that commissioners and commentators have recognized restitution as beyond the Commission's power. (R. Ad. B. pp. 11–17) However, it is quite clear from respondents' citations that those Commissioners and commentators whose views are cited for this proposition were in fact focusing their primary attention on the need for Commission authority to order respondents to pay *money damages* to the victims of their frauds and to assess civil penalties against respondents and were not in fact talking about restitution powers. Hence their views are not factually relevant to the issue of the Commission's restitutionary powers to which we are addressing ourselves quite apart from the legal irrelevance of such views to the issue of the Commission's actual powers.

[24] It should be noted that if the refund provisions of the order were designed to award monetary damages for respondents' fraud, the order would fall far short of its goal. Thus the order does not grant to any member or franchisee an award for any incidental damages which were suffered as a direct and reasonably forseeable consequence of respondents' activities. Similarly, there is no provision for calculation of interest a deceived consumer might be entitled. The order does not seek to render the defrauded franchisee or member "whole." Rather the order seeks to redress a violation of Section 5 based on the respondents' retention of funds obtained as a result of their spurious program. See *infra*, pp. 36–44 [pp. 663–68 herein] for a discussion of the refund order provisions to be entered.

exclusively public policy concern of the refund order is further demonstrated by its dual functions here to restore the competitive imbalance resulting where the businessman through deception or fraud retains substantial funds to the detriment of his competitors and the consuming public and to provide essential assurance that the respondents will not in the future continue their violation.

B. *Respondents' Contentions With Respect to Mootness*

Respondents also contend that the refund provisions of the order would be inappropriate with respect to both the corporate and individual respondents because they would be unnecessarily duplicative of or inconsistent with court proceedings which transpired subsequent to the filing of the Initial Decision.[25]

The papers submitted by respondents to support their various assertions confirm respondents' contentions that since the entry of the initial decision each of the corporate respondents has been adjudged bankrupt.[26] It would seem clear that as a result of their bankruptcy—which we assume from the papers reaches all of their assets wherever situated—the corporate respondents named in the instant complaint are no longer retaining any monies secured from their fraudulent program.

We do not believe, therefore, that there is any need to enter a refund order against these corporate respondents. Such an order provision under the circumstances now prevailing would strike us as a vain and futile act. Accordingly, we believe that the corporate respondents must be deleted from any refund order provision to be entered here. The rest of the order proposed by the law judge to be entered against these corporate respondents will remain undisturbed since such relief is obviously essential and we have no information about these respondents which would lead us to conclude that the entry of the balance of the order against them is unnecessary.[27]

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[25] This argument and the facts on which it is based were presented to the Commission for the first time during oral argument. With the permission of the Commission, the respondents thereafter submitted certified copies of the papers relevant to the court proceedings and all parties submitted additional briefs on the new issues thus raised.

[26] *In the Matter of Universal, et al.*, No. 3-72-542 (N.D. Cal., June 9, 1972). On May 25, 1972 an involuntary petition in bankruptcy was filed in a federal district court in California against Universal Credit Acceptance Corporation and Universal Credit Associates, Inc. of California, a corporation, d/b/a Continental Credit Card Corporation. (N.D. Cal., 3-72-542) Thereafter, the corporations named in the petition, in addition to each of the corporate respondents in this action and other named corporations consented to an order in which they were adjudicated bankrupt. (N.D. Cal., 3-72-542, June 9, 1972)

[27] Since we find that the corporate respondents should not be subject to the refund provisions of the order because they have been adjudged bankrupt we do not reach the merits or relevance of respondents' further contention that the refund provisions of the order are inappropriate

The situation with respect to the individual respondents, however, is not affected by the bankruptcy proceeding. Neither of the two individual respondents was named in the bankruptcy proceeding nor are either of them apparently affected by the bankruptcy adjudication.

The individual respondents are named as defendants in an action which has been brought against all of these respondents and others by the State of California.[28] The present status of that state court proceeding is unknown to us. The papers submitted to us indicate that certain of the relief requested in that action appears similar to the provisions of the order before us. However, we are obviously in no position to know whether the California court will enter any order against these individual respondents nor, if they do, whether such order will include restitutionary relief or some other type of relief which might render restitutionary relief in the instant proceedings unnecessary. Moreover, we do not agree, either as a matter of fact or as a matter of law, that parallel or similar enforcement action by state or local authorities ousts the Commission's jurisdiction or otherwise renders relief under the Commission's proceeding unnecessary or improper. The mere filing of an action in another jurisdiction—or even the securing of relief in such an action—would in no way lessen the need for us to ensure effective relief against future violations of the Federal Trade Commission Act irrespective of the relief sought or obtained to protect the citizens of the State of California. In any event, there is no evidence before us now that the individual respondents have, in fact, disgorged any of the monies which they received from the program. The mere possibility that such an order might be entered is not a sufficient basis to render the need for such relief a moot issue.

Nor does the class action filed against these respondents and the subsequent consent order agreed to in that action affect the proceedings before us, nor render moot the issue of the propriety and need for a refund order against these respondents. Respondent Gingold was not a party to the action and while respondent Heater

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because the corporate respondents are subject to a class action settlement in which certain franchisees were awarded $3,937,994.67 in damages. *Headley* v. *Continental Credit Card Corporation*, No. C-70-457 SW (N.D. Cal., August 10, 1972) Similarly, we need not consider respondents argument that "[a]ny order of restitution against the corporations would be meaningless as the trustee in bankruptcy has not been made a party to the action and would not be bound by any order that would be made." (R.A. 1)

[28] *People* v. *Continental*, No. 28930, Superior Court of the State of California In And For The County of Napa (March 13, 1972).

was named as a defendant together with each of the corporate respondents, the consent order and money judgment which was ultimately agreed to by the parties expressly excluded respondent Heater from its terms.[29] Thus, neither individual respondent is subject to the consent judgment entered in this private class action and hence it cannot affect the issue of the propriety of such an order provision in the instant action.

We conclude, therefore, that insofar as the corporate respondents have been adjudged to be bankrupt, a refund order would be a vain act. We conclude further that insofar as the two individual respondents, Heater and Gingold, are concerned the collateral state and private actions cited to us by respondents have in no way rendered these proceedings moot with respect to them.

The sole issue which remains then is whether the facts in the instant case demonstrate any need for the entry of a refund order against either or both of these individual respondents, Heater and Gingold.

C. *Necessity For an Order Against the Individual Respondents*

Respondents' primary contention is that it is improper to subject either individual respondent to a refund order because neither received income in his individual capacity. Complaint counsel argue that the record supports the liability of both individuals for the acts and practices here found to have violated Section 5 and that it is as essential that effective relief be secured against the individual respondents as it is against the corporate respondents.

Respondents argue that respondent Heater should not be subject to the refund provisions in the order because he received no income from the marketing and operation of the program, and alternatively, that he should be excused from the refund provisions on humanitarian grounds. Neither contention has any merit. The law judge found that respondent Heater was the essential author and promoter of the illegal credit card program. He created the corporations through which the program was implemented. He was the sole stockholder of the corporations which were active

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[29] The only papers submitted which relate to this proceeding is a stipulated amended judgment filed on August 10, 1972 in the United States District Court for the Northern District of California in which certain named franchisees and other members of the class received an award of damages of $3,937,994.67. *Headley* v. *Continental Credit Card Corporation*, No. C-70-457 SW (N.D. Cal., August 10, 1972) Notices in this action were sent to 641 members of the class. Of these 125 were returned unreceived and 6 elected to be excluded as members of the class.

during the relevant period,[30] served as president of both International and Universal for most of the relevant period and was found by the law judge to have primary responsibility for establishing, supervising, directing and controlling all of the acts and practices of these corporate respondents. (I.D. 6–7 [p. 585 herein], I.D. 12 [p. 588 herein]) He was in fact the alter ego of these corporate respondents which had no real existence separate from him.

The law judge's finding that Heater dominated every aspect of the program is fully supported by the record. All member and franchisee complaints were ultimately brought to his attention and were answered in accordance with his directions. (Tr. 154, Tr. 414–415, Tr. 422–423, Tr. 452–455) He took an active role in the preparation of the program's promotional material and prepared material was submitted for his approval. (CX 234 p. 14, Tr. 707) Additionally, he often acted as an instructor for the franchisees. (CX 234 pp. 1 and 3) His influence in the origination and implementation of this fraudulent scheme was all pervasive.

The evidence in the record also establishes that the control Heater exercised over the corporate respondents extended to matters beyond those relating to the sale and operation of the program. When he stepped down as president of Universal in March, 1971 he was hired to serve as a credit sales consultant for the program receiving a yearly fee of at least $30,000. (Tr. 757) In contrast the individual who assumed Universal's presidency in March, 1971 received only $15,600 a year. (Tr. 688) While the record does not indicate just what salary or dividends Heater received from the corporate respondents, it does indicate that he received at least $35,000 in loans from respondent Universal which have not yet been completely repaid. (Tr. 864)[31] His relationship to these corporate respondents as owner and virtual alter ego is clearly demonstrated by his statements to Dun and Bradstreet in response to inquiries about the financial condition of Universal. Mr. Heater wrote:

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[30] The stock of respondent International which became dormant in 1966 was wholly-owned by respondent Heater and his father. (I.D. 3 [p. 584 herein]; Tr. 764) According to the record, respondent Continental has presently no outstanding stock but does not indicate any further information about Continental's original stock ownership. (Tr. 758, 772–73) Respondent Universal, therefore, is the sole corporate respondent with outstanding stock which was active during the 1967–1971 period covered by the complaint. Respondent Heater owns all of the outstanding Universal stock. (I.D. 6 [p. 585 herein])

[31] According to information submitted by Heater to Dun and Bradstreet in 1968 Universal had $83,405 in outstanding notes from officers. (CX 126 B)

Should there be any question in your mind regarding our operation, it may be helpful for you to know that Universal Credit Acceptance Corporation is just one of many investments owned by the undersigned [J. Clifford Heater] and that there are net assets of over a million dollars available to meet the operating needs of this firm, should any additional sums of money be required. (CX 236 A)

In our judgment, the entire unconscionable scheme which respondents have been found to have been engaged in was the sole creation of respondent Heater. The corporate respondents were simply the means he created in order to carry out this scheme. Some of the corporate respondents have been inactive for some years. The remaining ones have now been adjudged bankrupt. It is respondent Heater whose future conduct must be the concern of this Commission. It is respondent Heater's conduct which this relief must be designed to effectively restrain if future law violations are to be prevented. It would be a totally vain act for this Commission to enter a refund order here which did not apply to respondent Heater. He has reaped the benefits of this program and it is he who must be required to disgorge these illegal gains illegally acquired and illegally retained. It is our considered judgment that respondent Heater must be bound by each of the order's provisions.

The remaining consideration with respect to Mr. Heater is whether there is any merit to respondents' argument, made in reliance upon the Commission's opinion in *Balfour, et al.*, Dkt. 8435, July 29, 1968 [74 F.T.C. 345,494], that "the charges against John Heater individually be dismissed on humanitarian grounds" because, according to respondents' brief, "Mr. Heater has acute problems which are exacerbated by litigation and result in feelings of persecution." (R.F. p. 2, T.O. pp. 24–26) Subsequent to oral argument, an unsworn letter from a psychiatrist was submitted in support of respondents' contentions stating that Mr. Heater had been hospitalized on June 19, 1972 at which time he was diagnosed as "Schizophrenic Reaction, acute exacerbation chronic type" which was based on the observation that Mr. Heater "seemed to be entertaining unrealistic ideas both of a grandiose and persecutory nature, and appeared at times to be hallucinating. He manifested a thinking disorder characterized by his inability to pursue a logical train of thought." When he left the hospital on

July 31, 1972, this condition according to the psychiatrist had "slightly improved." [32]

In *Balfour*, the Commission dismissed a complaint with respect to an 84 year old respondent who suffered several strokes and a heart attack and had not left his home for several months. Mr. Balfour had been the president and founder of the Balfour Corporation which together with Mr. Balfour had been found to have violated Section 5 by reason of their monopolization of the class ring market and various other distributional and contractual practices which were found to have restrained trade. There was no suggestion in *Balfour* that the corporate respondents were sham or simply the alter egos of the individual respondent. In consideration of Mr. Balfour's age and general physical condition, it seemed unlikely under the circumstances that an order against Mr. Balfour was required in the public interest and accordingly, the complaint against Mr. Balfour was dismissed on humanitarian grounds. No such facts exist in the instant case which would demonstrate the unlikelihood that Mr. Heater will not again engage in business or that the public interest will be adequately protected by an order entered simply against the corporate respondents. On the contrary, the facts in this record demonstrate conclusively that the public interest will be disserved unless the order proposed here is applied to respondent Heater with full force and effect.

We do not find that the respondent Gingold wielded any such all pervasive influence and conduct as respondent Heater did over the corporate respondents. While the record evidence respecting respondent Gingold's knowledge of the program and his participation in its implementation is more than sufficient to support the law judge's conclusion as to his individual liability under Section 5, we do not believe that the record is sufficient to demonstrate a need to bind him to a refund order such as we conclude is essential for respondent Heater. Accordingly, we sustain the law judge's conclusions respecting respondent Gingold's violation of law in both his individual and corporate capacity as well as the need to bind him to an order. We believe, however, and so conclude, that the public interest does not require that the refund provisions of the order be applied to this respondent.

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[32] The only statement in the letter with respect to the scope of Mr. Heater's disability or its likely duration was the psychiatrist's suggestion that "it would be in Mr. Heater's interest for the hearings to be continued rather than summarily dismissed * * *." The letter does not specify which hearings are being referred to although Mr. Heater's attorney indicates that this reference "was not meant to apply to the Federal Trade Commission proceeding." (R. F. p. 2)

Accordingly, we sustain the law judge's initial decision in its entirety with the exception of the applicability of the refund provisions of the order which shall be confined under the circumstances of this case to respondent Heater.

IV.

The Order

The law judge entered an order against the corporate and individual respondents containing provisions which prohibited their engaging in the specific misrepresentations and deceptions which the law judge found they had practiced, directed them to provide future members and franchisees with a seven-day period within which to cancel any application or contract executed by them and obliged respondents to refund any money obtained in violation of the order. These provisions have not been challenged by repondents.[33]

Thus we are concerned on this appeal solely with those features of the law judge's proposed order which direct respondents to refund illegally retained monies. The law judge's proposed order defined the category of persons to whom refunds should be made as embracing all actual or prospective members and franchisees from whom respondents had obtained monies during the period from January 1, 1967 to the effective date of this order. The amount of the refund to be made to these persons was to be made up of the monies which each had paid: (1) for air fare or other expenses for a home office interview; (2) for a deposit or down-payment on a franchise; (3) for a franchise fee (with certain monies earned by franchisees as commissions to be deducted); and (4) for membership fees, membership dues, and members' discount fees. Respondents were to be required to make the designated refunds to all those persons in the defined category "who show that respondents' solicitations, applications, agreements, contracts or performance were attended by or involved any of the practices, including, but not limited to, deceptive nondisclosure, which are now prohibited by this order * * *." (I.D. p. 70 [p. 641 herein])

We believe that the form of the refund provision as proposed by the law judge is in some respects inappropriate and in other respects cumbersome and difficult of implementation.

[33] Statement of respondents' position limiting their arguments before the administrative law judge and on appeal to the Commission is quoted *supra* note 7 at p. 7 [p. 646 herein].

We agree with the law judge that although respondents' program has been in effect for a longer period of time than that covered by the law judge's proposed provision, it is entirely proper to adopt some more limited period of time for the purposes of defining the monies which should be disgorged by the respondents.

The record indicates that respondents have records of franchisees and members going back to January 1, 1967. During the hearing complaint counsel introduced, without objection, exhibits based on respondents' business records which separately specified the exact sums of money which respondents received for franchise rights, membership dues and fees and members' discount fees for the fiscal years ending June 30, 1967 until June 1969. (CXs 122–124) A similarly uncontested exhibit was placed in the record which lists the person to whom each franchise was sold from January 1, 1967 to October 1969 and the exact amount each paid for their franchise. (CS 190 A–F) Additionally, while no exhibit specifically names each member who made a payment to respondents subsequent to January 1, 1967, it is evident from numerous exhibits that these members comprise a readily definable class and that the sum each is to receive is readily ascertainable.[34] In light of these facts and the failure of respondents to present any objection to the January 1, 1967 date as in any way inappropriate, we find that for the purpose of calculating refunds due under the order which shall issue in this matter, the period selected by the law judge is an appropriate and reasonable time span within which to measure the refund and one which is capable of ready ascertainment and compliance.

However, we do not believe that it is necessary to include within the class of persons whose payments shall measure the amount of the refund during this period, those persons who may have paid monies to respondents in the course of applying for membership of franchisee status but who subsequently did not perfect their

[34] One of these exhibits was based on copies of business records which were submitted in accordance with a subpoena which had requested information concerning specifically named members. (CX 197 A–H) The exhibit indicates that respondents' business records list the payments made by each member from at least January 1, 1967. (CXs 197–207) Another exhibit lists the total number of checks or statements sent to members from January, 1968 through October 1969. (CX 191 A–C) Still another exhibit which was introduced to establish the longevity of membership provides a list of randomly selected members who ceased to remain active during 1968. (CX 193 A–E) Finally, one exhibit which was introduced to show the special considerations some retail merchants were given to remain in the program lists each member who joined the program prior to January 1967 and was still active in the program as of October 1969. (CX 192 A–C)

application. Thus we would exclude from the persons to whom refunds will be paid any persons who did not actually become a member or franchisee. We have no doubt that to the extent such persons may have paid monies to respondents in the form of deposits, downpayments or the like, such monies would be illegally retained by respondents and could be used to measure the refund amount. However, we find nothing in the record which indicates that respondents' records contain any listing of such persons nor indeed that such persons constitute any significant subset of persons victimized by respondents' program. A refund order which is not as self-executing and easily implemented as possible could in fact be self-defeating as embracing too many areas of uncertainty as to compliance. Accordingly, our revision of the law judge's proposed provision limits the class of persons who in fact became members of franchisees within this January 1, 1967 period irrespective of the length of time they remained as such.

We also agree with the law judge that the monies to be used as a measure of the refund obligation should cover all franchise fees and membership fees, dues and discount fees paid to respondents by those members and franchisees who are listed as having such status during the defined period. We do not believe it is proper, however, to include within this measurement of the fund to be disgorged any monies expended by these members and franchisees for expenses incurred *by them* in connection with any home office interviews they may have undertaken. While such expenses might be part of an individual member's or franchisee's own damages which he suffered as a result of respondents' frauds, they are not monies which respondents *received* from the program and hence cannot be part of any obligation under this order which seeks only to ensure that respondents do not retain that which they procured through their illegal activities. Accordingly, we have modified the proposed refund order provision of the law judge to confine it simply to the funds received by respondents by virtue of payments made for franchise fees and membership fees and dues and members' discount fees, which in our judgment are all properly subject to the refund provision of the Commission's order as having been paid to the respondents and retained by them in violation of Section 5.

The law judge's order also provided that the refund due a franchisee for the amount of money paid to respondents for the franchise fee should be reduced by the commissions he may have

earned through the sale of memberships. We do not believe that this provision is either necessary or appropriate.

It is abundantly clear that it is respondents' retention of monies that is in violation of Section 5. To the extent any funds are illegally retained, the violation persists. In the instant case, this violation is in no way diminished by the fact that a member or franchisee may have incidentally earned any sum of money through his participation in respondents' fraudulent scheme. Respondents' violation of Section 5—and hence this refund order provision—is grounded essentially in the virtual worthlessness of their program and on the need to provide this refund remedy in order to redress the competitive imbalance resulting from this scheme and to ensure that respondents will not continue to violate the law in the future. In the instant case, the record is clear that the great bulk of respondents' franchisees and members in fact suffered substantial losses through their participation in respondents' program. Indeed this is the basis for the law judge's findings and conclusions as to the virtual worthlessness and blatant unconscionability of respondents' program. Thus the possibility that some few members or franchisees might have earned some benefits from the program is irrelevant to the essential purpose of this relief which is to ensure that respondents not retain the benefits which they procured through their illegal and unconscionable practices. To permit the retention of any portion of a payment made for a franchise because respondents, for a short time, successfully duped a franchisee to become an unwitting tool of the fraud would diminish the effectiveness of the remedy, fail to redress the competitive balance and leave undisturbed the essential law violation engaged in by respondents.

Finally, we do not believe that respondents' disgorging of the monies received from these designated members and franchisees should or need be conditioned in any way on any showing by these persons that their payment of monies to these respondents was in fact occasioned or covered by respondents' deceptions. It is unlikely that any member or franchisee could have learned—either directly or indirectly—of the program's existence except through respondents' deceptive representations. In any event, since the law judge found that respondents' deceptions inhered in every facet of its promotion and representations about its program, it is totally unnecessary to require respondents' members or franchisees to duplicate this showing for the purpose of implementing

respondents' obligation to disgorge the monies it illegally secured from these members and franchisees. Therefore, we have deleted this requirement as well from the refund order provision which we are entering here.

The remaining consideration before us is the procedure which should be followed by respondent to carry out this refund provision. Here again we believe that the law judge's proposed procedures for accomplishing this objective are unduly cumbersome and involve unnecessary steps. It is important with respect to any remedy and particularly with respect to refund orders that they be so devised as to render them virtually self-executing. It seems unnecessary, given the circumstances of this record, therefore, to require respondents first, to notify the members and franchisees of their right under the order to refunds and then to require such members and franchisees to file claims together with supporting documentation. Under the order as we have revised it, the members and franchisees to whom the refund is to be made as well as the monies to be refunded to them are clearly identified and known. All that is required, therefore, is that the respondent subject to the refund order first compile a list which notes the name and last known address of each member and franchisee entitled to a refund under the order and the amount each is to receive in accordance with the order, and then simply mail the appropriate refund to these members and franchisees.

It is clear that while we have sought to make the refund provision of this order as self-executing as possible, some questions may arise as to respondent's compliance with this provision. All such questions must be handled in the first instance under our compliance procedures. Normally factual disputes arising with respect to compliance are resolved by Commission staff who are charged with the responsibility of ensuring respondent compliance. They conduct a unilateral investigation, reach a conclusion as to whether or not compliance has been carried out and recommend that the Commission institute a civil penalty proceeding if there is reason to believe that full compliance has not been achieved. We believe that these procedures are entirely appropriate to apply to this refund provision in order to ascertain the facts respecting respondent's compliance with this provision. However, to ensure a full and fair hearing as to any dispute under these refund provisions, the order which shall issue in this matter provides respondent Heater with certain additional rights in the event

that questions are raised with respect to respondent Heater's compliance with the refund provision.

If it appears that respondent Heater cannot comply with the refund provisions of this order because of inadequate refunds, we have provided for a special procedure to enable respondent Heater to bring all relevant facts concerning his ability to pay before the Commission so that it can make such modification of its order as may appear appropriate in the circumstances.

If on the other hand, questions arise respecting the amount of monies received by respondents during the designated period, or the identity of the members and franchisees whose payments shall measure the amount of the refund or any other matter involved in respondent Heater's compliance with this refund provision, which cannot be resolved in the course of compliance, we have provided in our order that before any civil penalty proceedings are instituted, respondent Heater shall be notified of staff's conclusion that he is not in compliance. The order further provides that 30 days after receiving such notice respondent Heater shall have an opportunity before civil penalty proceedings are instituted to petition the Commission for such modification of the order as he may contend is warranted by the facts together with whatever supporting documentation he may wish to present as to why he is not in violation of the order. The Commission, on receipt of such petition, may modify the order, set the case down for a hearing before itself or a law judge or take such action as may be warranted in the circumstances. Such action by the Commission shall be in the form of an order which will be reviewable. By these procedures, the respondents' rights will be fully protected and the Commission will retain control over the proceedings so that it can make any modifications in the order which unforeseen circumstances may indicate are necessary.

CONCLUSION

The initial decision and the additional findings of fact proposed by complaint counsel which are to be found in their initial appeal brief (C.C.B. pp. 6–25) are adopted as the decision of the Commission.

The administrative law judge's order is modified in accordance with the specifications set forth in this opinion. An appropriate order will be entered.

FINAL ORDER

This matter having been heard by the Commission upon the appeals from the initial decision of respondents and complaint counsel, and upon briefs and oral argument in support thereof and in opposition thereto; and

The Commission having concluded that on this record and the facts and circumstances set forth therein that the appeals should be granted in part and denied in part;

It is ordered:

(1) That the initial decision and the additional findings of fact proposed by complaint counsel as set forth in the appeal brief of counsel supporting the complaint at pages 6 through 25 be, and they hereby are, adopted as the decision of Commission in accordance with the accompanying opinion;

(2) That the order contained in the initial decision being adopted in part and rejected in part by the Commission as set forth in the accompanying opinion, the following order be, and it hereby is, the order of the Commission:

It is ordered, That respondents Universal Credit Acceptance Corporation, Continental Credit Card Corporation, International Credit Card Corporation, also trading as National Credit Service, corporations, and their officers, and John Clifford Heater, individually and as an officer of Universal Credit Acceptance Corporation and International Credit Card Corporation, and Howard P. Gingold, individually and as an officer of Continental Credit Card Corporation, and respondents' franchisees, agents, representatives, employees, successors and assigns, directly or through any corporate or other device, in connection with the advertising, offering for sale or sale of franchises or credit card services, or any other products or services, or in the operation of any credit card service or other business in commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from directly or by implication:

1. (A) Representing that franchisees will earn or can reasonably expect to earn or receive any stated or gross or net amount of earnings or profits; or representing, in any manner, the past earnings of franchisees unless in fact the past earnings represented are those of a substantial number of franchisees in the geographical area about which such representations are made and accurately reflect the average

earnings of said franchisees under circumstances similar to those of the person to whom the representation is made.

(B) Representing that franchisees can expect to remain active franchisees for many years; or representing, in any manner, the longevity or tenure of past or existing franchisees unless in fact the periods of time represented are those for which a substantial number of franchisees actively pursued membership sales efforts.

(C) Selling, or offering franchises for sale, in any manner, without disclosing clearly and conspicuously in writing at or before the time of the first oral sales presentation, or in the event no oral sales presentation is made, reasonably prior to the execution of a franchise application, agreement or contract:

(i) the median and mean gross earnings from the sale of memberships in respondents' program by franchisees in the most recent calendar year (who were active for the entire year) preceding the year in which such sale or offer is made;

(ii) the total number of franchisees in the most recent calendar year preceding the year in which the sale or offer is made;

(iii) the total number of franchisees in subparagraph (ii) above who had earnings from the sale of memberships during the designated year in the following dollar amounts:

a. $1,000 or less
b. over $1,000 but not over $5,000
c. over $5,000 but not over $10,000
d. over $10,000 but not over $20,000
e. over $20,000

(iv) the number of franchisees referred to in subparagraph (ii) above who sold memberships for the following periods of time:

a. 1 year or less
b. over 1 year but not over 2 years
c. over 2 years but not over 3 years
d. over 3 years but not over 4 years
e. over 4 years

(v) the total number of members submitting credit charges in respondents' program during the most recent calendar year preceding the year in which the sale or offer is made;

(vi) the number of members referred to in subparagraph (v) above who submitted credit charges under respondents' program for the following periods of time:

a. 1 year or less
b. over 1 year but not over 2 years
c. over 2 years but not over 3 years
d. over 3 years but not over 4 years
e. over 4 years

(vii) the percentage of credit charges recoursed to members during the most recent calendar year and the full number and nature of reasons for which respondents may recourse charges;

(viii) the name and current address of each of respondents' franchisees in the most recent calendar year preceding the year in which such sale or offer is made;

(ix) a financial statement reflecting respondents' assets and liabilities (stating separately fixed assets and liquid assets) for the most recent calendar year;

(D) Selling, or offering memberships for sale, in any manner, without disclosing clearly and conspicuously in writing at or before the time of the first oral sales presentation, or in the event no oral sales presentation is made, reasonably prior to the execution of any application, agreement or contract:

(i) the percentage of credit charges recoursed to members during the most recent calendar year preceding the year in which the sale or offer is made and the full number and nature of reasons for which respondents may recourse charges;

(ii) the total number of members submitting credit charges in respondents' program during the most recent calendar year preceding the year in which the sale or offer is made;

(iii) the number of members referred to in subparagraph (ii) above who participated for the following periods of time:

a. 1 year or less
b. over 1 year but not over 2 years
c. over 2 years but not over 3 years
d. over 3 years but not over 4 years
e. over 4 years

(iv) a financial statement reflecting respondents' assets and liabilities (stating separately fixed assets and liquid assets) for the most recent calendar year.

Provided, however, That in the event respondents operated or used any corporate or trade name for a period of less than five years, the disclosures called for in this paragraph shall reflect the operations of the last preceding business entity used by respondents to sell and administer franchises and memberships.

2. Selling, or offering franchises for sale, in any manner, without furnishing to each prospective purchaser reasonably prior to the execution of a franchise application or agreement, a copy of the Federal Trade Commission Consumer Bulletin No. 4, "ADVICE FOR PERSONS WHO ARE CONSIDERING AN INVESTMENT IN A FRANCHISE BUSINESS."

3. (A) Representing that persons do not risk any loss of money in coming to respondents' offices, or any other place, for a franchise interview, or that respondents authorize the reimbursement of air fare expenses for such interviews, without disclosing clearly and conspicuously in writing prior the expenditure of any funds by such persons, all conditions which must be met to receive reimbursement, including the exact amount of any deposit or downpayment required.

(B) Failing to reimburse travel expenses to any person respondents have promised such reimbursement.

4. Representing that persons do not risk losing the deposits or downpayments submitted with applications for franchises; or that such deposits or downpayments are refundable when such deposits or downpayments may be forfeited if the applicants withdraw or fail to pay the balance due after acceptance of their applications by respondents, or for any other reason;

Provided, however, That respondents may make such representations if they do in fact refund such deposits.

5. Misrepresenting that any geographical area offered as a franchise has not been previously franchised by respondents or misrepresenting that such area has been franchised before by respondents and was profitable for the prior franchise holder.

6. Misrepresenting that respondents have a franchise committee which actually checks the qualifications of prospective franchisees, or misrepresenting, in any manner, that respondents check, or have checked the qualifications of a prospective franchisee.

7. Misrepresenting that respondents have a regional manager who will interview, or has interviewed, prospective franchisees for a particular geographical area; or that respondents have applications pending for a particular area; or that any person must act immediately to be considered for a franchise; or misrepresenting, in any manner, the nature and extent of interest of others in any particular franchise, or franchises in general.

8. Representing that franchise holders receive substantial benefits from renewals of memberships or from annual bonuses based on a percentage of net credit charges submitted by members; or representing, in any manner, benefits to franchisees which are dependent upon the actions of members, unless the benefits represented are those received by a substantial number of franchise holders.

9. (A) Representing that persons risk losing little or nothing in investing in a franchise; or that respondents will repurchase any franchise.

(B) Representing that respondents will aid or assist in the resale of franchises without contemporaneously, clearly and conspicuously disclosing the nature of such assistance and the amount of the resale purchase price which respondents will retain.

(C) Representing that respondents' franchises are vested property rights which may be sold, assigned, transferred or testated, without contemporaneously, clearly and conspicuously disclosing that franchises are subject to termination by

respondents if a franchise holder does not produce a prescribed sales quota.

10. Representing, in any manner, that respondents' program has received national acceptance, or that respondents' program can be sold with ease; or misrepresenting in any manner, the salability or degree of acceptance or approval of respondents' program.

11. (A) Representing that credit charges submitted under respondents' program are guaranteed payable or are payable without recourse; or that respondents assume the risk of nonpayment by members' customers in any manner including, but not limited to, using the terms "we honor all approved major credit cards," "honor all credit cards," "non-recourse," "without recourse" or any other terms or words of similar import or meaning.

(B) Representing that all members can expect to be successful or satisfied with the performance of respondents' program; or that members usually continue using respondents' program for two years and renew their contracts thereafter.

12. Using or disseminating any article written or prepared by respondents and published substantially verbatim in any newspaper, magazine, or other publication.

13. Using any letter, payment check, or other materials which purport to represent the satisfaction or success of any franchisee or member unless,

(A) such franchisee or member is actively selling or using respondents' program or service at the time such letter, payment check, or other materials are used;

(B) the full name and current address of the franchisee or member and the existence of any remuneration are disclosed clearly and conspicuously in conjunction with the use of such letter, payment check or other materials;

Provided however, That respondents shall not obtain or use any such letter, payment check or other material relating to any franchisee or member who has not sold or participated in respondents' program or service for at least six (6) months.

14. Representing that respondents' program costs members little or nothing at all; or that the program costs members

half as much as trading stamps; or misrepresenting, in any manner, the cost of respondents' program to members.

15. Representing that members complete just one simple form for all credit charges; or misrepresenting, in any manner, the procedures necessary to process credit charges and receive payment therefor; or failing to disclose contemporaneously, clearly and conspicuously any and all reasons which will preclude receipt of full payment of credit charges submitted by members.

16. Representing that members receive payment for each credit charge submitted to respondents in 30 days; or misrepresenting, in any manner, the period of time in which members will receive payment for credit charges submitted to respondents.

17. Failing to disclose clearly and conspicuously that respondents' program or service is not approved or endorsed by the individual issuers of the credit cards approved by respondents.

18. Representing that members are assured or can achieve a minimum 10 percent or any other percentage or amount of increase in business using respondents' program, without disclosing the number of members who have actually received said increase and offering to identify such members on request, and without maintaining verified statements from said members that they have received said increases.

19. (A) Using the name Fair Trade Bureau or any other name which represents that respondents' operations and activities have been endorsed by any independent or governmental organization.

(B) Writing, preparing, or disseminating any Better Business Bureau reports concerning respondents' business.

20. (A) Representing that every credit charge submitted by members is subject to the most intensive collection procedure in the credit industry; or misrepresenting, in any manner, the intensity or nature of respondents' collection activities.

(B) Using the name North American Collections or any other trade name or collection agency similarly related to respondents without disclosing contemporaneously, clearly

and conspicuously that such name or agency is owned, operated or controlled by respondents.

21. Representing that respondents will institute legal action against inactive members whose accounts respondents claim are in arrears, unless respondents do intend to pursue such remedies and have in practice pursued such remedies against substantial number of members.

22. Furnishing, or otherwise placing in the hands of others, the means or instrumentalities by or through which the public may be misled or deceived in the manner or as to the things prohibited by this order.

It is further ordered, That respondents incident to selling their franchises and credit card services:

a. Inform orally all persons to whom solicitations are made and provide in writing in all applications and contracts in at least ten-point bold type that the application or contract may be cancelled for any reason by notification to respondents in writing within seven days from the date of execution.

b. Refund immediately all monies to (1) all persons who have requested cancellation of the application or contract within seven days from the execution thereof, and (2) all persons who paid any monies for franchise fees, deposits or downpayments on franchises, air fare or other expenses for a home office interview, and for membership fees, membership dues and discount fees, who show that any of respondents' solicitations, applications, contracts or performance were attended by or involved any violation of any of the provisions of this order.

It is further ordered, That respondent John Clifford Heater shall:

a. Within thirty (30) days from the effective date of this order, compile a list which shall name each franchisee and member from whom respondents obtained any monies during the period from and including January 1, 1967, to the effective date of this order, state the last known address of each such member or franchisee, note the length of time each remained as such member or franchisee and specify all franchisee fees and all membership fees, dues and members' discount fees paid by each such member or franchisee to any of the respondents named in the complaint.

b. Within 90 days of the effective date of this order, refund by certified check or money order to each franchisee and member listed in accordance with subsection (a) of this order provision all franchise fees and all membership fees and dues and members' discount fees paid by each such member or franchisee to any of the respondents named in the complaint. Refunds shall be made via registered mail with return receipt requested and shall be accompanied by a brief statement substantially similar to that shown in Appendix A which shall inform the persons receiving refunds of the basis of the payment.

c. Hold any undelivered refund payments for a period of 180 days from the date of the first registered letter mailing and if the payment cannot be made to such addressee after due diligence within such period the obligation to refund shall expire.

Provided, however,

d. If respondent Heater claims not to have adequate funds to comply with this order provision, he may within 60 days of the effective date of this order petition the Commission to reopen the proceedings to consider his claim. The petition shall set forth the list of members and franchisees to whom refunds are due under this order and the sum of money each such member or franchisee is to receive in accordance with this order, a notarized statement of his assets and liabilities together with the assets and liabilities of all corporations in which he is an officer or stockholder.

Upon receipt of this petition and any response thereto which complaint counsel wishes to make, the Commission will assign an administrative law judge for the purpose of making findings and recommendations with respect to the claim. The administrative law judge shall furnish petitioner with the Commission's Statement of Financial Status (F.T.C. Operating Manual Chapter 6, Illustration 20, Paragraph 6.19), shall require its prompt execution and may conduct such interrogations of the petitioner or require the production of such documents as he deems necessary in order to make findings and recommendations as to any modification of this order which may be warranted on the issues raised by petitioner's claim. The findings and recommendations will be reported to the Commission for a final determination.

e. If any dispute arises as to the compliance of respondent Heater with the refund provision of this order which cannot be satisfactorily resolved by the parties, notice shall be given to respondent Heater of the extent to which he is regarded not to be in compliance and the facts respecting such alleged non-compliance. Within 30 days after the receipt of such notice of non-compliance, respondent Heater may petition the Commission for a hearing on such non-compliance or for a modification of the order provision giving rise to the disputed compliance or for such other relief as he believes is warranted and the Commission may set the matter down for hearing before itself or before an administrative law judge or shall either grant or deny such petition by order formally entered in the same manner and form as if it were an original order of this Commission.

It is further ordered, That respondent Heater shall maintain adequate records, to be furnished upon request by the Federal Trade Commission, which disclose the manner and dates members and franchisees entitled to refunds under this order have received refunds or the reasons such members or franchisees have not received refunds.

It is further ordered, That the respondents shall forthwith deliver a copy of this order to cease and desist to all present and future salesmen and franchisees or other persons engaged in the sale of respondents' franchises and services, and secure from each such salesman, franchisee or person a signed statement acknowledging receipt of said order.

It is further ordered, That the respondent corporations shall forthwith distribute a copy of this order to each of their operating divisions.

It is further ordered, That the respondents notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondents such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of the order.

It is further ordered, That each of the respondents herein shall, within sixty (60) days after service upon them of this order, file with the Commission a report, in writing, setting forth in detail

the manner and form in which they have complied with all of the provisions of this order. The report which respondent Heater shall file within sixty (60) days after service upon him of this order shall include the list he is to compile in accordance with subsection (a) of the provision of this order requiring him to refund certain monies to named members and franchisees. Thereafter, respondent Heater shall, within two hundred ten (210) days after service upon him of this order, file with the Commission a second report in writing, setting forth in detail the manner and form in which he has complied with this refund order.

Chairman Kirkpatrick not participating. Commissioner MacIntyre concurred in the result, including the restitution provision since fraud is found to have been involved here.

APPENDIX A

Important Notice

By order of the Federal Trade Commission I have been directed to refund any fees or dues or discount fees which you paid to me or to Universal Credit Acceptance Corporation, Continental Credit Card Corporation or International Credit Card Corporation to participate in my Honor All Credit Card Program. You are entitled to a refund of _____ for

(1) Payments for a Franchise; or

(2) Payments for membership dues or fees or discount fees.

I am enclosing a check for the amount of $_____ which my records show is the amount you paid to participate in the Honor All Credit Card Program.

_____
(signed)

John Clifford Heater

FINDINGS OF FACT PROPOSED BY COMPLAINT COUNSEL AS SET FORTH IN THE APPEAL BRIEF OF COUNSEL SUPPORTING THE COMPLAINT AT PAGES 6 THROUGH 25 ADOPTED BY THE COMMISSION IN ACCORDANCE WITH THE OPINION OF THE COMMISSION AND FINAL ORDER

III

ARGUMENT

The Hearing Examiner Erred In Failing To Make Several Findings Of Fact Supportive Of Related Order Provisions.

1. The Hearing Examiner Erred In Failing To Find That Respondents Fail To Disclose To Prospective Members Relevant Information, Which Would Assist Such Prospects In Evaluating The Probabilities Of Their Success And Chances of Achieving Longevity As Members, And Which Would Lessen The Potential For Their Deception, Including: The Median And Mean Period Of Time That Members Associated With Respondents' Program During The Previous Calendar Or Fiscal Year Submitted Payment Vouchers For Credit Charges Using The Program; The Number of Such Members Submitting Said Payment Vouchers Each Month; The Rate Or Degree Of Recoursing Credit Charges Back To Members During The Previous Calendar Or Fiscal Year; And, The Full Number And Nature Of Reasons For Which Respondents Recourse Charges. [CPF, pp. 50–51; see also I.D., p. 61 [p. 636 herein], Order provisions (1) (D) (i–iii)].

The hearing examiner did find that the foregoing disclosures were relevant and necessary for purposes of apprising prospective *franchisees* of material facts (I.D., pp. 20–21 [pp. 600–01 herein]). The order contains requirements for such disclosures to *both* franchisees and members (Order provisions 1 [C] [v–viii] and 1 [D] [i–iii]). Clearly, the record warrants the expressed finding upon which the order provision is predicated requiring the relevant disclosures to prospective members.

The record contains the full instructions provided by respondents regarding the presentation to be made to potential member prospects by both franchisees and home office membership salesmen, namely the "sales presentation" manuals (CX 130 and CX 180) and the sales kit that contains the testimonial letters, payment checks, and other promotional claims (CX 179A–Z88). These instructions, manuals and kits do not contain the material facts referred to above.

2. The Hearing Examiner Erred In Failing To Find That Respondents Represented That Articles Used To Solicit Sales Of Franchises And Memberships Are Unsolicited And Impartial Accounts About Respondents' Program. [CPF, p. 51; see also I.D., p. 65 [p. 639 herein], Order provision (12)].

The basic means by which this representation is made is the dissemination both directly and in sales kit form of reproductions or reprints of articles from newspapers, trade journals, and magazines (CX 110–119; CX 179 N–T, CX 179Z40 and CX 179Z51). In addition to the obvious capacity of purported reprints to connote a normal journalistic work product, the fact that these articles have been received as objective, unsolicited journalistic accounts is confirmed by witnesses (Davidson, Tr. 266–7; Colfels, Tr. 509–510).

3. The Hearing Examiner Erred In Failing To Find That In Truth And In Fact, Articles Used to Solicit Sales Of Franchises And Memberships Are Not Unsolicited And Impartial Accounts About Respondents' Program; And That Such Accounts, For The Most Part, Are Prepared And Placed By Representatives Of Respondents. [CPF, p. 51; see also I.D., p. 65 [p. 639 herein], Order provision (12)].

Respondents' Answer, p. 4, admits that "some" articles are prepared by representatives of respondents. At least ten such "articles" have been used to solicit memberships (CXs 110 through 119). Each of these articles was prepared by Leonard Snyder, who was employed by Universal Credit Acceptance Corporation for approximately 18 months as a public relations man. His testimony is that: "As a public relations man, it was my job to write articles which were partial and I did. Also, at Mr. Heater's behest, I solicited the publication of these articles in various periodicals, and successfully placed a number of them" (CX 234 at p. 14).

The record also indicates that six of the above-mentioned "articles" are contained in the respondents' sales kit (CX 179 N–T; CX 179Z40, CX 179Z51). In the case of CX 179Z51, a reprint of the "Photographic Trade News" contains what appears to be the result of an interview with a member, Brooks Cameras. It is apparent that what appears in said reprint comes from a so-called testimonial letter from Brooks Cameras also appearing in the sales kit (CX 179Z50). Said letter, according to the stipulated testimony of Joseph Dee of Brooks Cameras, was written for his signature by a representative of respondents, and because of the nature in which it was presented, Mr. Dee felt "constrained" to sign the letter, which was typed on a blank sheet of paper rather than on the stationery bearing the Brooks letterhead as it ultimately appears in the sales kit. The subsequent appearance of

said letter with the Brooks letterhead was accomplished without Dee's knowledge or consent. He was not interviewed by the Photographic Trade News nor did he participate in any way in placing the item (CX 234 at p. 8).

Additional evidence indicating that articles used by respondents are not unsolicited and impartial is revealed by the testimony of Leonard Lynema. As a franchisee, early in his tenure, Lynema received what purported to be a "newspaper article," including a dateline, in which respondents' program was praised and in which Mr. Lynema was quoted (CX 164 A–D). Mr. Lynema explained that this article entitled "Credit Cards are a Boon to Insurance" was sent to him by respondent Heater's representative, requesting that Lynema sign it. In fact, Mr. Lynema refused to sign the article (Lynema, Tr. 623–5). Despite his refusal in September 1968, such an article made its way into print on February 20, 1969 in "Underwriter's Report," wherein the quoted statements are those of respondent Heater instead of Leonard Lynema's (CX 116).

4. The Hearing Examiner Erred In Failing To Find That Respondents Represented That Letters And Payment Checks Used To Attest To The Success Of Respondents' Program Are Representative, Typical, And Current, And That Such Letters And Checks Reflect An Unbiased Evaluation. [CPF, p. 52; see also I.D., pp. 65–66 [p. 639 herein], Order provision (13)].

The letters and payment checks referred to are those appearing in the sales kit used by franchise salesmen to sell franchises and by franchisees and home office membership salesmen to sell memberships (CX 179Z7–37; CX 179Z41–50, CX 179Z52–60, CX 179Z63–65). In the "sales presentation" manuals containing the instructions and sample sales dialogue to be used in conjunction with the sales kit referred to, the following appears:

> Very shortly I am going to show you testimonial letters from business firms who *are* affiliated with us * * * (CX 180D and 180V–Z6) (emphasis added);
>
> SECTION VII: MEMBER SUCCESS LETTERS (RESULTS): (Success letters); * * * El Rancho Bijou * * * Motel California * * * S & D Richfield * * * Muffler Sales and Service * * * Midas Muffler * * * Ferre & Sons * * * Brodie & Schwerin * * * Jewel Box * * * Tomahawk Trading Post * * * Mam'selle * * * Misc. Success Letters * * * (CX 130 at pages 11–18).

The payment checks (CX 179Z7–18) are preceded by the following notation in bold-face letters: "checks to business firms from coast to coast—both large and small—confirm the profitability and acceptance of this business & sales program!" Said "confirmation" is stated in the present tense. Thus, there is the tendency and capacity to deceive persons into believing that the persons to whom the checks are written are all current users of the program. The section in CX 179 containing the so-called testimonial letters of merchants is preceded by a page containing the statement, "Here's what both large and small merchants are saying about * * * honoring all credit cards!" Accordingly, the capacity to deceive is again apparent from the statement that merchants "are saying" the statements contained in the letters that follow at CX 179Z26–37, CX 179Z41–50, CX 179Z52–60, and CX 179Z63–65, as long as such letters remain in the sales kit. The weight and importance given such statements may vary with the reader, but it is clear that the capacity to deceive exists through these "testimonial" letters, some of which date back to 1959, 1960, and 1961, because said letters appear to be from merchants who were still using the program in 1971, ten to twelve years later. Respondent Gingold confirmed the continuing use of such testimonials in the sales presentations to prospective franchisees as well as prospective members (Gingold, Tr. 742–3).

5. The Hearing Examiner Erred In Failing To Find That In Truth And In Fact, In Many Instances, Letters And Payment Checks Used To Attest To The Success Of Respondents' Program Are Unrepresentative And Atypical, And Are From Franchisees And/Or Members Who Are No Longer Active With The Program; That Many Of Such Letters And Checks Do Not Reflect An Unbiased Evaluation of Respondents' Program; And That Respondents Fail To Disclose That Many Testimonial Letters Have Been Prepared By Representatives Of Respondents And Many Are From Persons Who Received Remuneration Or Other Beneficial Consideration From Respondents, So As To Mislead And Deceive Prospective Franchisees And Members With Respect Thereto. [CPF, p. 54, see also I.D., pp. 65–66 [p. 639 herein], Order provision (13)].

(a) Testimonial Letters

Many members whose letters appear in respondents' sales kit (CX 179) discontinued using the program subsequent to writing

the testimonial letters, after discovering that the program had been grossly misrepresented and after becoming totally dissatisfied with it. Joseph Dee, of Brooks Cameras (whose testimonial letter appears at CX 179Z50) stopped participating in the program in May 1968, after signing the letter dated January 18, 1968 (CX 234 at p. 8). Morris Reznik, whose testimonial letter appears at CX 179Z43, dropped the program and has not used it since *1964* (CX 234 at p. 9). Morton Leeper, whose testimonial letter appears at CX 179Z37, stopped using the program after about 6 months, and has not used it since *1961* (CX 234 at p. 9–10). Leland McBride's testimonial letter (CX 179Z54) was given because he was promised that his $10 per month dues would be waived for the balance of his contract period if he would write such a letter. He rescinded his testimonial within about 45 days after submitting it (CX 218–224, CX 234 at p. 7), but that did not give the respondents the slightest compulsion to stop using it. F. G. Ferre, Jr., whose testimonial letter appears at CX 179Z35, signed a letter prepared for him by the franchisee who sold him the program (he did so as a favor because the franchisee's brother worked for him) (CX 234 at p. 8). Thereafter, in less than one year, Ferre discontinued the program because of misrepresentations and his dissatisfaction with the program.

All of the foregoing testimonial letters were still in use in respondents' sales kit issued November 1969, and were still in use as of the time of the hearing (Gingold, Tr. 741–3).

Franchisee Leonard Lynema personally contacted the businesses whose names appeared as satisfied users of the program in the company material he was given. He testified that "some claimed that those letters were forged because they did not write them" and "some claimed that they had sent the letter out but were sorry they ever did; but all of them that had any knowledge of the credit card business, every last one, was very, very upset and were perturbed to say the least, and every one of them claimed that they had lost all kinds of money" (Lynema, Tr. 629A–630). Similarly, a franchise investor in Wisconsin testified that "we * * * contacted some of these people in the state and found that they were only members for a short period of time and were, in fact, not satisfied. In fact, these letters in most cases were written a day or so after they became members, just as a favor to John Cadwell [the prior franchisee]" (Tronca, Tr. 655).

It is company policy to obtain success letters early in a member's tenure (Fish, Tr. 132–3). By definition, "representative" and "typical" connote the average experience of a large group. Since the average longevity of respondents' members is 8 to 9 months at best (Fish, Tr. 123–4; CX 193 A–E), letters obtained from any member soon after he buys a membership and before he learns of its real nature cannot be said to be representative or typical. Furthermore, any such so-called success letters are unrepresentative and atypical, in view of the frequency of member complaints and turn-over. The norm is dissatisfaction and failure with the program (Fish, Tr. 92–3, 97–8, 122).

Respondents' only explanation for the use of outdated testimonials—that they were allegedly valid when written—(Heater, Tr. 875–6), is clearly not legal justification for their continued use once they became obsolete.

(b) Payment Checks

Photocopies of 46 payment checks representing payment to members appear in respondents' sales kit to demonstrate the volume and activity of members using the program (CX 179Z7–18). Said sales kit was issued in November 1969 and it was still in use up to and including the time of the hearing in November 1971. Yet respondents admit that *42 of said members last submitted credit charges before 1969* (CX 194A–E, CX 197D–F, CX 198B). In fact, *26 of the members* last submitted credit charges under respondents' program *as far back as 1965 and 1966* (*ibid*).

(c) Use of Bias and Deceptive Non-disclosures

Many letters appear in respondents' sales kit which have been prepared, written or reviewed by respondents' salesmen or franchisees (Ferre, CX 234 at p. 8; Dee, CX 234 at p. 8; McBride, CX 218–224, CX 234 at p. 7). Therefore, the contents of said letters are obviously biased. Also, the many payment checks used do not reflect an unbiased evaluation because such checks are obviously chosen by respondents to reflect large amounts of money being remitted to members. The average amount of the 57 payment checks displayed by respondents is $2,500 (CX 179Z7–18). *In fact, the average member actually submits only $200 to $235 per month* (Fish, Tr. 126–7; CX 122, CX 191 A–B)![2] Therefore, the checks

[2] CX 122 reflects that $135,693 is the income from credit charge discounts for the year ended June 1969. Since this represents 6 percent of the total charge volume, the total for the year is $2,261,550; divided by 12, the average is $188,462.50 per month from *all* members.

used in the sales kit, averaging $2,500 each, do not reflect an accurate picture of members' charge volume.

As for the remuneration or other beneficial consideration to members who wrote testimonial letters, there has already been a reference to McBride, who wrote a testimonial letter so as to benefit from the offer of respondents to waive his monthly dues (CX 234 at p. 7, CX 221, CX 179Z54). Also, Harold Forkas continued to be charged only a 5 percent discount rate under his membership when it was renewed rather than raising the discount rate to 6 percent (CX 179Z59, CX 207 A–C). The Brodie and Schwerin membership was not charged $10 per month dues when its contract was renewed in 1965; it was not charged a $240 membership fee when it renewed again in 1967; and it paid only a 5 percent discount throughout its membership (CX 179Z41, CX 198 A–H).

Respondent Heater characterized the California Motel and/or the Proctor Motel as the longest-lasting members he has had in his program (Heater, Tr. 853), and the sales kit contains testimonial letters from both (CX 179Z31, CX 179Z29). The member account cards maintained by respondents on the California Motel (CX 203 A–L) reveal that this motel pays no membership fee, only $6 per month dues and a 5 percent discount on charges submitted, whereas current members pay a $240 membership fee, $10 per month dues and a 6 percent discount rate on charges submitted. Further special considerations are apparently conveyed to this member, judging from the way respondents' staff is cautioned to treat the account: "Do Not Send A Statement On This Account At Any Time" (CX 203 I).[3] The Proctor Motel membership, similarly, pays no membership fees, only $6.00 per month dues, and a 5 percent discount rate, and the member account card bears the notation: "Do Not Send A Statement On This Account At Any Time" (CX 192B).

Respondent Heater admitted that once testimonial letters are obtained and they are built into the "sales presentation" manual (CX 130), they continue to be used notwithstanding the fact that they may subsequently become obsolete (Heater, Tr. 874–6). He

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CX 191A–B reflects that the average number of members active in terms of receiving checks or statements from respondents each month for the year July 1968–June 1969 was 803. Therefore, $188,462.50 divided by 803 equals $234.70 total charges per month per member.

[3] Ordinarily, if a member's charges are not in excess of his monthly dues plus the 6 percent discount and any recourses, he would owe respondents money, for which he would be sent a statement instead of a check (Fish, Tr. 124–5).

further admitted that in addition to failing to remove obsolete testimonial letters from the sales kit book (which is a loose-leaf binder, easily susceptive to making both additions and deletions), he has seen fit to remove the addresses and phone numbers from the letterheads (Heater, Tr. 879–80; Krieger, Tr. 202–3). Thus, the result is that prospective franchisees and members cannot even contact those members to determine whether or not they are accurate "testimonials." It is evident why Heater has made it impossible for anyone to contact the members.

6. The Hearing Examiner Erred In Failing To Find That Respondents Represented That Members Complete Just One Simple Form For All Credit Charges; And That Respondents Represented Members Receive Payment For Each Credit Charge Submitted To Respondents In 30 Days.[4] [CPF, p. 60; see also I.D., p. 66 [p. 639 herein], Order provisions (15) and (16)].

(a) Simple Charge Form

The representation that respondents' program involves just one simple form for all credit charges is made to prospects in direct mailers (CX 28B, CX 31A, CX 32A, CX 34A, CX 38B, CX 39B, CX 41B, and CX 42A), and in the Franchise Proposals (CX 45B and F; and CX 46B and F). It is also included as an instruction in the "Sales Presentation" manual, wherein it is stated:

> What are the mechanics of the program? Well, as you can see here, with each charge customer, you will fill out a very simple form called the charge ticket (CX 130 at p. 8);
>
> Our program allows you to belong to one program, and receive one check a month for all of your credit charges with one simple form to fill out (CX 130 at p. 9).

The effect of such statements as to the simplicity of the charge form is to lull members into a false sense of security that there are no hidden traps in the program (Padgett, CX 234 at p. 14; Dorigo, CX 234 at p. 13; Brooks, CX 234 at p. 11; Manicucci, CX 234 at p. 13; Sheldon, CX 234 at p. 10; and Kiefert, CX 234 at p. 12).

(b) Payment Policy

The representation that members receive payment for each credit charge submitted to respondents in 30 days is made through statements such as "one monthly check" (CX 29B, CX 34A, CX

[4] The Examiner actually did make the latter finding in his general statement "Nature of Respondents' Business and Business Methods," without citation to evidence in the record (I.D., pp. 2–3 [pp. 583–84 herein]).

38B, CX 39B, and CX 42B); "* * * receiving just one check for all credit sales he made during any given month" (CX 45B and CX 46B); and "one monthly check covering all charges" (CX 45F and CX 46F). Also, instructions contained in the "Sales Presentation" manuals include the following:

(Payment Policy)

Once a month you will receive a check for these charges back by return mail. Any of these charges in to us by the first of the month will be paid to you by the 15th of the following month (CX 130 at p. 8) (emphasis added);

Charges must be forwarded to us weekly. And the payment to you is every 30 days (CX 130 at p. 26); and

How does he get paid: Stress simplicity. Explain mechanics. He mails the first and last copies of all credit charges along with two copies of the payment voucher every week. All charges that are received and processed by the 1st are paid by the 15th of the following month (CX 180F, #9).

While a *technical* analysis of the wording of the payment policy—"all charges in by the first of the month are payable on the 15th of the following month"—does indicate a minimum of 45 days or six weeks, this statement not only has the capacity and tendency to deceive, but it *actually* has misled numerous persons into believing that they would receive payment in two weeks or some other period of time less than the minimum of 45 days (England, CX 234 at p. 3; Smith, CX 234 at p. 5; McBride, CX 234 at p. 7; Brooks, CX 234 at p. 11; Padgett, CX 234 at p. 11; Manicucci, CX 234 at p. 13; Dorigo, CX 234 at p. 13. It is obviously calculated to have that deceptive effect.

7. The Hearing Examiner Erred In Failing To Find That In Truth And In Fact, The Forms Which Members Must Complete To Process Credit Charges Are Not Simple And Are Burdensome To Fill Out In Practice. [CPF, p. 61; see also I.D., p. 66 [p. 639 herein], Order provision (15)].

An examination of respondents' charge ticket (CX 138) reveals that members must obtain a substantial amount of information. The customer's name and perhaps his address, his signature, and the name and number of credit card used, is the extent of the information required by most common credit card operations which businessmen are accustomed to, namely BankAmericard, Master Charge, Diner's Club, or American Express. In addition to that information, however, respondents' charge ticket requires the merchant to obtain the customer's employer's name and address,

the customer's business phone and home phone, the customer's driver's license number and his automobile license plate number.

It is not difficult to conceive how members operating such retail businesses as service stations, restaurants, or motels (or any establishment which customarily has more than one customer requiring attention at any given time) would find it extremely burdensome in practice to obtain from the customer all such information. This situation is confirmed by the fact that in actual practice members failed to complete the charge ticket *in most instances* (Fish, Tr. 132). Also, respondents' former Director of Member Relations received complaints from members that the charge ticket was difficult to complete (Fish, Tr. 133). When franchisee Krieger found his members were receiving a high degree of recourses, he telephoned respondents and was told that "this charge ticket was set up in this manner because 9 out of 10 people left something out" (Krieger, Tr. 208).

8. The Hearing Examiner Erred In Failing To Find That In Truth And In Fact, Members Do Not Receive Payment For Each Credit Charge Submitted To Respondents In 30 Days. [CPF, p. 62; see also I.D., p. 66 [p. 639 herein], Order provision (16)].

A literal understanding of respondents' payment policy makes it clear that payment is received for all charges reaching respondents by the first of any given month by the 15th of the following month, which is technically a minimum of 45 days and a maximum of 75 days. Consequently, payment is made on or about the 15th of each month, but that payment is for charges submitted at least 45 days earlier (Fish, Tr. 92–3, 95–6). Obviously, respondents do possess the means to fully explain the payment policy, which is of course a crucial item of information to merchants, especially small merchants, to whom prompt "non-recourse" payment for their accounts receivable is the service for which they contracted. Respondents do employ a document (CX 170C) which simply and accurately illustrates when members will receive payments. Yet, respondents disseminate this document to members *only after they have signed their membership contracts* and paid their money, and sometimes considerably after that time. This fact is admitted in a 1966 letter to franchisee Roy S. McKinnon, in which Continental Credit Card Corporation stated: "we have always sent out the explanation of the payment policy with the member welcome letter and we are now also including the payment policy chart in this same letter" (CX 170A–D). It is not surprising that when

members later learn the real payment policy, they complain in great numbers (Fish, Tr. 92–3).

9. The Hearing Examiner Erred In Failing To Find That Respondents Represented That When A Member Becomes Inactive And Respondents Determine His Account Is In Arrears, Respondents Will Institute Legal Action For The Collection Of Such Monies Unless They Are Remitted By The Member To Respondents Upon Demand. [CPF, p. 69; see also I.D., p. 68 [p. 640 herein], Order provision (21)].

This representation is made through the use of form letters which state that "this account will be assigned to our attorney for collection within 10 days" and "if you would like to avoid additional expense of court action, attorney fees, interest, etc." (CX 148, CX 182, and CX 185). Also, follow-up form letters are used, stating:

> You have ignored our previous request for payment of the above contractual obligations.
>
> This is our last attempt to collect this account in a friendly way * * * we will be compelled to turn it over to our attorney for such action as may be necessary. * * *
>
> * * * *CONSIDER THIS PROPER NOTICE*! (CX 184).

An even more threatening form letter is used next if a member fails to respond to the above-mentioned letters:

> This is a business matter, and we would like to settle it with you in an amicable and business-like fashion. * * *
>
> On the other hand, if you make it necessary for us to seek court action, you will have to bear the additional costs, the embarrassment and other consequences of a judgment and seizure by the sheriff (CX 147).

Another exhibit in the record indicates a "Notice of Extreme Delinquency" is used by respondents' collection department wherein the following appears: "Redeem your credit and avoid—legal action * * *" (CX 149).

10. The Hearing Examiner Erred In Failing To Find That Respondents Seek To Sell Their Franchises, Memberships And Credit Card Services While They Know That Their "Honor All Credit Card" Program Does Not Operate And Produce Results As Represented. (CPF, p. 70).

The Examiner did find that "Respondents Knew Their Program was a Failure But Continued to Victimize the Franchisees

Regardless" (I.D., pp. 49–54 [pp. 627–31 herein]). Our only challenge to this finding is that it is too narrow, in being applicable only to the franchising aspects of respondents operation. We believe the record substantiates the broader finding set forth above. Whereas the examiner quoted liberally from the record to warrant his finding as to respondents' knowing victimization of franchisees, the record also contains ample foundation for extending such a finding to include respondents' knowing deception of members as well.

The testimony of ex-employees intimately acquainted with the internal policies pertaining to *both* the franchise and membership aspects of respondents' operations clearly reveals that respondents have knowledge that the "Honor All Credit Card" program does not operate and produce results as represented. After respondents former Director of Member Relations Fish had become aware of the deceptions involved in the operation of the membership side of the program, he spoke with respondent Heater and brought to his attention the complaints that he had received from members, particularly those about recoursing and payment policy (Fish, Tr. 141–2, 155). Not only did Heater fail to take any action to apprise prospective members at an earlier point in time of the many reasons for recoursing and the actual payment policy, but when Mr. Fish expressed that "the members were not buying what they thought they were buying" (Fish, Tr. 115–6), Heater's specific answer was:

> I'm sure the program may have some faults; but what if you sold a man a tin mine, and he went in and started to dig and found out he had a gold mine, would he complain? (Fish, Tr. 116–7).

Mr. Fish's response to Heater was: "Well, he might not complain, but it hardly seems the ethical thing to do to sell him a tin mine in the first place if you don't know there's tin there." Heater's retort was: "That wouldn't matter because the man would not complain" (Fish, Tr. 117). Mr. Fish estimated that in the course of 18 months he sent Heater about two dozen memoranda and also verbally recommended changes in the program to eliminate the complaints. During Mr. Fish's employment, no changes were ever made (Fish, Tr. 137, 154).

Moreover, there is evidence which indicates that the program had been operated the same way for many years and that respondents must be presumed to have knowledge of its failure. Specifically, franchisee Winstead discovered that his areas in the

State of Texas had been previously worked under the name National Credit Service. He spoke with an individual who had sold over 4,000 members in respondents' program in all 48 states and not one of them lasted over 6 months. This individual couldn't stay at the same place to work over a month at a time because of the bad feedback from members (Winstead, Tr. 337–8, 357). Similarly, when Leonard Lynema began to operate his franchise he learned that National Credit Service had previously operated in his area and had acquired an extremely bad reputation (Lynema, Tr. 629 and 629–A). Finally, CX 186, a letter from National Credit Service, Division of International Credit Card Corporation, signed by J. Clifford Heater, and dated November 23, 1964, advises a franchisee in Ohio:

> The best way to handle the "sticky" legal phrases in our membership agreements, is to tell the prospect that normally they are not important and are only designed to protect against members or employees who sometimes try to take advantage of us. Tell them: "certainly our contract or even our all credit card program is not perfect in all respects. However, let's not be looking at the hole in the doughnut." The question is, "Will you make money with our program?" * * * Don't get involved in technicalities with the customer, this will get you nowhere * * * (CX 186A, Tr. 397).

If a company were operating in good faith, it would obviously attempt to cure any defects and problems which were known to cause a high failure rate amongst participating franchisees and members. However, the respondents are of a different breed. As previously indicated, well-intentioned employees made numerous suggestions for changes to improve the life expectancy and earnings capabilities of franchisees and members, only to have their recommendations studiously ignored (Fish, Tr. 137, 154; O'Flaherty, Tr. 422–3). If respondents were interested in operating a bona fide credit card program, the bulk of their revenues would be derived from the discount fee on charges and monthly membership dues, but consolidated income statements indicate that respondents receive the majority of their revenues from initial franchise and membership fees. On the other hand, monthly membership dues and the 6 percent discount rate produce a very low proportion of respondents' income (CX 122–4). Therefore, it is apparent that respondents are making their money from high one-time fees from the initial sale of franchises and memberships. With these fees in their pockets, respondents could not care less for the welfare of their franchisees and members.

11. The Hearing Examiner Erred In Failing To Find That Respondents Know That The Realization Of Profit By Franchisees Contemplates, And Is Necessarily Predicated Upon, The Exploitation Of Member Retailers Who Must Be Induced To Participate In Respondents' Program By Misrepresentations. (CPF, p. 78).

Not only do respondents initially fail to give franchisees all of the material facts about the program (see the Examiner's Finding No. 28, I.D., pp. 20–21 [p. 600 herein]), but respondents know that the program itself cannot be sold honestly (O'Flaherty, Tr. 426–7). Consequently, respondents train their franchisees in seminars with materials and dialogue which cause the franchisees to repeat the misrepresentations to member prospects (CX 130, CX 179A–Z88). Respondents' former Director of Member Relations testified that not only are the seminars deficient in terms of complete omissions of material information, but he also observed erroneous information being disseminated (Fish, Tr. 119–20, 168–9, 170–1). Franchisee Richard Colfels was trained not to show member-prospects the back of the contract until after they had signed it (Colfels, Tr. 527). Franchisee Harold Winstead was trained to go over the contract so fast that member-prospects could not have time to ask questions (Winstead, Tr. 350–1). As one ex-franchisee concluded, the training seminar he had taken "didn't tell me how to tell the truth about the program," and in fact "we are told to lie * * *" (Davidson, Tr. 285, 301–3, 323).

Moreover, the seminar camouflages this deceit by using a "scientology," "pep-talk" approach (O'Flaherty, Tr. 424–5, 471). An especially lucid and enlightening analysis of the seminar was related by franchisee Colfels. His testimony vividly demonstrates that the over-all effect of the seminar is to subject the franchisees to a psychological build-up and send them out into the field to mouth and repeat the misrepresentations placed in their hands by respondents (Colfels, Tr. 513–18, 532–3).

12. The Hearing Examiner Erred In Failing To Find That At No Time Did Respondents Notify Any Persons Who Expended Money In Reliance Upon Respondents' Statements And Representations That Their Money Would Be Refunded If Respondents Knew Or, As Reasonably Prudent Businessmen, Should Have Known That Respondents' Program Would Not Operate And Produce Results As Represented; And In Failing To Find That Respondents Regularly Retain And Withhold Funds From Franchisees, Franchise Prospects and Members. (CPF, p. 79).

This allegation is supported by the statements in the Examiner's Findings Nos. 27 and 50, relating to the *continuing* financial losses of both franchisees and members. In addition, as of the hearing date (November 1971), respondents still had not satisfied requests by franchisees to buy back franchises as promised (see the Examiner's Findings Nos. 43 and 44, I.D., pp. 32–33 [pp. 611–12 herein]), and respondents still owed former franchisees commissions on sales of other franchises and on sales of memberships (Lynema, Tr. 626, 629; Winstead, Tr. 358–9).

The record also demonstrates the continuing failure of respondents to pay franchise prospects sums expended for air fares for interviews at respondents' offices and sums deposited with applications (see the Examiner's Findings Nos. 31–34, I.D., pp. 22–26 [pp. 601–05 herein]; MacDonald, Tr. 550, 554; Clay, Tr. 571–3).

Similarly, on the membership side, respondents' policy is such that refunds are not rendered. When a member quits using the program and has suffered a loss he is offered a "settlement" check for any outstanding monies owing to him after deductions for all dues for the balance of the contract period (Fish, Tr. 124–5). If the member endorses and cashes said "settlement" check, it constitutes "an acknowledgement of full payment and release of all claims or obligations against the issuer of this check or third parties arising out of the contract" (Clay, Tr. 577).

13. The Hearing Examiner Erred In Failing To Find That Respondents' Honor All Credit Card Program As Actually Operated Is Essentially Different From The Program As Represented And Has Proven To Be Substantially Worthless To Franchisees And To Members. (CPF, p. 81).

It may be argued that the examiner did actually adopt the complaint counsel's proposed finding to this effect (see the Examiner's Finding No. 50, I.D., p. 39 [p. 618 herein]). In finding "a scheme fraught with misrepresentations," in stating that "the program as administered has no merit" (I.D., p. 3 [p. 583 herein]), and in citing the *Curtis Publishing Company* case for the proposition that restitution may be a proper remedy where the consumer receives something that is "either worthless or of only token value" (I.D., pp. 56–57 [pp. 633–34 herein]), the examiner has implicitly made the desired finding. We feel said finding should be made explicitly.

That the program is basically and essentially misrepresented is clearly supported by the record. The program is advertised and promoted as "non-recourse," when in fact it amounts to a full recourse program (see the Examiner's Findings Nos. 49 and 50, I.D., pp. 35–41 [pp. 614–19 herein]); the program is featured as one under which the member will receive his money in a relatively short period of time (*e.g.*, two weeks to 30 days), when in fact he will not receive payment for 45 to 75 days at best (see CPF Nos. 58 and 60, proposed findings 6 and 8, *supra*); and the respondents are represented as a large, reputable, financial organization, when in fact respondents' size, reputation and financial condition are significantly different and inferior (see the Examiner's Findings Nos. 45–48, 61–66, 69–71; I.D., pp. 33–35, 43–48 [pp. 612–14, 621–24, 625–26 herein]).

The non-recourse feature is obviously the essence of the bargain offered by respondents and contracted for by both members and franchisees. Why should a merchant pay respondents a $240 membership fee, $10 per month dues, and a 6 percent discount, unless it is to be free of any risks of nonpayment by customers? If the merchant is to bear the risk of loss in any event, he is placed in the same position he would have been in had he accepted a personal check from the customer, or had the merchant allowed the customer to charge the sale and be billed directly by the merchant. In such instances the merchant would be in the same situation he is under respondents' program, *except* he would not have paid the respondents the membership fee, dues, and discount. To this extent, therefore, the program proves to be worthless, causing considerable financial loss and economic waste (Winstead, Tr. 355; Tronca, Tr. 665–6; CX 122–124).

Furthermore, for a substantial number of members the program is in fact worse than worthless. That is, because of the frequency of recoursing, the members not only pay $240 membership fees plus $240 monthly dues plus the 6 percent discount fees for a service they do not receive, but they also lose the value of their own merchandise and services to the extent the credit charges are not paid by their customers (Colfels, Tr. 517). The substantial worthlessness of the program to respondents' franchisees who attempted to sell it is also manifest (see the Examiner's Finding No. 27, I.D., pp. 15–20 [pp. 595–600 herein]).

14. The Hearing Examiner Erred In Failing To Find That For At Least The Past Six Years, Respondents, In The Regular Course

Of Their Business, Have Calculatedly Relied Upon A Literal Interpretation Of Formal Documents (Which They Deceptively Induce Their Victims To Execute) In Order To Evade And Insulate Themselves From Liability For Their Misrepresentations. (CPF, p. 82).

(a) Franchisees

See the Examiner's Findings Nos. 31 and 34 (I.D., pp. 22–24, 26 [pp. 601–03, 605 herein]) for discussions of how literal interpretations of respondents' franchise application and telegrams are used to evade refunding promised air fares and deposits to franchise prospects. By signing the franchise agreement, the franchisee certifies that "this agreement constitutes the final and complete understanding between the parties hereto and that no other representations or promises, verbally or otherwise, have been made" (CX 16A), when in fact a multitude of other representations, verbal and otherwise, are made (see the Examiner's Findings Nos. 23, and 26–71, I.D., pp. 11–48 [pp. 591, 593–626 herein]). Further, said franchise agreements ostensibly bind the franchisee to bring any suit that may arise between the parties only in the State of California, even though the franchisee may reside hundreds or even thousands of miles away (CX 16B, CX 17B, CX 18B). In addition, under the terms of respondents' franchise agreements, franchisees who quit or are terminated before the end of one year fail to receive any of their 1 percent bonuses from the charge volume of their members (CX 4, CX 16 A–B, CX 18 A–B; see also CX 190A–Q and the Examiner's Finding No. 27 for evidence that the average franchisee longevity is 8.61 months producing membership sales, I.D., p. 16 [p. 596 herein]).

Another document used by respondents to entrap franchisees is a "membership sales training questionnaire" which purports to be a final examination completed before franchisees leave the seminar (CX 226, CX 227, CX 233, RX 1, RX 2). The franchisees are actually given the "correct" answers before they take the "test." As far as respondents are concerned, the real purpose of the "test" is not to make sure that the franchisee understands the program, but to trap him into making admissions which can be used against him in the future (O'Flaherty, Tr. 430). Examples of such questions are: "Have any promises been made to you that are not set forth in the above agreement?" and "Do you understand that because your success and the success of our members depends upon

each individual (sic) 'ability,' that no representation or guarantee can be made as to the actual income or that any specific income or profit will be made?"

(b) Members

Members are entrapped in part by means of what the examiner characterized as "devious contractual language, not intended to be read and not clearly understandable, even if actually read" (I.D., p. 3 [p. 584 herein]; see also CPF pp. 83–84, CX 136 A–B). The record also discloses that respondent Heater acknowledged the use of "sticky" legal phrases in the membership agreements as far back as November 23, 1964 (CX 186 A–B).

The charge ticket (CX 138) is an additional document used deceptively to effectively insulate respondents from liability. It calls for a multitude of items of information, much of which is never utilized to effect collection (Fish, Tr. 107–8). Its only purpose is to establish a foundation, an excuse, by which to be able to recourse the charge to the member if the customer does not pay.

With respect to members who may see fit to bring a law suit against respondents for the misrepresentations which induced them to sign their contracts, respondents rely upon a membership agreement provision establishing venue in San Mateo, California (CX 136B, CX 137B). Obviously, most small merchants in areas of the country remotely located from California interpret this to mean that they have no remedy at all, since the costs of such litigation would exceed any judgment.

The foregoing, therefore, serves to document in the record what the examiner, without citations, made reference to as respondents' efforts "to insulate themselves" (I.D., p. 3 [p. 584 herein]).

15. The Hearing Examiner Erred In Failing To Find That Respondents Are Responsible For The Acts And Practices Of Their Franchisees. [CPF, p. 86; see also I.D., p. 68 [p. 640 herein], Order provision (22)].

The respondents train the franchisees and subsequently control and supervise their activities. Franchisees receive the same training as respondents' home office membership salesmen (Fish. Tr. 118). In the training seminar, franchisees are armed with sales materials and then are required to memorize certain sales dialogues (CX 180D, CX 180M). Before "graduating" from the seminar, franchisees take what purports to be a test, which contains a recitation of many representations about the program, including many omissions and half-truths (CX 226, Winstead, Tr.

345–6; O'Flaherty, Tr. 429–30). Moreover, respondents then bestow upon franchisees a "certificate of training" (CX 179A), which attests to the successful completion of the prescribed course of training as outlined in the company's training manual.

After the seminar, franchisees return to their areas and utilize the sales materials and dialogues furnished by respondents (CX 130, CX 131A–B, CX 133, CX 179A–Z88, CX 180A–Z33, and CX 187A–B). Also, franchisees are required to submit daily sales reports as well as any sales agreements they wish to enter into with salesmen (CX 134 and CX 135).

The essence of the relationship between respondents and their franchisees is revealed in the testimony of respondent Heater:

A. We find that they [franchisees] need about as much help as the salesmen and the money they have invested has been a very little factor.

Q. How about as much control, do you have to have pretty good tabs on the franchisee?

A. That is right.

Q. What kind of control do you try and keep over the franchisee?

A. We try to maintain a continuous correspondence with them and phone calls.

* * * * * * *

A. Phone calls, sometimes personal contact. We would occasionally go out there, they would come to the home office for retraining perhaps, sometimes we would go out there and conduct a sales training seminar for them and their salesmen to do what we could to make them successful.

* * * * * * *

Q. Could you tell me what your purpose was for keeping control over who the franchisee might hire?

A. It is always a good idea to know who is out there *working for you.* Sometimes we get phone calls into the office wanting to know does this person *represent us* and it can be very embarrassing if we can't say *yes* (emphasis added) (Heater, Tr. 767–8, 769).

In practice, therefore, respondents' franchisees are at best glorified salesmen, who have paid respondents $7500 to work for them.[5]

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[5] On these facts, the authorities are clear that respondents are liable for the acts and practices of their franchisees. *Parke, Austin & Lipscomb, Inc.* v. *FTC,* 142 F.2d 437 (2d Cir. 1944); *Steelco Stainless Steel* v. *FTC,* 187 F.2d 693 (7th Cir. 1951); *Standard Distributors* v. *FTC,* 211 F.2d 7 (2d Cir. 1954); *Libbey-Owens-Ford* v. *FTC,* 352 F.2d 415 (6th Cir. 1965); *Goodman* v. *FTC,* 244 F.2d 584 (9th Cir. 1957); *Federal Trade Commission* v. *Standard Education Society, et al.,* 302 U.S. 112 (1937).