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Meeting Before the Commission

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FEDERAL TRADE COMMISSION

INDEX

WITNESS: EXAMINATION

None.

EXHIBITS FOR IDENTIFICATION

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None.
FEDERAL TRADE COMMISSION

In the Matter of: Docket No.: P951201
HEARINGS ON GLOBAL AND INNOVATION-BASED COMPETITION

Tuesday, November 21, 1995
Federal Trade Commission
Sixth and Pennsylvania Avenues
Room 432
Washington, D.C. 20580

The above-entitled matter came on for hearing, pursuant to notice, at 9:00 a.m.

SPEAKERS:

ROBERT PITOFSKY
Chairman, Federal Trade Commission

ROSCOE B. STAREK, III
Commissioner, Federal Trade Commission

JANET D. STEIGER
Commissioner, Federal Trade Commission

CHRISTINE A. VARNEY
Commissioner, Federal Trade Commission

JODIE BERNSTEIN
Director, Bureau of Consumer Protection

ELAINE KOLISH
Acting Associate Director, Division of Economics

DEAN GRAYBILL
Associate Director, Services Industry Practices

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SPEAKERS (Continued):

EILEEN HARRINGTON
Federal Trade Commission

JONATHAN BAKER
Federal Trade Commission

GERALD LEVIN
Chairman and Chief Executive Officer, Time Warner

DICK DUNCAN
Editor, Time Inc. News Media

ERIC TvETER
Vice President, General Manager
Time Warner Communications, Manhattan

STEVE PEARSE
Senior Vice President, Engineering, Denver

TAMMY LINDSAY
Vice President for Communications,
Full Service Network, Orlando

SCOTT BLAKE HARRIS
Chief, International Bureau,
Federal Communications Commission

RICHARD D. HELD
Senior Vice President, Risk Management and Security,
Visa International

RACHEL LARABIE-LeSIEUR
Director, Marketing Practices, Industry Canada

GORDON ZUBROD
Assistant United States Attorney,
Middle District of Pennsylvania
SPEAKERS (Continued):

RICHARD G. MEIER  
Deputy Associate Trade Representative,  
Office of United States Trade Representative

ROBERT P. HALL III  
Vice President, Government Affairs Counsel,  
National Retail Federation

WILLIAM MacLEOD  
Collier, Shannon & Scott

MARI ANN BLATCH  
Vice President, Government Affairs, Readers Digest

STEVEN SPIVAK  
Professor, University of Maryland  
Chairman, Consumer Policy Committee,  
International Organization for Standardization

SUSAN LORD  
Vice President, Government Relations,  
Springs Industries, Inc.,  
Chairman, Export Subcommittee, American Textile Manufacturers Institute

BRUCE SILVERGLADE  
Director, Legal Affairs, Center for Science in the Public Interest

ZANE BROWN  
Director General, Consumer Products Directorate,  
Industry Canada

JOSEPH HOFFMAN  
Director of Policy, Ontario Ministry of Consumer & Commercial Relations

E. TONI GUARINO  
Buc, Levitt & Beardsley,  
International Bar Association Council

CARL PRIESTLAND  
Chief Economist,  
American Apparel Manufacturers Association

MICHAEL THOMPSON  
Director, Government Relations,  
Whirlpool Corporation

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CHAIRMAN PITOFSKY: Good morning, everyone.

I might mention that for those of you who are standing three deep, there is an overflow room in 532, where this entire demonstration is available. And there's another one on the third floor below us. And so if you want, you can watch this demonstration down there.

This is a continuation of a set of hearings that we initiated almost two months ago. Our aim then was to examine whether changes that are taking place in the commercial world -- and with particular emphasis on the globalization of competition on the importance and pace of technological change -- suggest that a regulatory agency like this should review the way in which we interpret, of course, the antitrust laws and consumer protection laws.

We have, throughout these hearings, placed some emphasis on high-tech industries and the way in which competition and marketing is changing as a result of changes in the marketplace.

We begin this final day of consumer protection hearings with a special presentation and a demonstration of what the future may hold for consumers involving the convergence of interactive technologies, televisions, telephones and the computer.

We are delighted to have with us Mr. Gerald Levin,
Chairman and CEO of Time Warner, the world's largest media and entertainment company with interests in publishing, music, films, and television.

A leader in the telecommunication's revolution, Mr. Levin, present his vision of the marketplace in the year 2000. We will then actually see an interact with some of the technologies of the future.

Before he begins, let me say that these hearings are devoted to consumer protection issues primarily, and they involve questions of policy. Any case that might be pending, or will be pending in the future, is not relevant to the discussion that we are going to have today.

Mr. Levin, I want to thank you for coming down here, and I want to thank your colleagues and your people for devoting such time and energy and resources to what looks like what will be a fascinating presentation.

MR. LEVIN: Thank you very much, Mr. Chairman. And we welcome the opportunity to appear before you this morning. I'm going to give some remarks, and my full remarks will be available for the record. We'll have demonstrations; and then, obviously, we'd love to take questions.

I think it's pretty clear that the history of media and communications in this country has been shaped by a series of landmark breakthroughs that has profoundly
influenced every aspect of American life.

I think that, taken together, the interactive technologies that we're going to demonstrate this morning, represent another milestone. And, although, no one can say with certainty what the final uses of broadband digital systems will be, we already know that the impact on the traditional media structure will be profound.

Digital interactivity turns the old system of electronic distribution on its head.

Instead of a closed and tightly controlled kingdom divided among a handful of powerful networks, a vast democracy comes into existence in which the key to success is not size but creativity and quality.

I'd like to identify at least three benefits for the consumer.

First, the digital nature of the networks that you're going to see means a new universe of choice, because along with expanded programming choices, consumers can enjoy high-speed access to the Internet and an efficient, reliable, competitive alternative to local phone service.

And when it comes to programming, consumers will have the best of both worlds. The analog side of television, which now includes, in many cases, 75 channels of broadcast and cable; and then the digital side where there are no channels. The very concept of channels
disappears.

Whether it's what we call video-on-demand or transactional services or access to libraries or print or video, the consumer will have a range of options that really was unavailable and probably unimaginable in the home.

Secondly, at consumers gain, what we believe is, unprecedented control, control over the information and entertainment that they wish to bring in or, indeed, look out of their home.

When you have digital interactivity, consumers become, in effect, their own programmers, able to call up content when they want it and exactly what they want. In effect, they are programming their PC's or their televisions to keep out specific materials or entire categories.

In our view, this offers the ultimate in self-regulation, and that is total consumer discretion. And, indeed, we believe it enhances the applicable regulatory regimes, whether it's under the Cable Act or under the regulations administered by your Commission or the FCC, as it relates to telephone marketing.

And, third, whether it's been the telephone or the television or the personal computer, the whole thrust of this communications technology has been to make life more convenient, taking what was previously hard to find or obtain and putting it at consumers' fingertips.

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The deployment of broadband cable dramatically enhances that convenience. It opens an electronic path that is indifferent to the nature of the screen that it's plugged into. What matters solely are the wishes of those who are using either keyboard or a remote -- which we will show you shortly.

The purpose of our demonstration is to demonstrate some of the concrete ways in which we are bringing this technology today to consumers.

I want to underscore the fact that these are not theoretical prototypes. Each application that you will see is currently in use in consumers' homes.

Before we look at the specific demonstrations, I'd like to just talk about the applications and implications of the architecture that makes this possible.

It's really rather simple but quite elegant, because what we've done is combine the traditional coaxial cable together with trunk lines of fiber optic where each of these little strands of fiber represents enormous broadband capacity.

Art, maybe if you could pass these along to the Commission.

So, essentially, the architecture we're talking about combines this older coaxial cable with very modern fiber optics which was developed by our engineers. And

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we're already building all of our systems to conform to what's called this hybrid and fiber-rich coax architecture.

What happens when you install this technology, the systems are then easier to maintain and subject to far fewer repairs; you get a clearer, sharper picture and a significant expansion of channel capacity that gives the consumers new choice.

And once you upgrade the system with this architecture, with only incremental additions, we can begin to offer an array of new services that we're going to describe this morning.

As you'll see in some of the demonstrations, this kind of cable, fiber architecture is already revolutionizing the delivery of the Internet and on-line services. By plugging a personal computer into what's call a cable modem, consumers can gain access to the Internet 50 times faster than what's available over a conventional telephone line. As we move into the next year, we will be 100 times and, ultimately, 1,000 times faster than a normal telephone line.

We recognize the special uses and responsibilities that this brings to on-line services, particularly in education. We already provide free cable access to 85 percent of the elementary and secondary schools in our franchise areas; and we intend to wire the rest in the very near future.
We soon be equipping all of these schools with these cable modems, at no charge, and providing this expanded service, that you'll see today, directly into the classroom.

At our cable company, we are also wiring commercial sites for transmitting television signals into a personal computer.

What this innovation enables viewers to do is to -- assuming you're hooked into the same networks, is to follow fast-breaking news are, indeed, a presentation that's related to their work that's video but it's coming through their personal computer.

The power of the interactive networks that we're building means that, with the installation of huge, but cost-efficient digital switches and what are called home interface units that attach to the side of a house, consumers will now have a fast, highly reliable, completely digital, and competitively priced alternative to traditional local phone service.

At the moment in Rochester, New York, the nation's first deregulated telecommunications market, our cable company is providing phone service to a certain number of consumers. And this makes this the first cable operation that is actively engaged in offering consumers real dialing choices.
Elmira and Rochester are two steps in the evolution of cable into what we call the Full Service Network that, in my view, truly unlocks this digital realm.

Our network, the Full Service Network, is in Orlando; and here we have the world's first fully operational, digital, interactive television system.

We are currently offering this system to over 2,000 customers in what we call "video-on-demand." By the end of 1995 we expect to reach 4,000 customers, a goal that we set at the beginning of this year.

And although we're still in the learning stages about what consumers will demand, it's not too early to draw some conclusions. The fact that we've seen the participation of firms such Silicon Graphics, Scientific Atlanta, and AT&T in the development of this technology, clearly indicates that the leadership that our high-tech sector lost to foreign competitors in the 1970s and '80s is being regained.

Today, the American cable industry is at the forefront of a high-tech success story that is not only creating new manufacturing jobs in the United States but will clearly lead to the worldwide export of networks that are largely American conceived, designed, and built.

In terms of programming, though the world that we used to know of a fixed number of pre-determined offerings,
according to a very rigid schedule, will not disappear. There are today very exciting alternatives.

The Internet has already made clear that digital interactivity is radically altering consumers' expectations. More and more consumers are choosing to travel in the digital domain because they can tailor their information, their news, their sports, and their entertainment to their own tastes and their own time tables.

Interactive television will benefit from this trend but will also accelerate it. I think the effects that we will see will be profound for suppliers of content as well as consumers.

As long as there was a relatively narrow distribution channel through which consumers could receive programs, there was an artificial ceiling on supply. Now that this channel is being thrown open and the demand of consumers, freed from the narrow confines of broadcasting as we have known it, the ceiling on supply is lifted.

I would have to say that the former limits on distribution made life much easier for studios and producers. This new instant access on-demand world is infinitely more complex, more competitive, and certainly more creatively challenging.

In the digital world, the open-ended nature of the
demand creates a vast number of programming opportunities that no single company could ever hope to meet.

The end result will be a dynamic increase in the number of suppliers and producers and new creative relationships among companies of every size aimed at satisfying what is essentially now a global demand.

Now, the demonstrations that you're about to see can only hint at the dimensions of the changes we are already in the process of introducing to America's consumers.

It's my personal view that if we do it right, if we have the wisdom to do what is necessary to spur investment in these technologies, if we have the foresight to let the market operate to the benefit of consumers, I believe that the biggest winner of all will, in fact, be our American ingenuity, because this is a case where we lead the world in conceptualizing and programming these networks.

Now, we're going go to our demonstrations. We'll make this as informal as possible; and when we're through, obviously, we'd love to have the opportunity for questions. We're going to start by going to Elmira, New York. We have a direct line to our computer servers there. My colleague, Dick Duncan, who was an editor from Time Inc. News Media, is going to be your tour guide. Dick.
MR. DUNCAN: Thanks, Jerry.

Good morning.

MR. LEVIN: I'll just come over here, and I can help out.

MR. DUNCAN: What you're looking at is the welcome screen of the cable modem community service in Elmira, New York.

Let me introduce Frank Kyst, who's our communications chief.

What you're seeing here is coming down this morning from Elmira, from our server in Elmira. It's a little slower than it is -- just a bit slower than it is in Elmira, where it's 50 to 100 times faster than the conventional telephone dial-up service that most people use to get on-line.

The distinguishing characteristics of this service are its speed and its community content. It really emphasizes all sorts of information about the community, unlike other on-line services.

And as we go from screen to screen, it will be Frank who is clicking, who's clicking on our Elmira server and bringing information down to you.

MR. LEVIN: So the first point is to just acknowledge the speed. I think what's frustrating about current computer downloading is what we call the "tap time"
it takes just for a screen to fill up with a picture or with any kind of digital material.

The key -- which is a winner, I can assure you -- is the speed with which these frames appear upon the touch of the clicker. That will be the persistent theme here, instant access, speed.

Sorry to interrupt.

MR. DUNCAN: That's fine.

Let's go to news first, and we'll show you what's there.

You see the speed.

This is oriented around five news summaries: The Times, Daily News Summary, the People magazine news summary, Money magazine news summary, Tech Daily down there, and a summary put up by the Elmira Star Gazette, a newspaper in Elmira which is our partners on here.

And this is last night's news.

MR. LEVIN: See, just looking at that picture, how long it takes the computer to fill up, with the telephone speed, to lay out a picture for you, I think that's what really most remarkable. The consumers see that almost instantly.

MR. DUNCAN: And let's go to the Times Daily. We have got some pictures there, too.

"Washington goes back to work."

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And, in addition, on the screen, on this news, we have other features. We have Reuters News Service 24 hours a day, constantly updated; we have outside services which supply us with stock quotations and sports and scores 24 hours a day. That's the news on here.

But the largest amount of content is in this "About the Town" area, where we have -- this is a community connection. We go to the institutions, which really provide the infrastructure within the community: the hospitals, the churches, the city government, the chamber of commerce, the institutions of higher education. In fact, we help them come up on here and tell what they're about, where people can get information from them and communicate with them.

MR. LEVIN: That's because access is really very easy and very cost efficient. In a sense, almost any member of the community can go on-line and to be received in homes. That's what's remarkable, you know, we call it kind of voice of democracy.

MR. DUNCAN: Absolutely.

We also have another very important service on here which has to do with the schools. Time Warner Cable and Hewlett Packard are donating computers and modems to the public schools in this area. We are connecting the schools to the homes, the parents to the teachers, the kids to everybody, as well, through filtered Internet, where we can
turn the kids and the schools loose on the Internet and make
sure they don't get into trouble.

We also, parenthetically, have another kind of
Internet control on this entire service where the person who
is the subscriber to the service can select one of three
levels of Internet access for anyone in the household to
have. So that can be controlled by the subscriber.

MR. LEVIN: Again, a key point: Once everything
is digital, the ability to program through software to deny
access or to only receive certain categories can be put not
only in software that usually you see in a box called a
"computer" but on the system itself.

That's an emerging technological capability so
that in schools, the educational programming is what's
available in high-speed Internet access, not other material.
The same thing at home where the consumer has the ability to
provide "digital denial," essentially.

MR. DUNCAN: The area we call the library is an
area, first of all, devoted to the local library where we
have put the Steele Memorial Library from Elmira on-line.
They have their own programs here, including the card
catalog so that this library and its branches can be
accessed instantly by computer from any home.

We also have our own area which is a reference
where we put up the CIA World Fact Book for Geography,
Compton's Encyclopedia, some historical documents for kids who might be doing a paper from home, or for anyone who works from home, these things are easily accessible there.

Of course, no community is totally about work. We have another area, this one called "Delights and Diversions" devoted to whatever is going on in Elmira that's for fun.

We have the movie schedules for all of the cinemas around town. We have the television schedules. We have a local journalists who writes about things that are just pleasant going on in town.

Let's go back to this. Yeah.

Note, by the way, that this with kind of broadband speed the amount of information that can be transferred rapidly over fiber optics. We can get nice big color reproductions of still photos. And, of course, we can have some video.

We like autumn leaves. They do very well.

MR. LEVIN: So it would have taken -- to scroll down on a computer with a telephone modem, you would have just sat there as the picture unfolded in very slow time. That is a real distraction and an inconvenience. So the ability to receive full color photos, kind of instantly, on the click of your mouse, is the kind of source of consumer control that's a wonderment.

Whenever we demonstrate this and people sort of
realize that that's what it can do, there is instant
recognition of its value. Most people don't have a lot of
excess time. So this is not for demonstration purposes
only. This is connected to the computers in Elmira. This
is exactly -- it's actually not quite as fast. We couldn't
get full cable into the FTC building here, so it's not quite
as fast. But it gives you some sense of the timetable.

MR. DUNCAN: The business that's transacted on
this service is largely transacted in the shopping area.
Shopping has Dream Shop, National Catalog. It has other
features. It also has local ads. We're encouraging people
to put up advertising locally and to transact commerce this
way.

We, as well, have the Chamber of Commerce area
where businessmen can tell what they do; people can look
for jobs, that that sort of thing. We figure it can't get
much more micro in this area than "Wax-On Wax-Off" services.

But here's one, and that's how people can do
business on this service.

Another business aspect we have to foster the
business is what we call "Work At Home" our line-on service
where people can work from their home at the same speeds as
they could in their offices. We connect their homes to
their offices at these speeds so that have all of the
facilities and all of the computer capabilities that they

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have in their offices.

This pretty rounds out the service.

MR. LEVIN: Okay, Dick. Thanks a lot.

Let me just kind of underscore again what I think
the messages have been.

Live demonstration that was done with computers
Elmira.

Speed. Instant gratification. Instant access.

A filtration system.

The ability to use software, digital software to
prevent or control material that's coming in or being
accessed.

And finally -- well, it's sort of a sterile word:

Content. But local content. It so important to have
community material that's constantly available.

And you can see, whether it's the local newspaper
or the local library or the local school system, it's a form
of digital community that is as powerful as any of the
national or international material that's being brought into
Elmira.

And we have approximately 400 homes and 100
schools, libraries, and public institutions that have this
system and these cable modems.

So that's demonstration number one in Elmira.

We're going to turn now to our second
demonstration, which we're going to call "PC Television."

And I'm going to ask Eric Tveter to join me, who is Vice
President and General Manager of Time Warner Communications,
our system in Manhattan.

And he's going to show you how you can run a
television signal through a personal computer.

MR. TVETER: Thank you, Jerry.

PC-TV is an exciting product because for the first
time, Time Warner can deliver, approaching 100 channels
direct to the desktop in a local area network environment
and in a cost-effective manner.

It's a product designed for the business
marketplace. For 25 years, we have provided service to
businesses who have an insatiable thirst for information and
knowledged-based services. It's a product that has been
developed over the past year. It's a video distribution,
hardware and software system. You can see the equipment
here.

There's an equipment hub that would reside in a
central computer room. And from that computer room, video
is distributed to the desktop.

Chief information officers like the product
because it works on Windows, DOS, OS/2 operating systems.
It can work on a 286 as well as a Pentium.

MR. LEVIN: Excuse me, Eric.
What we were just doing is showing you how, with
the computer control, you can fill up the screen with the
video, go to another channel, go to CNBC or CNN or C-SPAN,
to take the whole screen or just a part of the screen while
you're working on your spreadsheet. That's the kind of
versatility you have here.

MR. TVETER: That, in fact, is the most important
quality. Most users leave the screen in the upper
right-hand corner, and they can work on Excel. In this
case, my colleague Mark Stark, who is assisting, is
adjusting an Excel spreadsheet. A journalist can be working
on the wordprocessing package and be watching Court TV.

It's a very powerful tool. Chief financial
officers like it because they no longer have deploy monitors
around the workplace. In New York City, there are 60,000 of
them; and today they can be integrated into the workstation
environment.

Chief executive officers, head of schools,
government agencies, they're able to use it, primarily by
customizing the programming. They can select, say, 10 out
of the 79 channels that we offer out of the Manhattan system
and have CNN, CNBC, Reuters Television, Dow Jones Investor
Network, Bloomberg, C-SPAN, the Weather Channel, and others.

Most importantly, customers like the feature. A
trader will want to -- may be working on a spreadsheet, and
Alan Greenspan is testifying before Congress. So he can click on the screen, bring it up to a full screen picture -- Mark, if you could do that -- and listen to Mr. Greenspan, hear the tone of his voice, watch his body language.

Wall Street bets billions of dollars on the direction of interest rates.

Again, a very powerful tool.

Journalists can be working at midnight and watching Court TV and can adjust an article that they're working on.

Schools, government can use it for training purposes.

Advertising agencies like to monitor the commercials that are being broadcast.

Hospitals are looking at it because they do not want to distribute video in a radio frequency mode. They want a narrow band because they're concerned about radio interference in the hospital environment with CAT Scans being done and the like.

We expect to roll out thousands of units in the next year with our business partner CCC. We spent the last year developing this product and just rolled it out last month and are receiving a lot of interest.

MR. LEVIN: Eric, thanks. I really appreciate it.

Let me just give you what I think this means.
We used to think that you get television and video material through a television set, and through a PC would come the material that you could scroll over, spreadsheets or wordprocessing.

What this tells you is this buzzword of "convergence" is real, psychologically that, in fact, it is material assistance to have the television feed coming through your PC.

I know in my office, I have the television screens going on. I would like this service because, in a sense, a news wire is insufficient these days. You need to see, to look at the nuance of presentation, so that I can continue to do my work on my PC, but this screen is already on and it can catch my eye when there's something quite relevant.

So I think, again, all of our preconceptions about display screens for PC or television are going to get pushed aside by these very practical uses.

MR. TVETER: One other point, people can broadcast messages. You can have a daily message and distribute that among the workplace.

So, again, it's a very powerful tool.

MR. LEVIN: Thanks very much, Eric.

That's, again, the ability to use video for communications purposes.

Let's turn now to what we call "Cable Telephony"
so that we use the cable in its digital format to deliver telephone service that you're familiar with.

I'm going to call up Steve Pearse, who is our Senior Vice President of Engineering at our network operations center in Denver.

Steve.

MR. PEARSE: Thank you, Jerry.

The message I'd like to leave with you today is that Time Warner is in cable telephony services right now, today, in Rochester, New York. We are providing service to apartment buildings as well as single family residents. And I think this is a very important event in the history of telecommunications. And the reason why is because, for the first time, our customers in Rochester have a choice. Previously, you had to call your local telephone to provide the only telephone service you could receive.

Now you can call Time Warner to receive your local telephone service. And we're going to complete with the local telephone company on price, features, and quality. And we'll talk a little bit more about those attributes in a few minutes.

But first you might be thinking: How is a cable company going to provide you telephone service?

It gets a little complicated, but I'll try to show you, on a schematic here, exactly what I'm talking about.
Let's start in the home. This is a typical home. You have a cable TV, telephone, and a PC. All these things can be connected to your cable coming into your home.

The new element here is, outside the house, there's a little gray box -- and I'm going to show you that in a minute -- that's called a "network interface unit."

Time Warner will puts its network interface unit on the cable, and it will extract the telephone signals coming over the at cable and provide it throughout the home on the very same telephone system and wiring you have today; but it comes over your cable.

This is connected to the normal cable system running throughout your neighborhood. But there's a difference now. The cable is terminated on a little device called a "fiber node" in your neighborhood. It takes the cable signals and converts into a fiber optic signal. And that increased the quality. It allows much greater bandwidth for more services. And we're upgrading our entire nationwide network with this fiber optic system.

From the neighborhood, the fiber optics run all the way into a building in your community; and it's called a cable head end. The head end is the location where you have your satellite dishes receive broadcast television signals and off-the-air television signals and feeds that into your neighborhoods and into your home.
But in the cable head end, we have now installed a telephone switch. We buy ours from AT&T, for example. This telephone switch talks to the outside world. It connects to long-distance companies and the other local telephone company. And that's at the heart of the matter. We have to negotiate an interconnect agreement with the other local telephone company so we can terminate calls where they are.

And that's why we are very interested in what's happening with Congress right now with the telephone bill, because we want to make sure the barriers to entry for us are dealt with fairly.

Once we have that agreement, we can provide all of these telephone services.

Down here, we have the same thing that happens in the home, but it's in an apartment building. And we have special equipment in the basement to handle telephone signals there.

MR. LEVIN: All right. Steve, maybe we could make a telephone call?

But as we are doing it, if I could just emphasize that there are no telephone wires here, no twisted pair.

This is all digital bandwidth. And the way we manage it in our cable system, some of this bandwidth that's being switched in the home, is sending a movie. There are movies in these digits. Others are telephone conversations
or a picture or music. It could be a book. But they are all 1's and 0's that this switch sublimely indifferent to what's passing through. But, in fact, you really have a totally new concept -- and, you know, in your home, the telephone handset is exactly the same, and you have your telephone wiring. It's what happens outside the home in this digital box.

So why don't we make a call to Denver and make sure it works.

MR. PEARSE: This equipment we have here is exactly what we're using in Rochester, New York. This equipment is located in that building, the cable head end.

And behind there is the fiber optics and the cable system that ends up at your home. In fact, this is the little gray box. In fact, if you walk outside your home today, you'll see a little gray box just like this. It's from your local telephone company. This is our little gray box, in place of the local telephone company's.

It's better than theirs because it is a digital box. Today you have about a mile of 100-year technology, it's all twisted pair, it winds its way through your neighborhood into your house for your telephone. It's analogue, and it can pick up noise and interference.

This is digital, so it's superior in quality. But this cable comes in, and this box picks off and listens to
the telephone signals and let's all the other signals go
through here that go to the home, like the cable modem, a
basic cable, the Full Service Network functions. It just
picks up what it wants to listen to, the telephone piece.

This is working right now, so I have to handle it
carefully. This is what's going to be on the home. And
it's connected to this telephone. We will call Denver, to
our national operations center, which monitors our
nationwide network on a 24 hour, 7-day basis.

(Dialing.)

MR. LEVIN: You pre-programmed the number?
MR. PEARSE: Yeah, I had this on speed dial.
MR. LEVIN: This is a our operating center.
Someone better pick up.

(The following is a transcription of the telephone
call placed to Denver.)

MR. FRENCH: Central Communication, national
operations center. This is French.
MR. PEARSE: Hi, French. This is Steve Pearse at
the FTC hearing.

MR. FRENCH: Yes, sir.
MR. PEARSE: How are things going?
Could you tell the folks listening in how many
sites we currently monitor today.

MR. FRENCH: We have 15 sites.
MR. PEARSE: How are things going in Rochester, where our first telephone network is operating?

MR. FRENCH: Our switch is doing -- at the moment, is running clean and it's green.

MR. PEARSE: He's looking at the monitor.

Thanks a lot, French.

MR. FRENCH: Yes.

(End of telephone call.)

MR. LEVIN: We tried this earlier and got David Letterman on the phone.

Essentially, we have an operations center -- I'm going to ask Steve kind of the last question here as to why -- I believe we have the most sophisticated telephone operating center in the country -- how can a cable company have that?

What you have just heard is that all of this is centrally monitored. And when we mentioned all those cities, we have what's called business competitive access where we are providing telephone service for business customers to bypass their local phone company to interconnect with their long distance company. And we're doing that in 15 cities. The first residential full dial tone telephony is in Rochester.

So what's the answer to the question: How could we have the most advanced telephone center when we just
started?

MR. PEARSE: Okay. I'll answer that and then make one point.

MR. LEVIN: Okay. Good.

MR. PEARSE: We, basically, started from a clean slate. Current telephone companies have a rich 100-year-old tradition; but they also have software that's 30, 40 years old in assembly language. They have a lot of legacy kind of that's in the nature of their business.

We hired some of the best talent in the industry to come in and say: If you were to do a telephone company right, what would you do? And they are having a field day doing that. We're using the latest and greatest technology for software, hardware, transmission systems, everything.

So that's why you see some of the abilities we have here, done on a very efficient basis and a very rapid iteration basis.

One more key point I'd like to make, Jerry, is because of the architect we have, where you have a cable coming into your home and you're listening to and responding to any information you want to hear, it let's you do new features.

We just made what's called a "POTS," That's in telephone jargon. "Plain old telephone service." POTS.

But the "PANS," the Positively Amazing New Stuff,
we're going to do -- "POTS" and "PANS" -- is going to be introduced -- let's say you're sitting down at dinner and the phone starts ringing, do you answer the phone or not?

One feature we can do is, through the new generations of set-top boxes, you can look at the TV set and see the name and the number of the person calling you at that moment; and you can decide: I don't want to answer the phone call right now. You can even decide: I never want to receive a phone call from that number again.

These are some of the things that you can do with this kind of architect over the cable system. Over the next several years, we're finishing the upgrade of our cable networks with this hybrid fiber-coax architecture; so you will be able to see these services rolled out nationwide as we finish up our upgrades.

Thank you very much.

MR. LEVIN: Thank you, Steve.

So that was cable telephony.

We're now going to conclude with what I think is a new experience for consumers; and that is a digital interactive television.

I'm going to asked Tammy Lindsay to do this presentation. Tammy is our Vice President for Communications in Orlando in what we call the Full Service Network. She is going to use a remote control. And what we
will try and do is pass one of those around to you so you can see what it looks like.

Tammy.

MS. LINDSAY: Thank you, Jerry.

It's my pleasure to show you the world's first digital interactive television network. It is fully operational, working in paying customer homes and has been since December of last year.

The Full Service Network programming is all digital, as Jerry has been describing. And it's loaded on computer servers that hold vast amount of storage capacities and programs like movies, shopping, and games and the things that I'm going to show you today.

Because it's digital, you can access it as a consumer at your convenience. So the premise behind the Full Service Network is to provide consumers greater choice, more control over the programming that comes into their homes, greater convenience so they can access it when they want to rather than when it's programmed to air, and also the ability to customize the Full Service Network for every individual in the household.

When we sign on customers to the Full Service Network, we give them this remote control. This accesses not only the digital services of the Full Service Network but also the regular broadcasting cable TV signals that come...
into the home. So this is the only remote that you'll need to access all those services.

We also provide them with home communications terminals. This is the black box here. It's essentially a Scientific Atlanta cable converter box, an 8600 X, in the upper left-hand corner. And it has been integrated with a Silicon Graphics computer workstation platform. There's a lot of computer processing power in this box. We put essentially the computer processing power behind television to make it interactive.

Also we provide the Hewlett Packard color Desk Jet 550C printer. In some of the shopping applications and others, like games, it actually gives the consumers the ability to download full color graphics for things like game instructions, recipes, maps, and the like. And this is an example of the color graphics that come out into your home.

MR. LEVIN: So what you're saying is that's what you would associate with the computer printer, but it also associated with a television set. There is an extremely powerful computer in that box. And, in essence, what we've got here are 200 million old fashioned television sets out there. We really put all this computing power behind that and say: Now, for those people who don't want to use a keyboard or a mouse, who are computer intimidated, all you need to use -- the assignment here was to be able to control
video coming through a television set with something that looks like a remote control.

And so you essentially have an electronic VCR. That's all this is, but it took more computational programming than it took to put a person on the moon to pull this off.

MS. LINDSAY: That's correct.

But the point for the consumer is that it's very easy to use. It's transparent to the consumer, all this computer processing power behind it.

We have made specific use of color coding on the remote, for the buttons that you use most often, to manipulate your way around the network. In the center you see this arrow key that allows you to go in eight directions, left, right, up, down, and diagonally; and then the green select button you press any time you want to enter or complete a transaction.

With that background, I'm going to show you how consumers actually interface. We have downloaded some of the video assets, just a portion of them, from Orlando and brought them into a small computer server here to D.C. to show it to you.

But the consumers access the network through the carousel. And what I'm doing is depressing the arrow key to the right, and it will actually turn the wheel. And I can
turn it to the left, because I'm the consumer, I'm in total
control of that.

As you see, as a venue is highlighted, I can press
the green select button, stop, and enter that venue; or I
could punch in the channel number that we've assigned to
each venue.

And we only did that -- it's really unlimited
channel capacity, but we have done that to help bridge the
gap for consumers because they are very comfortable with
channels and channel surfing.

MR. LEVIN: One point to note, there are no
channels here. We are on the digital side. There is a
switch bringing a television program from a big computer
that is going right into your home.

But most people think in terms of channels. So to
provide easy access, we are saying movies are on channel --

MS. LINDSAY: 98.

MR. LEVIN: --98. There is no channel 90. So
when we say "digital domain," it's real. It is kind of
cyberspace. But if you said that to consumer, it would be
disorienting. So, in effect, like an old fashion channel,
you can go in and get those movies; but there are no
channels.

MS. LINDSAY: Okay.

With that, we talked about control.
I'm going to show you in the controls venue, this is where you would enter the Full Service Network, the administrative area. It's where you can customize the network for every member of the household, save your personal favorites to personal lists, favorite movies, and things like that.

And you can get how-to video tutorials. We don't give a written manual on the Full Service Network. We show you on television because it's fun and entertaining and a lot easier to use.

In a TV setting, this is where a parent is important to enter because this is where you can actually program in purchase locks. Through the use of a pin number, you can make sure that little Johnny doesn't buy things when you're not at home.

You can actually block out movies based on their rating at your discretion. And you can block out channels, regular broadcast, cable, or digital Full Service Network channels in the TV settings mode.

Now, back to the carousel. I want to show you one of the popular applications, of course, is the home video theater.

And as Jerry mentioned, we have that on pseudo channel 98. The home video theater puts you into a list of all the movies we have available on the network. This is
just a sampling; but in Orlando, we have about 97 movie
titles available today.

    We have categorized these movies. So if you just
like action films, you can scroll up to action and just get
those.

    Now in A-to-Z, you can see on the right we have
listed all the movies available on the network in
alphabetical order.

    Now, Ace Ventura Pet Detective is highlighted, and
you get the video promo -- to give you an idea of what the
movie is about playing -- behind it.

    And as I scroll through movie to movie, my video
promo is going to change.

    Now what's happening there is that I'm traveling
from the box through coaxial cable, down to a node in the
neighborhood, which transforms it into an audio signal, back
12 miles to our network operations center, that houses
equipment like the AT&T ATM switch and the computer servers
that store all the program.

    And then it's actually sent in ATM packets quickly
through the home communications terminal that streams the
data and decompresses it and displays it on the television
screen in less than half a second.

    You can see how fast the video programming is.

    Now let's say I want to order a movie, Outbreak,
for instance. If I press the green select button, I'm taken
to an order screen. We have made the movies free for you to
today. But in Orlando we are charging for --

MR. LEVIN: We're running a special for the
Commission today. It's $3.95.

MS. LINDSAY: The movies vary in price. They
range from $1.95 to $4.95.

And to order the movie, all I would do -- now, I
also should point out that we give you a brief description
of the film, tell you how long the movie lasts and give you
a running length time we are giving you access to the film.

We are varying that from one and a half times the
length of the movie to three times the length of the movie.
And we'll be playing around with that with consumers to
determine what they want.

Now, to finish my order, I just press the A
button, and then I'm asked to confirm my order, in case the
dog stepped on the remote, which happens in homes. So we
have to hit the B button. And I'm reminded that I have full
VCR-type functionality.

MR. LEVIN: These are the VCR symbols.

Now the movie is started.

Instant access.

On demand.

Now the credits -- can we --
MS. LINDSAY: Now I can fast forward through the credits.

MR. LEVIN: Yeah, let's fast forward through the credits.

MS. LINDSAY: Now, there's no crazy lines like you would see on a VCR, you might note.

MR. LEVIN: Can you --

MS. LINDSAY: I can also resume play of the movie. I can skip forward by hitting the skip forward button, and it then jumps in 10 minutes increments through the film. So I can look for my favorite seen. I can skip back the same way.

And, of course, if the phone rings, Jerry, I can press pause. And it's going to remember the scene, right there and let me go answer the phone, answer the door, do whatever I want to do.

MR. LEVIN: Excuse me, Tammy.

Great ideas can be conceived in a very simple phenomenon.

All we want to be able to do is provide a movie on demand that you can be able to handle the problem if you're watching television, the phone rings and you can't stop it. We know you can do that with a VCR. Why can't we do that digitally? Once you can do that, then there are so many other capabilities.
Go ahead.

MS. LINDSAY: I'm just going to send it to improv. And I put the bookmark right there at that sign for a moment on the screen.

And then I can go out and do something else on the Full Service Network.

See, it reminds me that I have a movie in progress.

MR. LEVIN: And the time remaining.

MS. LINDSAY: Now, I'm going to jump quickly to the shopping venue just to show you some of the stores available in our Dream Shop. And we provide consumer access and delivery 3 to 10 working days from any of these stores. And many of these are available on the Full Service Network, and some will be added by the end of the year.

But I would like to point out, of course, the post office is a popular application because you can actually order stamps and have them delivered to your door through the postman the next morning. So it's very, very popular with our customers.

I'm going to quickly jump back into the games venue.

MR. LEVIN: Okay.

MS. LINDSAY: Here we go. We call it the "Play Way. And you see "Skate Kid" is going to help the kids get

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down this roller coaster ride to get to all the games. We have four network games that you play using the remote control, and then we have 16 Atari Jaguar games that you play using the Atari Jaguar game unit.

The TV box that's shown on the screen allows 16 households to play this game simultaneously. So you can even join a game in progress. You can have a game with your neighborhood.

It's a lot of fun.

I'm going to quickly go back out to the carousel, in the interest of time, and I'm going -- should I jump back to the movie, Jerry, and see what happened with that?

MR. LEVIN: Sure.

MS. LINDSAY: It shows me that I have a movie in progress, that it's called Outbreak. And I just press the select button. And, boom, there I am right at the scene, just as I left it. So I never miss a beat. And I can have full VCR functionality.

MR. LEVIN: You want to fast forward and see that again?

Now stop.

And rewind.

All right. So it looks simple, but that capability isn't very different from what we were doing with the PC where you were scrolling up and down, except here
The concept was basically to say that a compactible form of communication is what we call full motion video. If I can control that and manipulate that, we call it video-on-demand. What else can I do? So I would like Tammy to show you what we're about to do. It may not be commercially viable, but it's something that we have been working on for a year and a half, and that is news on demand.

If I can pull up a movie, why can't I pull out the video news?

MS. LINDSAY: We call it the "News Exchange." And it allows you to pull up the news at your convenience. If you miss the 6 p.m. or 11 o'clock news, when are you going to be able to watch it?

You can watch it here on the News Exchange. What we have done is digest the day's news. You can get it from a local news anchor like you normally would, or you can go to the category of news and --

MR. LEVIN: You can stop this news anchor.

MS. LINDSAY: Right. You can move from local to world and national news. I can enter that category and see where we have categorized all the news.

Now, this is being developed by Time Inc. working with CNN, and ABC, NBC; the Tribune Company; the Weather
Channel; and, of course, the Tribune Company owns the Orlando Sentinel, so we get local news and information.

Now, if I wanted to see the latest World News Tonight, a 20/20 program, or any of these, I can actually pull it up on demand and then have full VCR functionality.

MR. LEVIN: Why don't we try "Cross Fire"?

Again, controlling this news program the same way we control the movie.

MS. LINDSAY: All right. Here's the fast forward.

MR. LEVIN: Okay.

MS. LINDSAY: We have many other services under development today, and I invite you to come to Orlando to try the real thing out for yourself.

Thank you.

MR. LEVIN: Basically, we don't know -- I guess we can put the logo back up.

I don't know how consumers will react to this concept of news on demand, but essentially what we're trying to do by creating the technology is, now you turn it over to people who are much brighter and more creative than we are to figure out how to use it.

I'm very anxious to see whether this, what we call command and control, can apply to all forms of programming.

So let me try and give a kind of impromptu summary, and then we'll go to questions.

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Basically when you have digital capability, you have on-demand speed, instant access. It's a very significant consumer characteristic.

Secondly, because it's digital, you can program the software; you can have denial devices, filtering systems that are very interesting in terms of consumer protection.

The third is that -- and this is hard to explain -- everything becomes a telephone call. When I pick up the telephone handled set, when I use my mouse with a PC, or when I use this remote control for the TV, it's all going back to a server; the server can be in the community, it can be somewhere in our country, it can be somewhere around the world. And there is a switch, a very intelligent switch that's satisfying my command with a personal direct program -- it could be a telephone conversation, video, local news -- that is basically coming to me.

So my own view is that this is a marvelous form -- and I don't mean to get too philosophic about it -- self-actualization, that instead of having just a relatively limited set of materials that are thrown at me by companies who in the media and entertainment business, I am assembling, digitally what I want and what really reflects my personality. It's just as if I come into your home, I can see what magazines are on the coffee table and see your furniture. It says a lot about individual personality.
So I think it's highly significant.
The last thing I'd say, not to confuse you,
everything that was seen today is electronic digital
distribution. There's a whole other side of what we call
hard copy digital capability, something called a digital
video disk, which we have been much pushing.
And we now have a worldwide standard for movies,
for music, for multi-media information, for computer storage
that can do on a five inch disk a lot of what you have seen
today, except this is real-time.
So this is the digital revolution. I'm sorry we
took so long. But I think that gives you some idea, some
experience of what it is.
That concludes our demonstration.
CHAIRMAN PITOFSKY: Well, thank you, very much. I
think we are all in Future Shock, but we'll pull ourselves
together to try and ask a few questions here; and I think
maybe we'll run over a little bit here. This is worth our
time.
I wonder if you'd say a little bit more about
access. I mean, I see that you can purchase a movie, you
can buy a PC, I guess, you can buy a hearing aid and so
forth, you can buy a news service.
Down the road, how do you see the decisions made?
It's like a shelf space question. How do you see the
decisions made as to who gets on this screen?

Suppose there are five companies selling PC's and a sixth wants to get on the screen, would they pay for that opportunity?

MR. LEVIN: Well, the question, to get access onto the network, is a fascinating questions.

We're already seeing, I think, on the Internet, where the cost of getting on to a network is so relatively small that there are no real barriers to entry any more.

I'll give you a very prosaic example on the Internet that's of great interest to a lot of companies that involves copyright protection and other issues.

We are almost at the point where you could have what's called real-time audio on the Internet so that anyone, anywhere in the world, in the garage or in a home, with a PC and a fairly simple application modem can go on to the Internet with real-time audio and can, in effect, start what we used to call a radio station. That could be received or accessed by anybody.

So I think we need to shift our whole concept of limited, you know, gatekeeping limited access.

Now, let's fast forward to this rather robust digital television. What about access there? And here we try to make the point -- it's very hard to get your arms around it because you're so used to thinking about channels
and just a couple of channels on a television set -- but when we go into this digital domain, there are no channels. So anybody with a server, with a digital server, who can put material on that server can be accessed.

I mean, for example, in a community, in Elmira, if we had the Full Service Network running there, people who are inputting from the schools or from the libraries could input video, because video cameras as we know -- and we should have demonstrated one -- are small as a little pocket light that can be digitize and put right on the system.

So think about television that can be inserted in this system. And as long as I have now come to what's important from a software point of view, you do need navigation, you do need the ability -- that's why these web browsers, navigation browsers -- you need some kind of software that can open up your access to everything that's on the system.

So, it's a long-winded answer to say that we have to throw out our old ideas of -- that's why we even use the phrase "broadband" versus "narrow," that, in fact, the digital math is working in our favor.

I'll give another example. The big switch that we use in Orlando to switch television into the home was a multi-million dollar switch. It's now several hundred thousand dollars, and that price is going down so that
individual digital applications, I think, will be highly
cost-efficient. There is something called Moore's Laws that
every 18 months the capacity doubles, triples, ten times;
and the cost gets reduced by almost 50 percent.

COMMISSIONER VARNEY: Mr. Levin, is that to say,
then, in the demonstration from Elmira and the demonstration
from Orlando, I think in both of those you had shopping
categories.

MR. LEVIN: Right.

COMMISSIONER VARNEY: So your network or your
corporate organization exercises no control over who gets
on?

MR. LEVIN: Yeah, that's a good question,
Commissioner Varney.

Our intention -- I mean, obviously in this early
stage, we've had to round up people because you have to kind
of digitize and you have to be, in a sense, somewhat of a
pioneer to want to do it.

But the intention, as Tammy mentioned, we're going
to put Best Buys on, like 250,000 items. We want to be, you
know, almost a near-infinite department store or retail
operation, where, essentially, we want to get as much into
this system as possible. And when you recognize,
physically, that we ultimately do not control the system.
We've have to start this up so that people can see it's
done. And there are servers, yes, that we have in Orlando. But what we want is a communications system that will tap into anybody's server, anywhere in the country, anywhere in the world. That's why I think the Internet is a terrific kind of analogue to what it means.

So what we want to do, as a system, is simply to get consumers interested in this so they can eventually communicate. That's why I came back to, it's all like a telephone conversation; it's a form of communication; it's not a form of -- it's kind of the packaging or delivery on our part.

CHAIRMAN PITOFSKY: I have one other question on behalf of many people in the room here. Forgetting about the hardware, do you have any estimate of what this is going to cost once you really have this thing rolled out?

MR. LEVIN: You mean for the consumer?

CHAIRMAN PITOFSKY: Yes.

MR. LEVIN: We are looking at what I'll call the cable model, and the cable model is a very interesting one, not just because it's an industry that I came from.

And that is, when we put all of this equipment -- instead of you're going to a store and purchasing consumer electronics and computer, which changes fairly rapidly and it has to be replaced -- because of cost-efficiencies of
using kind of a system that will replace this box, will
replace the switch and move it to another system,
essentially what I believe we will provide for the consumer
is that you will have the basic charge that you'll need to
subscribe to the cable system. And most of what we've
shown, to order a movie or something, will be on a -- kind
of a per choice or per view basis.

The interesting question for us -- and things that
we are working with the FCC on -- are the kind of material
that we want to provide as a base charge. For example, we
are going to wire up schools and provide these cable modems.

But for the consumer, we're not talking about a
huge bill. I think the way to look at is, like Tammy said,
going to the post office electronically. Well, I will be
billed for my stamps; but it's something that I would have
paid to the post office anyhow.

It's the same thing with the movie: I might have
gone to the video store and paid a couple of dollars to rent
a video.

So these are really -- you're purchasing
something. It's essentially substitution economics. The
same thing with the digital telephony.

So we are not looking at what we think are high
charges.

One thing we do worry about in addition to a whole
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other subject, privacy and data collection, is what I'll call a fear of "We don't want to create information aristocracies." We definitely want this kind of technology to be available to everyone.

And one thing I would say to you that, by working so hard in Orlando, instead of an average consumer having to purchase very significant computing power, we are trying to bring that cost down so that it's available to the consumer.

COMMISSIONER STAREK: I had one question. From what I've heard this morning, it sounds like you made a giant leap over the technology that is available and currently in use by the regional telephone companies.

I was wondering if it's necessary for this system to have some sort of a strategic alliance with the regional companies for the system to operate?

And if it is, do you foresee a variety of those kinds of alliances and relationships with regional telephone companies?

MR. LEVIN: Well, Commissioner, it's a very question. Because, you know, obviously public policy intersects with the financing mechanisms in the marketplace.

I strongly believe that we are in a period where we have an opportunity to build the infrastructure to create this kind of digital interactivity. And it is heavy capital requirement, and I do believe we are in the forefront,
worldwide of this kind of networking. And, in fact, it is a
model for export around the world.

So if I were designing public policy -- which I'm, obviously, am not -- I would encourage relationships between telephone companies, cable companies, computer companies, in some form of joint venture, common use of certain facilities so there isn't capital duplication for the sake of constructing the infrastructure because I think it's a central characteristic, is to provide such abundant, interactive, on-demand opportunity that everyone will be competing. But the challenge for America is to build this digital highway. And I just think the public policy ought to encourage this.

I think there are a lot of theories that are in our law that are really 19th century theories. They don't take into account this digital reality. So we, in fact, have relationships with the telephone companies. But you have to kind of work your way through regulations in order to make it happen.

And the last thing I would say is that every company has been operating in a slightly zone. Cable companies have been, in the past, delivering one-way video; telephone companies have been used to second-by-second monitoring of switched signals. We're really talking about the convergence of that. And then I add one other thing,
and that is computer software.

So somehow if we could have an relationships so that the financial markets -- because I do believe this needs to be private sector financed -- can feel comfortable that the infrastructure will be built and then there's robust competition on the system.

COMMISSIONER STEIGER: On the question of that infrastructure, it sounded to me as though area you're working with now for the optic fiber interconnects is possibly somewhat small. There is a gray box on my house. A block ago there's the black box to interface the signals from my box.

If this is the case, do you expect that that area, before you need a middle server, another black box, is going to increase?

And, if not, what does that say about the difficulty of optic fiber ing a neighborhood?

MR. LEVIN: Well, I think what we're seeing -- and I've probably understated the development that's already taken place, Commissioner Steiger. Because, in fact, the cable industry, in what we call this fiber upgrade, is laying, each day, miles -- and now thousands of miles of fiber and connecting the head end to what we call the neighborhood.

And then I think the economic elegance of this was

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to retain the last mile of coaxial cable, which is the most expensive part of the system. You don't need to replace that.

So that if you change out this trunk line and to fiber optics and go to neighborhoods of about 400 or 500 people and then retain the coaxial cable, you have a highly cost-efficient system.

So when we talk about upgrading cable, remember cable passes today about 90 percent of the homes in America. So there is coaxial cable running past almost 90 percent of the homes, 65 percent actually subscribe. So this process of changing out, putting all this fiber in, is underway today.

I think the architecture of that we need to have. And I believe over the next several years, you will see that put in place. But it takes advantage of the fact that this last mile of coaxial cable is not taken out. It's the most expensive part and it gets retained.

Then we, by, really, electrifying the system with all of this switching power, you have converted what was formally a rather prosaic tree and branch plumbing system to a very magnificent switch-star digital system.

COMMISSIONER VARNEY: I just have one question, and I'm not very technologically sophisticated, so I'm a little apprehensive.
MR. LEVIN: Nor am I. I'm able to deal with the literature.

COMMISSIONER VARNEY: It shows in your profit, right?

If the coaxial cable and the fiber optic upgrade is combined into this one system that can deliver this tremendous capacity like we have seen in Orlando, do we end up in 20 years with one system, like we had with AT&T, that basically delivered phone services throughout the country? Are we seeing the future where there's only one game in town?

MR. LEVIN: Well, you have asked the question of the ages.

If I back up and say that I think we should encourage the construction of this capacity, what's the best -- from a public policy point of few and for the financial markets and for our global situation, what's the best structure to kind of let this go?

Then, somewhere down the road -- and you know, I know regulation of vertical integration kind of runs in cycles -- you know, where are we at that point?

My own view is that it's important to construct the infrastructure and that, through some collaboration, that's probably helpful, rather than having duplicative facilities.
And I think you can throw old ideas like common
carrier and other regulatory forms, because I think then
what you'll have is, everybody is kind of converging on
providing lots of software, lots of navigation systems, lots
of access so that there will be a highly, robust form of
competition in this infrastructure if we just kind of let it
get built.

So, you know, I will go out on a limb and say,
even if 20 years there is, essentially, basically one piece
of infrastructure here, there will be so many switches, so
many components used by so many different players that it
almost doesn't matter.

CHAIRMAN PITOFSKY: Well, let me thank you, again.
We are extremely grateful for this extraordinary
presentation. It brings to a climax the issues that we have
been addressing and illustrates the point that, as
regulators, we've got to understand the way the world is
changing and make sure that our thinking is not devoted to
an earlier era but is adjusted to these new realities.

And I want to thank you, again, form coming down.
Incidentally, we will resume these hearings in
room 332 so that the Time Warner can retrieve their
equipment.

(Whereupon, a short recess was taken.)
COMMISSIONER STAREK: Good morning, again.

We are continuing our series of hearings on global competition and consumer protection enforcement in the future.

We had a fascinating presentation this morning about what we can expect with the convergence of the three technologies that we have been discussing: the television, the telephone, and the computer. I thought it was fascinating. For those of you who had an opportunity to see, I suspect you agree.

We're going to move now to what I consider the guts of the program, which is how enforcement agencies are going to react to fraud and deception in international markets. With the new technologies that we've learned about in the previous three days, how is it, then, that enforcement agencies are going to respond when the inevitable occurs? And that is that scam artists, and others with fraudulent intent, will use advanced technologies to provide even more sophisticated scams in the future.

I think we have assembled a very interesting panel this morning. And what I thought we would do is to hear from our panelists initially and then have some questions and open it up to discussion.

And I think we'll start with the feds here.
first witness is representing the U.S. Department of
Justice. His name is Gordon Zubrod. He's an Assistant
United States Attorney for the Middle District of
Pennsylvania. He is a Senior Litigator for the U.S.
Attorney's office there and has extensive criminal
prosecution experience, including many cases that involved
economic fraud.

When I first came to the Commission, we were
bringing a lot of cases involving all sorts of fraud, but we
were having a difficult time pursuing criminal charges
against our most egregious defendants. Our friends in the
Justice Department were very bogged down with drug cases and
other major criminal conspiracies. But in the time that
I've been here, which has been about five years, we've seen
this enormous response from our colleagues at the Justice
Department, the Federal criminal prosecutors who work with
this Agency, the FCC, and other agencies that are
prosecuting in fraud and trying to put together cases where
one of the remedies is the most severe: Criminal penalties.

So, Gordon, thank you for coming; and we look
forward to your remarks.

MR. ZUBROD: Well, thank you, Commissioner, for
inviting us to this. It's been a fascinating presentation
so far; and I definitely feel like I'm in the vanilla league
after watching the presentation that just preceded.
COMMISSIONER STAREK: I can't even get my remote to work. So I'll be really lost when I've got to do all these things with a remote.

MR. ZUBROD: This whole field of high technology and communication is one that we have a real concern about; because you look out on the Internet, and I just know that the frauders, scam artists see the fields ripe for harvest.

And the dual concern we have is that they will be able to create some virtual reality mechanism whereby they give themselves legitimacy, technologically, that they don't have in reality.

The second one is the ability to cover their moves by being able to leap from place to place technologically and really be around the corner; and it would take forever to locate them, and by the time you do, they have moved on and set up in another place.

My point today is that the fraud -- however, having said that, fraud is not intrinsically technological, that the sophistication is psychological and not technological; and the technology is the not the driving force behind it.

The thing that, having been in this particularly economic crime now for about 15 years, is that the same techniques reappear over and over again, very simple techniques.
I once asked an international defrauder what is --
what's the earmark that you go for? What is the thing that
sets in motion a scheme to defraud? Expecting all sorts of
answers, both technological and otherwise, he said:
Recession. He said, because when there's a recession,
people's judgment diminishes and their fear level rises.

He made an interesting comment, he said that
Americans are noted as some of the hardest working people
anywhere; but the reason for that is not because they like
work. It's because they fear the future.

And it is that which they play upon.

They did a study once on successful businessmen
and women and to see what it was that drove them and
motivated them. In most of cases, the highest motivator was
fear of failure.

And we find that we're not just having elderly or
undereducated victims. We're having doctors, lawyers,
accountants, corporate presidents, as victims of these
scams, who have paid millions in order to protect their
future.

As I said, many, if not most, of the big scams are
low-tech. The nature of fraud hasn't changed. Sucker lists
ads, post cards, telephone pitches, glib telemarketers.

With these really dedicated, career individuals,

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So where does the FTC's greatest contribution lie in addressing telemarketing fraud and particularly global telemarketing fraud?

And I would suggest that it is in the forging of relationships, productive partnerships, that we need your help in maximizing our effectiveness in law enforcement. The critical need of the hour is groups focusing on fraud to form cooperative relationships.

We need you to make us more effective both in the private sector, administrators, law enforcement, internationally, we need to have some clearing house, some continual way of exchanging information.

We need the FTC to make us more efficient and maximize our effectiveness. If you were to ask me: How? I would say: Help us in several ways.

Number one, by identifying what fraud is currently the fraud du jour. It could be indium scams. It could be gem scams, sweepstakes. They tend to come in waves. And this rush pours through the criminal element, and they see some things working, and everybody leaps on board. And by the time we get around to it, with out grand jury subpoenas and our court-ordered immunity and so on, they've moved on.

We need a business organization that is responsive to what's going on and can alert us as it's happening.

Secondly, we need to know who the victims are,
what regions are being defrauded.

We worked with Bob Friedman in your gem scam case because it's a bottomless victim pool. And what he was able to help us do was to identify victims that were really going to be dynamite for us. He found people who had had mental breakdowns, having giving their life savings; people who had borrowed money from family; and so on, all of the ones where the jury is throwing the rope over the tree half way through the testimony.

That was very, very effective for us in our Canadian gem scam case. We need to know things such as: Who are the most prevalent miscreants because they tend to ride the wave, like a surfer from one scam to another. And sometimes it is productive to focus on individuals rather than on scams themselves.

We need to form an international telemarketing database. I would really love to see the FTC take the lead in cross-border information sharing in the forging of productive partnerships.

For instance, Industry Canada, I think would be a very valuable source of interplay between our country and Canada because you are more responsive in the sense that you react more quickly than we do to a lot of what's going on.

This would include operational collaboration, Postal, FBI is now becoming involved, the Royal Canadian Heritage Reporting Corporation (202) 628-4888
Mounted Police, the York Regional Police, the Ontario Regional Police, Metropolitan Toronto Police have become very heavily involved in the process.

I think the time has come and we're seeing now, for cross-designation of FTC attorneys in criminal investigations. Now, we should begin by acknowledging that there's some institutional resistance to that, which Jon Rush and the telemarketing working group are slowly overcoming; and there's a hesitation about the sharing of grand jury information, about, you know, violating any disclosure or discovery rules, et cetera.

But that's gradually being overcome, and I think we will be seeing -- there are certain cases I'm not allowed to comment on, but we're going to be seeing more and more Federal Trade Commission attorneys involved working as Special Assistant U.S. Attorneys in these prosecutions.

I could go on, but I think I'm going to save for the roundtable discussion a more particularized discussion, particularly after Ms. Larabie-LeSieur speaks on the interplay that's necessary between countries in dealing with corporate fraud.

But primarily, our point is, we really need the FTC to make us more effective and efficient in addressing, in a timely fashion, the rapidly moving area of telemarketing fraud.
COMMISSIONER STAREK: Well, thank you, Gordon. What I can say is that I agree with just about everything you've said. It's music to my ears. The problems are only going to become more acute on an international basis; and the way to respond to the increased sophistication is through joint efforts, not only internationally with our enforcement colleagues around the world, but also in our own agencies working cooperatively providing assistance that we can offer through our various statutes and the various powers that we have designated to us.

So I think I'm looking forward to the roundtable. Let's hear from our next witness, who is Richard Held. Mr. Held has headed efforts to develop risk management, fraud control, and employee safety program at Visa International. And I think he is extraordinarily well qualified for this job because he spent over 25 years with the FBI. He headed FBI operations in Puerto Rico, the Caribbean, and Northern California.

I think today we have asked him to discuss the growing problems of cross-border fraud from the perspective of the private sector and what they are doing to address this rapidly growing problem.

Mr. Held.

MR. HELD: Mr. Chairman, Commissioner Starek, my name is Richard Held. I am the Senior Vice President of Heritage Reporting Corporation

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Risk Management and Security of the Visa International Service Association. And on behalf of Visa, I appreciate the opportunity to come before you to today to talk about cross-border fraud.

Visa is a membership association of over 19,000 financial institutions worldwide licensed to use Visa marks in connection with payment services, including credit and debit cards and emerging technologies, such as stored value cards and electronic commerce.

Detecting and preventing fraud that's associated both with fraudulent cards and fraudulent merchants are of great concern to Visa and its members, given our commitment to protecting the integrity of our brand and maintaining the confidence of cardholders and merchants who use our products and services.

While fraud is a problem for Visa members, it's important to put it in perspective. For the year ended September 1995, Visa's ratio of fraud-to-sales volume is something less than one-tenth of 1 percent on an estimated sales volume of some $780 billion.

Despite the relatively low ratio, Visa is still working to further reduce fraud and to continue our worldwide leadership in this area.

Visa's found that by using a variety of fraud detection and prevention methods, we can effectively isolate
fraudulent activity and prevent systemic problems.

Of particular relevance to today's hearings, cross-border activity is responsible for a growing percentage of the fraud we experience. The worldwide Visa organization operates with six regional groups of countries, and in 1994, 13 percent of all fraud and one-third of all counterfeit was transactions between regions.

I'd like to now review with you some of our worldwide fraud prevention tools. Since fraud is a global problem, our solutions must also be global.

It's programs like those to which I'll refer that have enabled us to reduce fraud to the level we're experiencing today; and it's programs like these that will set the precedent for our response to future problems. At the outset, issuers -- those institutions that issue Visa cards -- carefully review all applications in order to detect the potential for fraud.

Similarly, acquirers, those institutions that acquire merchants to accept the Visa card, they carefully evaluate each merchant's relationship in order to keep fraudulent merchants outside the system.

At Visa, we're constantly taking advantage of new technology in our efforts to reduce fraud.

For example, to combat counterfeiting, we implemented what we call the Card Verification Value
Program, or CVV, which incorporates a secret code in each card's magnetic stripe. When a merchant swipes the card at an authorization terminal, the information on the stripe is read -- is transmitted to the issuer and read at the issuer location.

This CVV enables the issuer to detect if there has been any alteration to the magnetic stripe and, if so, to deny authorization for that particular transaction.

Another new technology is our neural network system, called the Cardholder Risk Identification System, or the acronym we use is CRIS, which allows card issuers to detect fraudulent cardholder and merchant transaction patterns and relationships by using hundreds of variables to analyze massive quantities of data.

This highly specialized software "trains" itself and develops enhanced predictive models as each new piece of data is received. Responding to ever-changing criminal patterns, our neural network system is updated continuously to quickly uncover new fraud patterns.

Card issuers can base their authorization decisions on a risk value that's assigned to each transaction processed through our global payment system, VisaNet.

This system also electronically alerts card issuers to potentially fraudulent activity up to eight times.
a day via a Compuserve mailbox, thus, providing them with an 
early warning system that prompts them to follow up with 
their cardholders by telephone to ensure the accounts are 
not being compromised.

Our Global Fraud Information System is a PC-based 
service that allows us to alert members as we see a 
fraudulent scheme developing any place in the world. It 
also gives members worldwide the ability to communicate with 
each on problems, fraud schemes that are being experienced.

Another method that we use to determine where 
fraud has clustered, in order that we may be cost effective 
and surgical in applying solutions, is our Fraud 
Concentration Analysis program wherein Visa analyzes 
extensive transaction data to determine what kind of fraud 
is occurring, is it counterfeit, is it on lost cards, is it 
on stolen cards, where it's occurring, by country, by 
merchant category, by a particular merchant, which issuers' 
cards are being compromised so we can determine why a 
particular institution is being exploited, and, finally, 
individual acquirers whose merchants are being compromised 
above the norm.

Visa then develops potential solutions with the 
issuers and acquirers and asks for feedback in order that we 
not reinvent the world for these ever-migrating fraud 
schemes that move from one place to another.
Similarly, our Risk Identification Service monitors fraud processed at merchant locations. Again, looking for clusters of fraudulent activity and patterns. When fraud is centered at certain merchant categories or merchant locations, we notify those merchants, acquirers so that Visa, the acquirers, and again the merchants can work together to determine the causes of the fraud and prevent it in the future.

Visa's Acquiring Monitoring Program identifies acquirers whose merchants introduced excessive amounts of fraud into the system. Thereafter, our risk control specialists visit the site of their operation and reviews all aspects of their operation.

If certain shortcomings are detected, we work with the institution to correct them and strengthen their process.

We also use floor limits as a risk control tool. A floor limit is a value above which the transaction must be authorized at the point of sale. The value varies by country and by merchant category. By authorizing a transaction, the card issuer tells the merchant: This card is valid and the transaction is within the cardholder's credit limit. When a transaction does not involve the authorization process, it invites increasing potential for fraud.
The United States telecommunications system is highly developed and relatively inexpensive compared to systems in other parts of the world.

This enables U.S. merchants and financial institutions to authorize most all Visa transactions, regardless of the amount, by merely swiping the card through an authorization terminal at a point of sale.

In other countries where telecommunications costs are higher, in systems less developed, Visa sets floor limits, taking into consideration the cost of the authorization as well as the fraud experienced, in order to minimize our exposure in those countries.

Through our Central Deposit Monitoring Program, Visa tracks the number of transactions a merchant deposits into the system over period of time. Where unusual increases in volume are detected, this is a sign of laundering drafts. And, again, we would go to the acquirer to seek corrections.

Laundering occurs when an authorized Visa merchant submits Visa transactions on behalf of another merchant who is not authorized to do business with Visa.

Our International Points of Compromise Program allows us to trade counterfeit cards to determine whether a particular card or a series of cards was comprised at a specific merchant location.
We also regularly review the facilities and operations of vendors worldwide that manufacture cards, holograms, or otherwise participate and impact on the integrity of our system.

Finally, we at Visa believe that awareness and education programs also play a vital role in reducing fraud. As a result of active participation by Visa members, merchants, and law enforcement agencies, the human intervention efforts, we think also have been quite successful.

The focus of these hearings is on three technologies: television, telephone, and cyberspace.

Advances in these technologies will clearly give consumers new opportunities -- as we saw this morning -- to communicate with merchants globally without being physically present to effect a transaction and use, in the process, Visa's products to make purchasers.

All of the fraud combating tools I have discussed today are in use by members worldwide and virtually all will -- or already are-- being used to combat both domestic and cross-border fraud in television, telephone, and cyberspace payment environments.

Visa fully intends to continue its leadership role in fraud detection and prevention. Our programs are continually evolving to meet new challenges in emerging

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technologies. We have no intention of varying from that precedent.

As Visa develops new products and services, our Risk Management staff is an integral part of that product development process. Our role is to evaluate the products and services as they evolve in order to pinpoint any potential exposure there might be for fraud and put that on the table as a business decision is made.

While others may see technological advantages creating new opportunities for fraud, we see new technologies as opportunities to offer new services that will substantially benefit consumers not only by adding convenience and access to information but also making transactions more secure.

For example, as we migrate from magnetic stripe cards to integrated circuits, or chip cards, transactions will be authorized in an off-line environment without using telecommunications lines. Although a main reason for chip technology is to take advantage of its increased memory, to offer new product capabilities, a significant additional benefit, will be that all transactions will be authorized, making it easier to detect lost and stolen cards, and schemes that target payment environments with high fraud floor limits. Also chips are much more difficult to copy than magnetic stripes, thus cutting into the danger of
counterfeiting.

Obviously, cards used at the point of sale are only one vehicle for emerging technologies. Home banking and electronic commerce are other technological advances that are in nascent stages today but will become the norm. We'll bank from home using a phone, a personal computer, interactive television, or a virtual bank. We also will shop in virtual malls from anywhere we have a personal computer connected to the Internet.

Visa's already working on encryption methods that will secure credit card account information on computer networks, such as the Internet, and be able to authenticate parties to a transaction.

As these and other technologies evolve, our Risk Management programs will evolve with them, offering those who participate in our systems better security systems.

Thank you for giving Visa the opportunity to address you this morning.

COMMISSIONER STAREK: Well, thank you very much for coming and offering that fascinating testimony.

Now that we know that major companies that deal internationally are using technologies for risk management to combat fraud, I wonder what the government's response is going to be. How are we going to use these new technologies to increase our enforcement efforts?
And maybe for an answer to that question or at least some enlightenment on the issue, we turn now to Scott Blake Harris, who is the Chief of the International Bureau of the Federal Communications Commission in Washington.

His international work at the FCC includes telecommunications, radio, satellite, and other developmental matters. He has an extensive background in this having worked both in the law firm of Williams and Connolly here in Washington and at the Commerce Department.

I think he's going to discuss with us today cross-border telemarketing fraud and how those new technologies will support the globalization of the marketplace and could enable the scam artist to evade law enforcement and how law enforcement can, then, use the new technologies to curtail scam operators.

Thank you for coming, Mr. Harris.

MR. BLAKE HARRIS: Commissioner, thank you.

We all talk glibly today about the communications revolution, but it isn't a communications revolution. It is a series of multiple revolutions.

The first and the most obvious is the technological revolution. Communications are becoming digital and being driven by computer technology.

The second, though, is the philosophical revolution. Just yesterday we thought communications were
best delivered by monopolies, one country, one phone
company. Today we know that's nonsense.

The third is the commercial revolution. Commerce
is increasingly global. No longer does one need to be
visionary to think about doing business internationally.
Everybody does.

Each of these changes is to be encouraged.
Together they mean new services, more consumer choice, and
lower prices. They also mean greater communication and more
economic growth.

But I suspect that all revolutions have a dark
side, and these are no exception.

More sophisticated technology, more competition,
and global thinking have all made it easier for con men to
defraud consumers -- and this is important -- to avoid
national regulatory authorities.

Today it is literally nothing to route a call from
Kansas to Sao Tome to New York in the blink of an eye and to
do so in a way that leaves the consumer thinking he has made
a call around the corner at 15 cents a minute when, in fact,
he is paying $15 a minute.

Sao Tome, for those of you who don't know -- as I
did not until this problem arose -- is a small country off
the West Coast of Africa. It's an island which has become a
hub of international dial-a-porn activity.
I don't know why Sao Tome.

Just this past spring, we discovered a dramatic increase -- and I do mean dramatic -- in the use of international information services, or audio-tech services, as they call themselves, to defraud consumers. And I use the term "information" rather loosely in these purposes. What I'm talking about is international dial-a-porn, international chat lines, international astrology lines, international job information services.

We discovered this problem only through a surge in complaints, both to the FTC and to the major long distance telephone companies in the United States, AT&T, MCI and Sprint.

These international information services have become big business. A conservative estimate -- and I emphasize this is a conservative estimate -- is that the information providers, the guys at the end of the line providing the dial-a-porn, providing the astrology, providing the chat lines, took in about $250 million last year, profit. That's not total revenue. That's not all the money in the stream. That's just the profit for the bad guys at the end of the line.

Every month there are four to six million minutes of telephone calls to information services based overseas from the United States. And that, by the way, is just in
the top five countries alone, just in the top five.

Now, where did this problem come from? Why did it spring up over night?

Actually, it is the result of a success story.

Over the last four years, the FTC and the Congress successfully cracked down on the abuses of the domestic pay-per-call industry.

So to avoid the domestic restrictions, the pay-per-call providers moved off shore where our jurisdictional reach is attenuated.

Now, what are the abuses? Why do we care?

As used to be the case for domestic services, the abuses arise from these services being accessible through a direct dial phone call. You don't need to use the Visa card off shore. And the charge appears on the local phone bill.

That means that anyone with access to a telephone, authorized or not, has easy access to the service, the kid in the house, the employee in the business who have no business making phone calls to a dial-a-porn service or a chat line have easy access. No one stops them on the other end and asks for a credit card. All they need for access is the phone.

Number 2, adults are misled about the cost of these services. So even when an authorized user has the intention of using these services, they are routinely misled.
about what they're getting and what they're paying for.

Thus, consumers, unexpectedly, get enormous phone bills. And I'm talking in the thousands of dollars here. Suddenly you open your phone bill and rather than $30 a month or $40 a month there's a $6,000 phone bill because someone has had access to a dial-a-porn service in the Caribbean.

And here's the worse part, if you don't pay the bill, you can lose your phone service.

Now, how do these international schemes work?

Every time an international call is made from the United States, the United States-based international carrier makes a payment to the telephone company on the other end of the line in the foreign country. This is called a settlement payment. They are part of the -- what they receive for completing the call at the other end of the line.

The amount of this payment varies by country. Because the rest of the world has not yet moved to competition, essentially you have monopoly carriers in almost all of these other markets, there's no push on this price to make it bear any relation to cost, right? If there's competition, prices should move to cost.

But they own all the phone lines in the other country; and they can negotiate rates significantly above cost; and, without exception, these rates are above cost
around the world, significantly above cost.

Where the foreign settlement rate is high enough, the foreign phone company can make a kickback to the information provider, who set up service, of 60 percent and still make a lot of money on the phone call, on the settlement payment.

So this is the way it works: local phone company in Sao Tome goes into business, in essence, with the information provider; he says, you come here, set up shop, you advertise in the U.S., you create a tremendous influx of calls from the U.S. to Sao Tome.

You get a dramatic increase in revenues for the Sao Tome telephone company and kicks off a percentage to the information provider who is now based in Sao Tome.

That phone call then gets billed back from Sao Tome to the U.S. international carrier on to your local phone bill; and if you don't pay, you lose your phone service.

The final piece of the puzzle is that if you look at the advertisements which appear in even major newspapers, they are always misleading. Free phone calls. Long-distance rates apply. They break up even the international phone numbers in a way that is impossible for me to tell where you're calling, and I understand the numbering system. And if it's in a Latin American country,
part of the North American numbering scheme, their numbers
look like ours. 809 is a foreign number area code. Not
many people know that.

And so people literally think they are calling
around the corner, and their phone call goes to Sao Tome,
off the West Coast of the Africa.

By the way, the girls who do the dial-a-porn are
often back in New York and the phone call just visits Sao
Tome for the blink of an eye to make the whole scheme work.
And, in fact, it's all going on in New York City or Seattle
or some place like that.

Let me just give you this brief idea how these
schemes can boost phone traffic. In 1992, there were 40,000
minutes of telephone traffic from the United States to Sao
Tome. In 1994, two years later, 13,202,000. 40,000 to over
13 million.

Moldova, in 1993 had 81,000 minutes of phone
traffic from the United States. In 1994, it went to 6
million minutes of traffic from the United States.

Since the spring we have been trying to grapple
with this problem at the FCC. And let me be candid with
you, I had hoped I'd find a single bullet, one thing we
could do which would make it go away. I'm coming to the
conclusion that there's no one thing to do. There's no
silver bullet that solves a problem that crosses

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jurisdictional lines with technology the way this one does. 

We think we have a multi-faceted problem which is going to require a multi-faceted solution. Among other things, it requires far greater cooperation among regulatory and law enforcement authorities in the United States than we have today. It requires additional concentration of time, money, and effort from regulatory and law enforcement authorities. It also requires more cooperation among regulatory authorities internationally.

This is not a problem, I think, ultimately that we can solve in this country alone. We need to work with our colleagues overseas.

Let me tell you what we've done so far and what more needs to be done, in my view.

First, we've already developed, through our own investigation, information that suggests that folks who engage in these endeavors routinely violate all manner of criminal laws.

These or not people who are real concerned about what the law says. This is an area ripe for Justice Department prosecution. And I think, frankly, all the good that regulatory agencies can do, putting a couple of these bastards in jail is really the way to get at the problem in a way sets the record straight and lets folks know where we're going. We've given a bunch of information to the
Justice Department, and we're hoping they're going to do that.

The second is that the essence of all of these schemes is misleading consumers in the United States, something that is squarely within the jurisdiction of U.S. regulatory authorities; and, to be more precise, is squarely within the regulatory jurisdiction of the Federal Trade Commission. Without the vital connection to the consumer in the United States, none of the schemes work. All the technology, all the rest of it, unless you have that hook into the consumer, that misleading hook, it all falls apart. That's where the FTC can bring its enforcement authority to bear. It can sever that crucial relationship with the consumer.

Third, we have already worked with industry to craft a voluntary agreement among all of the major telephone carriers in the United States to protect consumers. We've met with all of the major long-distance carriers. We've met with all of the major local telephone carriers. And we now have a nationwide understanding designed to protect consumers. None of the major carriers now will collect payment from consumers whose phones have been used for these services without authorization or who have been deceived.

The local telephone companies have also agreed not to terminate telephone service for non-payment of

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legitimately disputed charges.

The U.S. telephone industry basically came together and said: We refuse to be used by these people to defraud our customers.

Fourth, we've already begun to work, both with foreign telephone companies and regulators, to cut off the fraud at the other end of the line. And we've actually made some progress already. We have a couple of carriers overseas who have signed up, essentially, to the kinds of protections we have by regulation in the United States.

And we have embarrassed a couple of regulators overseas. And some, frankly, we didn't have to embarrass; they share our view of the world and are already beginning to crack down on these practices. But as with any international endeavor, that takes time.

So there's still much to do. There's much more we need to do together. I think we're making progress on the problem, but we are not there yet.

Thank you.

COMMISSIONER STAREK: Thank you, Mr. Harris.

Mr. Chairman.

CHAIRMAN PITOFSKY: Just a clarifying question.

We were doing well against suppressing fraud when the call was Minneapolis to New York. What difference does it make that the call goes by way of Moldova?
MR. HARRIS: Basically, what we were able to require -- because of our jurisdictional authority -- is that if you make the call in the United States, you can require the fellow at the other end of the line to demand a Visa card, some form of the payment which protects the person whose phone is being used because someone needs an independent way of calling. We required information providers at the other end of the line to provide information before people could be charged over the telephone system.

When the folks in Moldova -- you can't make them require a Visa card.

CHAIRMAN PITOFSKY: But can't you make the -- when it lands in New York, on the second leg, can't you require that --

MR. HARRIS: Basically, because of international agreements, no, you can't.

CHAIRMAN PITOFSKY: Ah, that's the problem.

MR. HARRIS: No. The answer is there is an international treaty regulating how international phone calls are made and how they work.

CHAIRMAN PITOFSKY: Okay. We have a technical assistance grant from AID to aid the good folks in Moldova. They may be way ahead of us.

COMMISSIONER STAREK: Well, our final presenter

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this morning is an old friend Rachel Larabie-LeSieur.

Rachel is the Director of Marketing Practices with Industry Canada, a good friend of this agency, known to many of us.

She and I participated in the establishment of an international group of law enforcement agencies. It's known as the International Marketing Supervision Network. It's an informal network of law enforcers in various OECD countries who get together and exchange information on the problems we have in enforcement in our own countries as well as cross-border enforcement.

Rachel, thank you for coming. Thank you for making the trip. We look forward to hearing your experience with cross-border fraud, and maybe you can share with us some of the Canadian-U.S. experience and some of our international cooperation that we've been trying to accomplish.

MS. LARABIE-LeSIEUR: Well, let me thank you for inviting us. And coming to Washington is a true enjoyment since we left 30 centimeters of snow back in Ottawa; so I mean, it's like a trip down south. It really feels good. I'm telling you.

So thanks for inviting us. These hearings, I think, are very important; and they are very timely, in light of the changes that are occurring both within the

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marketplace and within government.

Within government, I think I would like to start by saying that fiscal constraints in Canada has forced us to review the structure of the Marketing Practices Branch, which is part of the Bureau of Competition Policy.

And we have, just recently, closed all of our regional offices. We had seven regional offices, very small offices; and it was felt that it was better to consolidate all activities in the headquarters in the national capital region.

We've created a complaint's unit with a toll-free line, which I think is going to compensate, to a certain extent, for the closure of the regional offices.

Over the past 10 years, I would say, we have witnessed an increase in cross-border practices that contravene our legislation and American legislation.

And in our estimate, this is due to closer trade relations and more sophisticated and cost-effective communication and computer technology.

We are now operating in an environment that is characterized by an increasingly unified, global market for business and fragmented law enforcement jurisdictions, coupled with restrictions on cooperation and information sharing among agencies, all operating with substantially reduced budgets.
I think that sums up the situation from our perspective.

So there is an obvious need, in our view, to fill the gap, through cross-border enforcement and education initiatives if law enforcement agencies intend to continue playing an efficient and a relevant role in the marketplace.

On top of this, there is an obvious shift towards an increased criminalization of deceptive marketing practices.

The number of cases which now include elements of fraud is on the upsurge. And one of the most egregious example is the typical telemarketing scam.

In Canada, the majority involving U.S.-based practices relate to deceptive mail solicitation which target consumers offering prizes or premium promotions, travel certificates, or businesses through look-alike invoices.

And there is also evidence that some elicit American-based, multi-level and pyramid sales companies that contravene Canadian legislation are also being promoted in Canada.

On the other hand, it's also well known that some Canadian telemarketers and direct mail operators target U.S. consumers to offer dubious investments, gem stones, strategic metals, lottery tickets, deceptive prize promotions and solicitations that look like invoices are
also sent to U.S. businesses by Canadian operators.

So that, I think, sets the scene. And I would like now to give you an overview -- or a Canadian perspective, if you want, on the enforcement of the criminal provisions that are contained in the competition act that deal with misleading advertising and deceptive marketing practices.

These provisions deal with misleading advertising, unsubstantiated performance claims, misleading testimonials, double ticketing, bait and switch, pyramid sales, whatever. And all of these are strict liability offenses, meaning that we do not have to prove the criminal intent. And this is being referred to as being a criminal regulatory regime, which distinguishes it from the criminal code offenses.

Some of these provisions contain specific defenses that can be used. And one of the provisions provides for a due diligence defense when we are talking about misleading representations.

The act also contains formal powers, so we can obtain search warrants from the courts, we can obtain orders to examine witnesses, to compel production of documents, or to require written returns of information. And failure to comply with such orders is usually punishable by either a fine and/or a jail term.

What is happening, though, is that search warrants

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have been very useful in investigating typical marketing practices offenses. But this, too, has limitations when the target of the investigation is more fraudulent or mobile.

So I mean, to a large extent, that becomes meaningless. So we think that we have to turn to quicker and more flexible means to gather evidence in such cases, like search of banking records, surveillance, use of informants, as well as increased cooperation and information sharing with police forces and other law enforcement agencies.

And I know that sounds repetitious, but I think it's going to be the message of the day.

The director, which has the responsibility for the enforcement of the competition act, is only an investigator. We have no adjudicative role to play. So once an investigation is completed, a summary of evidence is referred to the attorney general of Canada which then has discretion as to what action is appropriate or should be taken.

So when we refer a summary of evidence, we usually make a recommendation towards laying of charges as well as a prohibition order.

Penalties. Most of the misleading advertising and deceptive marketing offenses can result in fines at the discretion of the court, and jail terms can reach five
However, we've seen very few jail terms. In fact, I know of one that goes back to the 1970's, and it was a one-year jail term.

What we've seen in the past few years, however, are community service terms that are imposed by the courts. And in addition to those type of penalties, there are also what we call prohibition orders, which goes to the continuation or repetition of the offense or to the doing of any act that would be directed towards the continuation or the repetition of such offense.

And those prohibition orders -- and this is a tool that we use a lot. Those prohibition orders can be obtained on contempt. So it makes the process more rapid and streamlined.

And, again, failure to obey such order is punishable by a fine or a jail term.

Our experience with the criminal courts -- and this is something you may find interesting -- is that we find, because of the sparsity of court time, that the process is very, very lengthy.

Moreover, criminal courts often lack the expertise to deal with the reality of some misleading advertising subtleties, such as the fine print disclaimers. And our experience is that often courts look at those as being
contracts. So we've not been very successful in those areas.

There is a need for increase deterrence. And to achieve this end, we give priority to high impact cases; and we attempt to provide the courts with evidence of the economic impact of the impugned practice on the market.

The average fine level has increased significantly over the past years with some significant peaks and always, from a Canadian perspective, reach half a million dollars.

It is our experience in some cases that charging the corporation can be virtually useless since they can be without assets, they can easily become bankrupt or cease operations temporarily only to resurface later under a different identity.

In such cases, charging key individuals appears to be more effective; but this approach, of course, requires more time at the investigation stage since we have to gather more evidence to link the individual with the practice that is going on.

Substantial fines, on the other hand, can become meaningless should the accused demonstrate incapacity to pay.

So we think that taking action to seize proceeds of crime should be considered as a possible avenue to achieve the deterrence enforcement against those criminal
marketing practices.

Presently, the competition act offenses do not qualify for proceeds of crime, that are contained in the criminal code. But we are working on that, and we hope that this can be changed.

In the context of cross-border practices, consideration will have to be given to the transfer of assets to foreign jurisdictions as a means to avoid seizure.

The opportunity of improving existing international agreements in this area to better deal with cross-border marketing practices, I think, should be closely examined.

I would like to say a few words about the reform. We have a reform of legislation going on. The minister and the director published a discussion paper back in June of this year which proposes the addition of a non-criminal option to pursue misleading advertising and specific deceptive marketing practices, criminal prosecution as the sole legal instrument of enforcement has a number of shortcomings, such as lack of speedy decision making, specialization and consistency in decision.

Criminal offense sometimes can be too severe a response for some instances of unintentional misleading advertising and invoking the criminal process can be unjustifiably expensive of time and resources for both
businesses involved and the bureau.

Under the proposed hybrid regime, criminal prosecutions would only be used in the most egregious transgression while the availability of a non-criminal alternative would provide more flexible remedies.

Cease and desist orders, both interim and final, complimented by remedial orders, such as orders directing the payment toward consumer education or publication of information notices, would be available to the director.

And we are now at the stage where we are reviewing the submissions that were made during the consultation period.

Just a few words on the use of international agreements. And that's one of the advantages of criminal enforcement, is that there is a growing framework of international agreements which foster cooperation between jurisdictions. And, although we have never taken any direct enforcement action against a U.S.-based operation, unless it had a business presence in Canada, some interested avenues have been explored to deal with exploratory territoriality issues.

I can think of two examples that I would like to share with you.

Last year we initiated proceedings pursuant to the Canada-U.S. expedition treaty in order to compel a U.S.
citizen, accused of misleading advertising in Canada, to appear before a Canadian court. Because the accused subsequently agreed to appear voluntarily, it was unnecessary to obtain the expedition order. And this initiative was undertaken in conjunction with the USDOJ and the FBI.

In another matter, which is still ongoing, we have initiated an Em-Let request to recover the fine imposed on the Canadian subsidiary of an American business that was convicted of misleading advertising in Canada.

Evidence demonstrated that the Canadian entity, in fact, was a corporate shell with no assets. And shortly after the end of the practice -- of the offending practice, the Canadian subsequently became dormant.

So if this fine is recovered through Em-Let, this is going to be a precedent. So we're crossing our fingers, and we hope that everything works out fine.

I guess one word on confidentiality. And I think that we could say that the current, the existing confidentiality provisions contained in our respective statutes as well as restrictive related policies and interpretations limit our ability to exchange confidential information regarding cross-border issues.

And, accordingly, the director has proposed in this amendment package that is now being reviewed -- he has
proposed amendments to the act that would expand the statutory protection and that would make explicit the extent of his authority to communicate confidential information in his possession with the appropriate safeguards.

I mean, of course, there is this balance to be achieved. In other words, safeguards have to be found. And I think I would like to conclude by stressing the following points:

We believe that misleading advertising and deceptive marketing practices can be addressed more effectively in a hybrid, criminal, non-criminal enforcement regime. And we hope we are going to be successful in putting these amendments through parliament.

Cross-border, misleading advertising, and deceptive marketing practices are here to stay. They will not go away. The number of such transactions is likely to increase steadily in the future. And law enforcement in this area has to become international in order to remain effective.

It is very important to further develop cooperation approaches between Canadian and American agencies to combat such practices both through enforcement actions and sustained education initiatives.

It's important that the gathering of information in a foreign jurisdiction to deal with cross-border
practices starts with the establishment of a network among law enforcement agencies to facilitate assistance in obtaining public information. I mean as it is now, we do not even have access, or we cannot even share public information because we don't know one another. We don't know what we're all about.

Although a lot can be done by sharing public information, necessary adjustments to our legislation may be essential to develop the facts of cooperation modes.

And the new BCP-FTC-DOJ agreement that was signed in August I think provides an appropriate foundation to build a cooperative relationship between our respective agencies. And we think that we should examine the necessity and the usefulness of establishing mutual legal assistance provisions to assist each other in the enforcement of non-criminal, marketing practices.

And, finally, I think that in order to meet these great challenges -- and God knows they were huge -- if we want to meet them collectively, I think we have to remember that mutual trust and sharing of a common vision are key elements to our success.

Thank you.

COMMISSIONER STAREK: Well thank you, Rachel, for some very outstanding suggestions. You have laid out the problems that we face, I think, in our countries, both in

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Canada and the United States, and made some very interesting
and helpful suggestions as to how we can address those
problems and maybe make some progress on enforcement.

It seems to me that we all agree here that the
first step in effective enforcement against telemarketing
and other kinds of scams is for law enforcement agencies
within our countries to work together.

And I can say that in the United States and from,
Rachel, what you said about Canada, that's happening; and
that's been happening now for the last several years. We are
working together, using the tools that we have in our
respective agencies in the United States and also in Canada
to combine efforts to take on these scam operators.

The next step, however, is what Rachel suggests,
which is that these agencies within our countries begin to
work cooperatively and closely with other law enforcement
agencies in other countries.

You point out clearly that the obstacle to that is
our confidentiality statutes in our respective countries.
And we run into this in our International Marketing
Supervision Network where we make inquires of each other and
we have to spend a considerable amount of time trying to
determine whether or not the laws of — in our case — the
United States, will allow us to provide that information to
a foreign law enforcement agency.
So how it is, then, that we can overcome these problems and begin to work more closely together with our counterparts in other countries?

And, then, secondly, how is it that we can incorporate the kinds of technological response that Mr. Held outlined about how Visa is addressing fraud and how they're responding to this technologically?

How can the law enforcement agencies respond to this increased use of technology with a response that makes our enforcement by fraudulent operation much more effective.

Any takers to those two, sort of, general questions?

MR. HELD: I would, I suppose, bring both perspectives coming from a career in law enforcement and looking at the changes that are taking place today.

I mean, I think we all agree: The world is becoming an increasingly small place, and technology is changing how everything is being done.

Speaking only for myself, I would say I think that agencies are going to have to work to stay relevant to these problems. The need for cross-border communication is absolutely imperative between governments. But it's something that is going to require an awful lot of work.

In organizations like Visa, of necessity, we must seek our own solutions because we cannot wait.
When I was in law enforcement, if someone from a payment scheme came to us for help, in truth, I would have to say -- as Mr. Zubrod said -- this is going to take a while. In a complicated case, there's going to be a question of willingness to take it; and with all of the things already on the government's plate, that's difficult. It must be prioritized. There's going to be a question of capability. Do they understand what has happened? And does the law, as conceived a long time ago to deal with a problem that was more readily -- you could readily get your arms around -- does the law apply?

If I go to Sao Tome and I need local currency, I take my card, I don't travel with currency any more because there's a new global currency today. I put my card into the machine and in a fashion that I can barely yet understand, in a matter of four seconds, a signal is transmitted through a computer, off a satellite, relayed around, comes to my bank in the Midwest, and goes back and says: He has an account, and this cash withdrawal is authorized, in five seconds. I don't think the law in the United States ever conceived of having to deal with a problem like that.

There is a question of adequacy of law.

By the time that we have a fraud taking place in that environment, it will be, in fact, years before there will be a solution. And we can't wait for that.
integrity of our payment system, a global payment system, which is important to the financial community in this country and every other -- it's as important as checks and cash are -- our industry, our payment system can't wait, and we must go forward.

The answer to the question is: All of these things that you talk about must be done. But things are going so fast and the question of challenge for government is: Will you be able to go fast enough?

We need your partnership, but will you be able to go fast enough to overcome the reality that there is no precedent for solving these problems.

MR. HARRIS: I would like to add just a mild dissent to all of the above.

I think it's a mistake to expect that there's going to be an easy technology solution to all of these problems, in part because technology costs money.

One could, in theory, require all the phone companies in the United States to reprogram or buy new software or new hardware for all their computer switches and, therefore, provide an easier blocking solution for these kinds of international calls.

The costs imposed upon the companies and, thus, on the consumers would have so many damn zeros, it would scare you all and say, better that we just pay the dial-a-porn
people ourselves.

So you can't, necessarily, on those solutions.

Technology costs money.

Number 2, it's not clear to me that we don't have
the basic legal regime that we need.

I mean there may be nicks that need to be fixed,
tweaks to the law. But in truth cross-border fraud is
nothing new.

What we need, in my view, is more enforcement in
the United States. What seems to be difficult is how we get
from here to there.

I would love to have 10 people, since we have
discovered this problem, that I could just put on this
problem; and you could shake this whole problem up a lot
with 10 people in the course of 6, 8, or 12 months.

The likelihood of me having 10 people for any
purpose in today's environment is real small. And one of
the reasons we're desperate for help from Justice or from
the FTC or wherever else we can get it, from state
regulatory authorities, is that, Jesus, we don't have the
people, we don't have the funding, we don't have the budget
to do what we would like to do for enforcement purposes; and
the likelihood of our getting it, it seems to me, is 0. If
we're lucky, they don't cut our budget. Right? If we're a
little unlucky, they cut it 10 percent. And right now,
we're operating at 75 percent.

So, you know, you get what you pay for. And I think the real issue is enforcing the damn laws, because we have some pretty good laws in place, we have some pretty good regulations in place. Enforcement does work. We've seen it on the domestic side. The international side is a little harder. But, you know, we're firing people.

So I think it's not going to be technology. I think it's going to be enforcing the law. And I think we have to figure out how to do that, though the way does not seem entirely clear to me at the moment. We're doing what we can with the limited resource, and we'd love to do more.

CHAIRMAN PITOFSKY: Scott, if some one magically gave you the 10 people, what would you tell them their first priority is?

MR. HARRIS: Well, at the Commission, we have all sorts of consumer difficulties, as you're well aware. I mean the kinds of thing that you can see on TV at night or read in the paper.

I think this is a problem that's coming to the fore, this international audiotext problem. And these people, I believe, are violating existing regulations; they're violating existing laws. And we are, with our limited resource, attempting to find these people right now and impose regulatory fines, turn it over to the Justice
But, you know, you find people who have a little bit of time available and you throw them into the problem; and then they get, you know, pulled away to work on something else and then they get furloughed.

CHAIRMAN PITOFSKY: We've noticed.

MR. BLAKE HARRIS: Yeah.

CHAIRMAN PITOFSKY: But with this Moldova business, you think with 10 people the treaties would not be a block and that you could get at it?

MR. HARRIS: The treatise make enforcement more difficult. The fact that there is attenuated jurisdiction overseas. And you have to be careful with a purely regulatory approach.

I'll give you another example. Suppose we simply required all of the phone companies in the United States not to process these charges through to customers. Required it.

The U.S. phone companies would still have to make the payments by international law overseas. And so what you would simply do is place this enormous burden on the phone companies -- and some of these calls people fully intend to make.

So that regulatory -- it makes regulation much harder because you have one piece of the system that's unregulated.
Having said that, the people who engage in defrauding consumers are violating, nine times out of ten, existing laws, existing regulations. You just got to catch them, and you got to impose fines, penalties, whatever it takes. And I think the -- you'll never make it go away. Criminal penalties, regulatory penalties never end a problem; but they can affect the problem, as we've seen.

We could use more enforcement ability, and we need help from other agencies.

MR. ZUBROD: I would say that there are really four issues that need to be considered. The first one is what my brother here referred to as education. It's important to get law enforcement to perceive that there is a problem. Because the tendency is to say that: We're being overwhelmed by X, you know, fell in the blank, drugs, technology, smuggling, et cetera, and they will tend to respond to it.

But when there's a top-down emphasis that this is important, once prosecutors and investigators are educated, then judges are slowly educated and start getting sentences. And we are now seeing people getting sentences of three to seven to eight years -- my last one was ten years -- for fraud prosecutions; and that's beginning to have an impact.

I note in dealing with Canada, we discussed this morning, how one of the real disappointments is prosecutors
are becoming sensitized. Investigators, particularly in Toronto, are now very sensitized to the issue.

And prosecutors are beginning to become sensitized. The courts are not sensitive to it at all; and if you are a white collar criminal doing global telemarketing fraud, you are going to get a probationary sentence, regardless.

We have a gem scam case, a $35 million fraud, where my counterparts told me that, this is a probation case. And so we have taken them down, and we can get about a seven-year sentence on a guilty plea and probably 10 if they try to go to trial.

The next area is in the -- my experience working with the Swiss in implementing our mutual legal assistance treaty was that the seizure of assets is a powerful incentive for cooperation. That's something that people respond to.

But to do that, you have to move out beyond the common law of the particular nation and to explain money laundering or expanding the definition of a straw party or the idea of forfeiture of the proceeds of a crime after it changes its character and moves into maybe a straw party's asset or moves into the name of, for instance, under Canada law, my understanding is, that if you put something in the name of your wife, it is absolutely immune as an asset of
the individual.

Yet, under modern American theory, you could
pierce the corporate veil, you could pierce that
relationship, look behind it and seize the assets if it's
pure proceeds; and proceeds is never protected no matter how
many times it changes hands if there is some knowledge on
the part of the individual.

There needs to be some procedural statutes, too,
some procedural changes because the areas of confidentiality
and discovery -- we got the Canadian Royal Mounted Police to
do a search warrant for us. They are as tough on showing us
the results of the search as we are on grand jury material.
And so it was a very delicate process involving Washington,
D.C. -- our going through Washington, D.C., their going
through Ottawa; and it was months before we could look at
documents that we put together the probable cause for.

And finally our experience has been that, in terms
of speed of action, the most effective so far has not been
top down. It has been bottom up. One investigator getting
involved with another investigator, getting involved with a
specific individual at FTC putting their heads together and
saying: How are we going to attack this problem? What's
the best way? And from out of that comes victims, search
warrants, arrests in other countries, arrests in this
country, and a tandem approach that has been very, very
And I can't emphasize the need for one-on-one -- the formation of one-on-one, personal contacts, which are the most effective.

MS. LARABIE-LeSIEUR: Can I add that I believe that there will be need to change the organizational culture, if you want, in a way.

We have a tendency within our agency to prioritize cases using location of victims, for instance, as a factor that would influence its ranking.

And you were right, Scott, when you were saying that cross-border practices have been there for a long time; but we have just ignored them for a long period of time because they were not making the priority list. There were no victims in Canada; there was no victim in one province.

I mean, this is the type of cultural change that has to take place within our own organization if we want to enforce together.

COMMISSIONER STAREK: Many of the countries that are in the process of trying to combat global fraud scams also have a very effective competition enforcement agency.

And in the United States last year, we had enacted into law, which was signed by the President, a statute which permits our competition authorities to exchange confidential information as long as the country with whom we are planning
to exchange the information has in place the safeguards that
we have in place to protect this confidential information we
obtain from companies who are engaging in a merger or
some other transaction that would come under the review of
this Agency or the Department of Justice.

The Justice Department and the Federal Trade
Commission have been talking to competition authorities in
Europe and Canada and Australia, et cetera, about changing
their laws, similarly, to put in place the kind of
confidentiality requirements that are necessary to assure
our companies, as well as their companies, that the
information that's shared with the foreign enforcement
authorities is going to remain, just as they expect from
their own country's agency, confidential.

Is this an avenue that we might want to look at?
Is this kind of action that consumer protection authorities
might want to look at?

MS. LARABIE-LeSIEUR: Well, the director, as I
indicated previously, has launched consultation on
amendments to legislation that would deal with
confidentiality issues and ensuring confidentiality of
information based on reciprocity and with appropriate
safeguard.

And these amendments would -- because they are
amendments to the Competition Act, they would find
application in regard to misleading advertising and
marketing practices.

And I think that what it amounts to is some kind
of mutual legal assistance treaty that is within the
mandates of the law enforcement agency.

So we are all in favor of that.

COMMISSIONER STAREK: Well, it sounds like you're
ahead of us. Because while we've done this for information
obtained in competition cases, including grand jury
information under certain circumstances, we have not looked
at it in this country for the kind of information that we,
consumer protection enforcement agencies, would need to
share.

But it sounds like Canada thinks it's a good idea.
That's great.

MS. LARABIE-LeSIEUR: I think we're ahead of you,
perhaps, on the consumer protection side, as you referred to
it; but I think we are lagging on the antitrust side.

COMMISSIONER STAREK: I think there have been
discussions.

One of the suggestions that Gordon made was that
we establish an international telemarketing database. Now,
this might run into the same kinds of problems we were just
talking about.

We have a rather extensive telemarketing fraud
database here in the United States administered by this Agency. And there are a number of law enforcement agencies, both state and local, as well as federal, who use this and develop cases based on the information contained in this telemarketing database.

Are the constraints on sharing confidential information too great to try to think of the appropriate way to fund an international telemarketing data base?

MR. ZUBROD: I don't think so. I think there's sort of an institutional reluctance. But when you sit down and talk to people, they say really we could be creative and we could form such a database.

I noticed that one of the things that the Swiss did, was the Swiss said: Our law forbids us from sharing information; however, our law does not forbid us from opening a case of our own if we were alerted to it; and our law does not forbid us from letting you open a case of your own.

So in one sense, the Swiss concluded that it was a way in which the question was asked. If you would say: We want information on such and such, it would be far better if the United States would ask the Swiss, saying: Is there such a person as John Smith? And does this individual own a corporation? We have information which indicates he may be involved in criminal activity. And the Swiss would say:
Well, we're going to open our own investigation on John Smith and this organization.

And information was passed back and forth, I won't say promiscuously, but to a far greater degree than the three to six months it takes to get an Em-Let going back and forth, that the information that's passed between investigators moves -- there's sort of an agreement, it ought to move a little more quickly. When you get to certain documents seized and viewing documents, it slows down.

But that type of information, I think it's doable.

COMMISSIONER STAREK: Well, that's sort of the opposite of the way our confidentiality laws work. I mean, once we have an investigation open, is when we are prohibited from sharing that kind of information.

But, you know, whether or not John Smith exists and whether or not John Smith is a principal in a company is relatively public information and information that we can oftentimes share.

MR. ZUBROD: It flags the individual.

COMMISSIONER STAREK: But once we get into an investigation that's been formally opened, that's when the door comes down and the barriers to sharing that information, even with foreign law enforcement authorities, go into place.
MR. ZUBROD: That's true.

MS. LARABIE-LeSIEUR: We think that central sourcing of complaints is an interesting avenue and needs to be explored. I think it's one way of getting speed in that the central sourcing approach does give you an immediate snapshot of what's going on instead of having complaints going from jurisdiction to the other until it gets to the right one. I mean, this is one clear benefit.

We have done that, to a certain extent, in Canada through project "Foam Buster," which is a partnership with police forces, provincial governments, Bureau of Competition policy, Canadian Bankers Association, and other partners, where we're doing central sourcing of complaints with the OPP, the Ontario Provincial Police. And this allows the individuals involved there to know, I mean, on a weekly basis what type of new scams are being created, what is going on, the number of complaints.

And this information is shared with the partners. And so far, it has proven to be very useful.

COMMISSIONER STAREK: Any other questions--

Eileen?

MS. HARRINGTON: I have a question, I guess, initially, for Mr. Held.

It seems to me that one of the real beauties of the bank card payment system is that you've been able to
protect its integrity by controlling access. Only licensees have access to that system.

And we just saw a presentation this morning of a technology -- and I think the Chairman asked a question about access there. And the answer is: Everyone will have access to this new product of converged technologies.

It seems as though there's a real rub there between -- if that's the case -- between our ability to replicate the kind of integrity that you have created for fraud prevention and other purposes in the credit card/bank card payment system internationally and our ability to protection against fraud on this new emerging global information infrastructure.

What are you guys -- you must be thinking about that at risk management and security. And what do you think?

MR. HELD: Well, one, it was not clear to me how payment would be effected in that environment. I presume it would be just part of the billing process. But I'm not sure.

I mean, we clearly are looking at: How do you secure transactions in open networks? And from a risk management perspective, absolutely. I mean, now there are some business conducted on the Internet. It's not really clear how much. For the most people who shop on the
Internet are prompted to -- having effected a transaction, to now go to the phone and give us card information to enable payment by card.

But in the future, as this expands, as certainly it's going to, what we're look at is now: How are we going secure that transaction? How are we going to confirm for the cardholder, protect the consumer, to say this is a legitimate merchant who is entitled to do business, and we will certify their legitimacy in the process.

And, similarly, for the merchant, that is a legitimate card, and there is not a problem with the card; and you can be assured that we will make payment on this if you conduct this transaction.

So we will credential the two parts; but then, also we need to the secure the transaction so that it is not -- it can't be intercepted, it can't be changed. It is just between the sender and the receiver.

And we are now evaluating, with Technical Laboratories, to see that what we see as the solution, in fact, will minimize any risk of compromise.

MS. HARRINGTON: If I could just follow up, one of the things that the bank card industry learned painfully during the, you know, incredible explosion of fraudulent telemarketing was that fraudulent merchants, pretty easily, were able to, initially at least, be accredited in your
system.

Now you have a lot of checks and controls, on-site inspections, all the things that you described.

How are you going to credential merchants that might exist only in cyberspace? And how are you going to protect consumers in the United States who may get onto whatever the information highway is, do business with a merchant that's based in some other country --

MR. HELD: Dubai.

MS. HARRINGTON: -- where that merchant really only exists in cyberspace?

MR. HELD: Well, I mean, for us the beauty of our system is, we have contractual arrangements with acquiring institutions with institutions who go out and find merchants to accept the card. And they have contractual arrangements with merchants.

So what we would do is a continuation of the process that we have now, that we --

MS. HARRINGTON: Have you thought about what those criteria might be, though? How do you do it?

MR. HELD: Well, the criteria -- I can't say -- the answer is, yes, I can't see how they would be much different than what they are. And that would be -- there's a set of expectations that we have for an acquiring member. And that is: They go see that there is, in fact, a
business, that it meets some material criteria to confirm
its existence, that it does have bank accounts, that it does
have a place of business, that it does have a product.

This will be different because, at the outset, the
information is apt to be research, pictures, movies, and
what have you.

But the process, in our minds, will be the same.
But clearly, it's complicated in the eyes of the law because
what will an agency like the FTC do with a merchant some
place else?

I mean, I think that that need for both
cooporation with the private sector, there needs to be
interaction, but also intergovernmental relations are going
to be increasingly critical; and it's going to be a huge
step because borders in commerce are virtually disappearing.

COMMISSIONER STAREK: Well, thank you. I found
this fascinating. We certainly agree that enforcement
agencies, in our own countries anyway, are doing better at
working together to enforce the laws, which we must because
of our diminishing resources and because of the different
tools that each agency has to address a part of the problem.

The question is how we are going to improve upon
working together internationally. Everybody seems to think
we need to, but how can we get rid of some of the barriers
to cooperation, seems to be the question that we need to
give more thought to and try to come up with some creative solutions.

I want to thank all of the panelists for appearing today. I found it very interesting. And I invite all of you to return this afternoon for the grand finale of the consumer protection phase of these hearings, which is convening I think at 2 o'clock here.

We'll see you then. Thank you.

(Whereupon, a brief recess was taken.)

COMMISSIONER STAREK: All right. I guess we are all assembled for the final session this afternoon of our hearings focusing on consumer protection in global markets.

We have looked at various instruments of communication: the telephone, television, computer. We had a very interesting presentation this morning basically describing how all of these technologies are, certainly very soon, if not already, going to converge. And the benefits of all three of the technologies will be obtainable all together and utilized together.

Also, we have looked at fraud in the marketplace and had a very interesting discussion earlier this morning about how both industry and governments are going to respond to fraud as it becomes more technologically advanced. We agreed that the scams, really, will probably be the same; but they will be harder to detect because of the
technologies that will be utilized.

And this afternoon, we are going to continue that.

This afternoon we are going to begin with an overview of developments in international trade and how that affects consumer protection.

Our first witness this afternoon is Richard G. Meier, who is the Deputy Associate Trade Representative from the U.S. Trade Representative's office.

Mr. Meier is responsible for policy development in international negotiations regarding a wide variety of trade issues and standards.

During the Uruguay Round of the multi-lateral trade negotiations, he was the Chief U.S. delegate to the negotiating group dealing with non-tariff agreements, including the agreement on technical barriers to trade. We look forward to hearing your remarks.

MR. MEIER: Thank you very much and good afternoon.

I am challenged here this afternoon to present quite a bit of information in a rather short period of time. So forgive me in advance if I am somewhat summary in my approach; and I certainly would be pleased to answer questions later in the afternoon session.

I don't pretend to be a consumer expert; although, I become increasingly sensitized to the issues relating to
consumer protection and the relationship to the things that I do. Some of the people responsible for that sensitization process are around the table. So I thank them for their help over the recent years.

Let me just take a moment to be somewhat parochial and just talk about international trade and its importance to our economy in a very broad way; and then I'll go through some specifics on technical barriers to trade and what the U.S. Trade Representative's office is doing and how we relate. I hope I will try to be able to say how we relate to some of the issues that you're dealing with here.

Some of these facts and figures may be of interest to you; but I think they're always somewhat startling when you review them -- or when I review them. So let me just run through them and I think it explains why we take such a keen interest in trade and trade policy.

Back in 1970, international trade, both exports and imports, accounted for 13 percent of our gross domestic product. This doubled by 1993 to 26 percent. And it's now about 30 percent. Obviously, a very important share of economic performance is accounted for by trade activities, again both exports and imports.

In 1994, we had exports valued at $657 billion. That's both goods and services. We also had imports valued at $760 billion. So it was a little bit more of those than...
there were of the exports.

On the services side -- and my figures are a little bit older there -- back in 1992, we had $168 billion of service exports and a $60 billion surplus. The services account does quite well.

This year our trade performance has shown some signs of dramatic improvement. In August 1995, we had had export growth, for the year to date, moving ahead for the first time of our rate of import growth, 15.7 percent for exports, 15.4 percent for imports. And we expect that trend to continue.

I believe the new -- I could be proven wrong tomorrow, because I think the new trade figures -- right, the new trade figures should be out tomorrow. There might be some delay due to the problems in recent days with government funding.

Estimates are that U.S. jobs supported by export activities accounted for 11 million jobs in 1992.

At the same time these figures are very impressive, we are facing increasing global competition. In the Post World War II period, the United States accounted for 40 percent of global output. Now it's about 20 percent, and that's understandable. But it just shows that we have many more competitors and we have to compete in a very different world than we did in that period.
Moving to the issue at hand, I would say there is definitely a convergence of interest between consumer issues and trade policies issues. Over recent years -- and I think it's increasingly evident that we recognize there's a very strong relationship between our trade policies and our regulatory policies; and these affect consumer interests.

These issues are important both for exports -- in other words, you are the requirements that our industries have to comply with to enter foreign markets -- and for imports -- the role of the government to ensure that our standards are upheld and our consumers are protected.

I would like to briefly speak of a series of international agreements that provide the framework, at least in the trade policy sense, for our activities in these areas.

I'd like to spend a moment on a couple of definitional questions. First of all, these agreements deal with both standards, which are defined as those that are developed and maintained on a voluntary basis and regulations which are standards that have the force of law because they are made mandatory through regulations that are in force by the government.

These agreements deal with both of these areas, and they also deal very importantly with matters of testing and inspection and product approval, which has become known
as "conformity assessment."

And I would say, in the trade policy field, we are probably as concerned or deal more with conformity assessment issues than we do with the standards themselves, because this is where I think the trade policy intersection occurs: How products are approved to enter markets and be sold commercially.

The most fundamental agreement we have -- and the one that is drawn upon in other agreements that I will mention this afternoon -- is the agreement on Technical Barriers to Trade, TBT, as it's commonly known, which was originally negotiated during the Tokyo Round of trade negotiations and which was renegotiated during the Uruguay Round of multi-lateral trade negotiations and is now part of the World Trade Organization.

One important aspect of this development is that the agreement and its obligations previously were adhered to by only 45 countries. As part of the institutional construction of the World Trade Organization, all countries who are members of that organization must comply with this and every other agreement.

This means that right now we have over 100 countries who have ratified and are now obligated to this agreement. And within, probably another 18 months, we expect to have about 145 countries included in this

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So we are really talking about a very global coverage of commitments here. Let me just spend a minute on what that agreement does, and then I'll briefly note some other agreements that have similar objectives and principles.

The major objective of the agreement and its major commitment is to not use standards or conformity assessment procedures as barriers to trade.

The other basic commitment is non-discrimination, that is not to discriminate in the application or development of standards either vis-a-vis domestic producers versus foreign producers or one group of foreign producers versus another.

The final basic obligation, which is really more of an encouragement, is to use international standards. This is, obviously, a long-term goal.

But if more countries and industries use international standards, then the process of harmonization becomes automatic. The process of harmonization also is encouraged in these agreements as a long-term goal.

The basic principles of the agreement have now found their way into a number of other agreements, which I'll touch upon very briefly.

Foremost of these, perhaps, is the NAFTA, North
American Free Trade Agreement and, before that, the Canadian 
Free Trade Agreement, which builds upon the Tokyo Round 
agreement and expands it and intensifies it in terms of a 
smaller group of countries. Thus, we could tailor the 
agreement to meet the special needs of those countries; and 
it goes somewhat beyond the TBT agreement itself.

It's also -- certainly the NAFTA is in the process 
of revolution. There is a committee that not only oversees 
the agreement but looks to application of the agreement to 
new areas and to basically refine and expand its coverage. 
And I think some of the other people on the panel will 
probably speak of that.

We are now talking about these same types of 
issues in the APEC, the Asian and Pacific Economic 
Cooperation forum, which just had its summit in Osaka, 
Japan, last week and over the weekend.

There's been a great deal of work there to examine 
and identify the standards requirements in the various 
nations of that region. And there's a great improvement in 
our degree of knowledge of the problems and requirements 
that are our exporters face in that region.

We are also starting to negotiate a free trade 
agreement of the Americas, stemming from the Miami summit 
and more recently at Denver meetings.

Standards, here again, is an important issue. We
are at the very early stages of looking at the work program there. And this would be a very opportune time for interested parties to provide their views as to how work should proceed in that very important region.

Standards and conformity assessments issues are also addressed in a whole series of bilateral arrangements, too numerous to mention here this afternoon.

Basically, these programs provide us with an opportunity, I think, to use American leadership to encourage these countries to use or adapt themselves to U.S. standards and U.S. regulatory approaches. This is not an easy process; but I think it's an opportunity to provide American leadership.

It would also contribute to an easy form of harmonization if we could present our regulatory system to these countries and have them adopt or adapt their program to be compatible with it. It certainly would improve our trading relations and make it easier for our exporters to sell their goods in these countries.

So I would note that as an important opportunity.

Since I think I'm already nearing the end of my time, let me just make a few concluding remarks; and I'll be glad to come back to any of these issues later.

First of all, effective competition in foreign markets depends critically on the ability of American
manufacturers and exporters to conform to prevailing product
standards, regulations, and conformity assessment
requirements.

At the same time, we are very aware of the
legitimate role the governments have in protecting consumers
and ensuring the safety and quality of products that are
traded.

Both the WTO and the NAFTA provide disciplines in
a framework for resolving perceived barriers to trade; but
at the same time, they clearly preserve the sovereign rights
of governments in this area.

I am quite aware, as we seek market access and
negotiate our trade agreements, that we must seek the advice
and support not only of our industry and consumers but our
regulatory community within the government.

Working toward harmonization with our governments
on the basis of international standards, if that's possible
and appropriate, should contribute to safer products and
greater regulatory efficiencies.

I would like to commend the FTC for bringing
together this very important set of hearings. I believe
that it's a statement about the importance of this issue and
the need to work together in new and creative ways to
achieve multiple, but compatible, policy objectives.

Thank you very much.

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COMMISSIONER STAREK: Thank you very much, Mr. Meier. I'm no expert in this field, but I know that there are a number of international organizations that are looking at standards being utilized as non-tariff barriers against trade; and, yet, no country really admits to that. And so therein lies the dilemma.

Our next speaker this afternoon is Robert Hall III, who is the Vice President and Government Affairs Counsel at the National Retail Federation. He will continue our overview of international trade developments, obviously giving, not the government's perspective, but the private sector's view.

Mr. Hall joined the National Retail Federation as Vice President for Government Affairs in 1991. And he serves as the retail industry's primary strategist on international trade issues.

Prior to joining the National Retail Federation, he served as a Legislative Counsel to the Honorable Senator Sam Nunn, from 1987 to 1991. And today he will share with us his ideas on the growth of international trade and how businesses are responding to the challenges of globalization.

Thank you for coming, Mr. Hall.

MR. HALL: Thank you, Commissioner.

I would like to start off with a few introductory
remarks on the retail industry itself and where we see it
going, not only globally but also here in the United States.
I think that is instructive as to why some companies are
trying to globalize and also why some of the foreign retail
companies are having difficulties as they attempt to stretch
into the United States markets as well.

I think it's safe to say that in the retail
industry, we're seeing very dynamic changes within the
industry. Right here in Washington is a good example.
You're seeing fewer and fewer department stores. And what
we're really moving to are bigger national retail department
store chains with May and Federated and others being the
prime examples there.

And we all know about the closure of the downtown
Woodies and also the merger of -- or rather the acquisition
of Woodies chain by May and Penney as a joint venture, and
also in California the example of Federated buying out
Broadway.

We're also seeing even slowing signs in the
discount mass merchant end of the business. And there's
some thoughts among some analysts that perhaps we're
becoming over-stored on that end of the spectrum as well.

The apparel business, particularly the fashion
business, has been off for most of this year; although,
we're hearing some signs here in the Washington area that
November might look good; but there's still some real
concerns about where it's going to go for the balance of the
year and really into next year as well.

And what you're really seeing is competition from
all sides. You've got military PX's attempting to sell more
and more goods that have usually been restricted to retail
companies. The government and the armed service folks are
getting into those discussions.

You are also seeing manufacturers that are getting
more and more into the retail business, some with FTC
approval. Levi Strauss is one example of that. Liz
Claiborne and others.

You are even seeing catalogues becoming stores
with J. Crew and other examples of that nature.

I had to clip with interest, we now have what
we're calling cross shoppers. Women's Wear Daily, which is
the primary newspaper in the retail and apparel and textile
industries, has given quite a bit of ink, about eight pages,
back in the Spring to the advent of what we're calling cross
shoppers. And that is -- particularly in this case, it was
a study of women's apparel that people are shopping, not
only in departments stores, but also in specialty stores and
in discount stores and in factory warehouses and in discount
chains and at outlets. I mean, really across the board,
doing a lot of at home, direct. I mean, a real growth of
all sorts of retail formats, if you will.

Many have said that globalization is the way to go for retailers because of the fact that we've got some perception of over-stores here in the United States.

But I think it's safe to say -- many have said -- that that may, in fact, be just a myth and may be not the reality. With a very few notable exceptions, WalMart being one of them, the big push to globalize has not materialized at the levels anticipated by analysts just a handful of years ago.

Several problems have added to industry's chances of success as we move abroad; and one particular is market access, which I'll address in a moment. But also, quite frankly, retailers are having to look at using fundamentally different formats as they attempt to globalize.

Going in with your same, conventional approach doesn't work very well in many cases. And so as not to pick on any particular domestic firm, I will use two foreign examples in this case; and one of those would be the Galleries Lafayette. McKenzie & Company did an extensive study for the retail industry which was released at a Goldman Sachs' conference a few months ago.

And they looked at the Galleries Lafayette in New York. Here you have a French company coming in with high-priced merchandize with their sizes and fitting and labeling.
lined up in the French manner, of course, meeting the U.S. standards in terms of some labels. But in terms of sizing and perception and presentation, it was exclusively French.

You had also limited exclusivity. And, quite frankly, the business was Paris driven. It was not driven by a perception of what the retail market would bear in the United States, a perception of what the retail consumer was looking for in New York or in that area.

And, quite frankly, we saw the departure of Galleries Lafayette

A similar example would be Marks and Spencer's foray into Canada. That company expanded beyond it's normal apparel base and went into food retailing. It chose not to advertise because it had not been advertising in Britain; but, quite frankly, the Canadian consumer depended on advertising to form their decisions and to form their choices about retailing. So you really didn't see the big success that they may have anticipated there.

Let me turn now to international trade in what I would call an important corner for retailing. And this is on two fronts, both from the perspective of where we source for our products that we sell to U.S. consumers and also for our purposes of extending into other markets for market access purposes.

As we see the growth of private label apparel in

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the apparel sector, you're going to see more and more international sourcing.

Now, some have argued that it's going to grow at a much faster pace or faster clip than we believe in the U.S. retail industry.

Right now, according to the American Apparel and Manufactures Association, the U.S. and foreign mix of apparel is right at 50/50. That's their 1994 numbers.

But we will not see a march to off shore, in my sense -- in my judgment -- after the phase-out of the GATT textile apparel program in 2005 to the level some feared.

Quite frankly, our sense is that the import growths will level off and that we're going to see more U.S. home grown goods, particularly what I would call in-stock items, jeans, t-shirts, socks, underwear, and particularly goods of that matter.

We're also going to see what I would say is an increasing regionalism in the sense that, with the growth of CBI and Mexico as a sourcing alternative, there should and there can be with a CBI parity bill that could pass as soon as early next year. You will see more of the sourcing trends move from the Far East to this hemisphere and, quite frankly, keep scarce U.S. dollars in the western hemisphere.

In terms of market access, as retailers dip their toes into globalization, market access continues to be one
of our biggest issues in terms of the service sector expanding. We have worked closely with USTR and others in the past on this issue. But for retailers and people in the service sector, it means financial issues, it means customs issues, it means transportation issues, labeling, rules of origin, and a whole history of other issues.

One example I would point to you in particular and that is the example of Mexico.

With Mexico, we had what many called hip-hip-hoorays for NAFTA. There was a lot of excitement about moving into Mexico to serve the Mexican consumer and, quite frankly, for the Mexican market to help serve the U.S. consumer as well with goods.

But in an effort to block Chinese-made goods, the Mexicans put in place some very restrictive certificate of origin requirements that would make retailers and people who import in the United States and then, in turn, re-export into Mexico goods for the Mexican consumers -- it would make them have to come up with original certificates of origin for every single container of goods that goes into Mexico.

This is not only for retailers. This is for apparel manufacturers in the United States and others, textile companies and others, who want to import goods or bring in goods that are non-NAFTA originating, maybe U.S. made, but non-NAFTA originating for purposes of rules of

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origin under the U.S.-Mexico NAFTA agreement.

Now we are seeing a block on our efforts to come up with a self-certification proposal. This is hurting U.S. manufacturers. It's hurting U.S. retailers who want to re-export.

For example, let's say Company A wants to bring 100,000 pairs of shoes -- this applies to textiles, apparel, and footwear -- 100,000 pairs of shoes from somewhere in the Orient, let's stay Malaysia or Indonesia. They want to sell 90,000 pairs of shoes to U.S. consumers but 10,000 pairs of shoes into Mexico. When they bring that shipment into their warehouse -- that central distribution warehouse in the United States -- split it up, send 90,000 into their stores into the United States -- that shipment they want to send of 10,000 pairs of shoes into Mexico will be blocked at the border; it will not be allowed to cross because there's not an original certificate of origin that says "10,000 pairs of shoes, made in Malaysia," signed and documented by all the appropriate authorities there.

And this is a major, major concern.

And, quite frankly, as a trade lawyer representing the retailers, I also get calls from importers. I had a woman calling me from Miami just last week, quite frankly, in tears because she's got a shipment of apparel goods for consumers in Mexico. She can't get it into Mexico, nor can
she really get it back into the United States to try to turn
around and sell it somewhere else, because she doesn't have
the quotas and the Visas to sell it here in the United
States. She had it ready to go to Mexico.

So it is a major problem.

Emerging trend issues, as I see for the future, are: One -- and I know that Susan will address this more completely because the retail industry also has similar concerns as does the apparel industry, too -- and that is
labeling.

We are very concerned that labeling may emerge as
a form of market restriction. We urge the Commission to
look carefully at labeling issues, particularly "eco-
labeling" -- as we have now seen as it has emerged in the
European countries -- but also particularly the Care labeling issue that's before you right now.

Retailers and the retail industry, we will oppose
and continue to oppose any use of proprietary labels, such
as those used by GINETEX and other companies.

One other final -- rather, another trend is
technology; and that's one you have asked us to address
here; and I'm not the technology expert at the National Retail Federation. But I have had conversations with
several of those individuals, and I would like to point out
just a few of those for you this afternoon.

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Technology clearly plays an increasing role in all aspects of retailing, from quick response to inventory systems, to point of sale machines, to our increasing use of EBT, Electronic Benefits Transfers. This is an issue where you're going to see all federal income payments or benefit payments to any individuals who receive any sort of aid.

Right now it's restricted primarily to welfare and other AFDC payments. It's being used in a pilot program in Texas. But EBT-2, as they call it, the Electronic Benefits Two Transfer, will also add social security and other retirement benefits that come from the Federal Government.

People are going to be using a debit cart at their local retailer and at their local food store.

Primarily, right now, in the pilot stage, this is a food retail issue; but it will be moving into what I would call general merchandise and other retailing. And this is an issue of access. I think there's some fraud issues there you've got to worry about. A lot of other issues.

And, quite frankly, the reason the government is moving to EBT is to avoid the fraud problems of the checks getting lost and people forging names on their benefit checks.

But there is still the added problem of what to do about fraud in that area, too. And also simply just getting stores and other segments of the industry up to speed and

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ready to be able to serve the customer when they walk in
with their EBT card and want to use their federal payments
to pay for needed clothing, needed household items, or food.

   A parting comment, also, on interactive shopping.
   And this, again, being an area of electronics. This has not
been the strong success many in the retail industry had
envisioned.

   While a number of formats have been successful --
Home Shopping Network and others -- several high-end pilot
projects have really not gotten off the ground. And this
issue, quite frankly, went from being one of the hottest
topics at NRF's annual convention, national conference. In
January 1994, it was probably the hottest attended; there
were probably several -- 4, 5, 600 people in the room, one
of our big super sessions. It was one of the hottest issues
in January of '94. January '95, not a mention on the
program.

   And I use the annual convention as a real good
barometer, if you will, of retail interests and where the
trends are going. So, quite frankly, we did not see
interactive shopping take off like many thought it would. I
think we need to watch it continually for consumer reasons
and for technology reasons; but for right now, it's not
going to be the issue many had thought.

   Now, just one final thought on trade specifically.

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And that is -- and here again, we've been working with others in the industry, apparel and textile and others -- on moving to what I would call paperless transactions in trade. And there have been examples, and there are some pilot cases now of using what the Customs Service and the CITA folks -- that's the people, the Committee for the Implementation of Textile Agreements, who regulate textile and apparel trade in the United States -- are calling the ELVIS system. And it is a paperless transfer.

There are four countries that are presently using that for visa purposes. And that's Singapore, Korea, Philippines, and China. These right now also require parallel paper requirements. But we will be seeing in the future a paperless visa system and a paperless import system here in the United States, as all the kinks are worked out. So that's another issue to bring to the Commission's attention in terms of technology in the textile and apparel trade.

COMMISSIONER STEIGER: Very interesting.

COMMISSIONER STAREK: Yes, indeed.

Well, thank you very much, Mr. Hall.

I have just a couple of comments. The first is, with respect to the labeling issue that's before the Commission, I'm not going to say any more on that because we have certain rules about what Commissioner Steiger and I can
However, that doesn't stop any of you from commenting on that proposal because we are on the public record. So we will be anxious to hear any comments that you might have on --

MR. HALL: We plan to file formal comments, Mr. Commissioner. So we'll be doing that.

COMMISSIONER STAREK: Terrific.

The second thing is, you would think that I had much more to do with putting together this program than I really did. And the reason for that is our first two witnesses today have touched on the two principal issues that we are addressing in the OECD Committee on Consumer Policy right now.

The issue of non-tariff barriers against trade by international standards is a major project of that committee, looking basically at standards for the safety of products.

And the dilemma that I raised earlier is exactly what we're facing. Everybody seems to suspect that these standards are being implemented either too rigorously high to protect the domestic markets or the alternative is that they actually are high because there's a strong consumer movement in the countries and they don't want to lower their standards to allow other products into their markets. Both
of them seem achieve the same thing, and it causes a huge
dilemma, I would imagine, for trade officials having to deal
with it.

But it also causes a huge dilemma for consumers
who are denied access to products which may, in fact, be
safe.

The other issue that we're addressing is the one
raised by Mr. Hall, market access. We had a conference in
June of 1994 which basically said: Look, markets are
becoming globalized; but, yet, there are impediments or
barriers for consumers to participate in these markets.

What are these barriers and impediments? And how
can we get rid of them so that consumers can enjoy the
benefits of international markets?

So I find it interesting, and I think some of our
other speakers will comment on that.

We move now to another phase of our program and
that is the differing national laws that we face. And one
of the implications for enforcement by the FTC and by other
consumer law enforcement agencies, is what are we facing
with these differing national laws?

Believe it or not, in several European countries,
it's still illegal to have comparative advertising, as one
example; and there are many more.

Our first speaker on harmonization and potential
harmonization of international laws and what are the
impediments to that is Bill MacLeod of Collier, Shannon,
Rill & Scott.

And I notice that you must have gotten an old name
tag there from the Bush administration because Mr. Rill is
left off.

Before joining Collier, Shannon, Bill was the
Director of the Bureau of Consumer Protection here at the
FTC and also served as Director of our Chicago Regional
Office from 1983 to 1986.

And today he's going to talk about the role of the
FTC as the marketplace becomes more global, and what should
be the FTC's approach to regulation compared to the
enforcement agencies in other countries.

Bill, thank you for coming.

MR. MacLEOD: Thank you very much, Commissioner
Starek. Commissioner Steiger, it's a pleasure to be here.
And I, once again, would like to commend the Commission for
holding these hearings, but particularly holding this phase
of the hearings.

When I first got wind of the plans that the
Federal Trade Commission was going to have global
competition hearings, my first thought was: Well, I
certainly hope they also have plans to consider that subject
of which competition is a part, and that is consumer
And I am delighted that they have expanded the consideration of issues all the way to consumer protection.

My subject today is a little bit of a daunting subject as it's laid out in the agenda. I was asked to make some suggestions for how the FTC might be able to provide some leadership in the area of inconsistent international approaches, policies, philosophies when it comes to advertising.

And I thought that possibly the best way for me to give that advice -- not to be so presumptuous and tell the Commission how to do it and what to do -- but, perhaps, to pass on to the Commissioners a few of the mistakes that I had made in the course of my efforts to try to exert some leadership a few years ago.

And I think that, at least, in a couple of the areas where I found some frustration, there might be some keys for finding a way of exerting some significant influence, not only internationally, but also influence that can come back here to the United States.

One the things I discovered very quickly in my tenure as director of the Bureau and in my experience as a delegates to the OECD Consumer Committee is that consumer policies are very contagious internationally.

As Commissioner Starek and Chairman Steiger -- I
hope you don't mind, Chairman Steiger, if I call you by that
-- once President, always President; once Chairman. As I
think we have experienced in the last several
administrations, probably most of the time of the Consumer
Committee is spent with consumer protection officials of
various agencies comparing their consumer protection
policies.

What I discovered early on in that process was
that, by and large, there is a very broad area of agreement
of philosophies of policies that the consumer protection
officials are empowered to uphold.

Most of the countries that meet at the OECD are
countries that have general consumer protection standards.
When you look through them, you will see in many statutes or
cases or codes, whatever the source may be, likely to
mislead quotes; you will see allowances of puffery
recognizing that the impressions upon consumers of puffing
claims versus subjective claims is something that should be
recognized in the law.

Yet, at the same time we see some very puzzling
anomalies and inconsistencies among the various countries.
Commissioner Starek, you mentioned one of them: comparative
advertising.

When you run through the roster of what can and
can't be done in the various countries, it is somewhat
surprising. In some countries, buy one get one free is illegal. In other countries, it may be legal if the one you get free is one that is different from the one that you are buying. The reasons -- I think that Mari Ann will go into a little bit further -- delve back not to consumer protection ideas but to unfair competition ideas.

One of the problems that we see in a number of the other countries around the world is that they are a little bit like the Federal Trade Commission was before the Wheeler Lee Act. They are enforcing consumer protection standards as a result of unfair competition rules. And the consequence of that enforcement is that, while consumers are often a primary concern and consideration in the policies that develop, competitors often get equal say and equal consideration.

What are the implications of this?

I found fascinating a list that appeared in Advertising Age just a few weeks ago in which Advertising Age identified what they believed were going to be the next 25 global household words, the brand names that were about to burst upon the global scene. And they were such brand names as we have heard here: The GAP is an example; Acer computers, something that any of us who are fiddling in high-tech are admiring these days; also some names we haven't heard here in the United States, like Daewoo, the
Korean maker, and Ericsson, the Swedish telephone manufacturer. We're going to see more and more names like these around the world.

What I found fascinating from this list was the kinds of items that were not on it, the kinds of brand names that were not there. We saw nothing from health care, either health care products or health care services or any other professional services for that matter. We saw nothing in the nature of investments or consumer credit. We saw nothing in the nature of nutrition-oriented food products and so on.

There were a number of categories, categories that were as important as apparel, as important as cellular phones and computers, but for some reason, at least in the judgment of the experts at Advertising Age, not ready to break on to the world stage. Why is that?

I have a couple of suspicions, only suspicions but something that I think is worth further looking into.

Why not investment and credit? I think one very good example has to do with conversations I had early on in my days at OECD. One of the areas in which the other consumer officials were especially curious was about the United States' experience in enforcing its credit regulations. The FTC, as you know, has a major share of that responsibility.
And the other countries where credit instruments were probably ten years or so behind the development of the United States were also suddenly very interested in the kind of laws that we had established in the 1970's to govern our credit transactions.

I tried to tell my fellow delegates that, at the time the Federal Trade Commission was actually going through a little bit of reconsideration. We had recently modified some orders and we had done some other changes. We had issued some commentaries. Because one of the things that we had discovered was that, for example, in the area of truth in lending, we were asking for advertising to carry more disclosures than a lot of advertisements were able to contain. As a consequence, we were discovering that instead of disclosures, we were enforcing silence in consumer advertising; and the Commission modified its policies.

Nonetheless, while they were interested in that, they were far more interested in the volumes of regulations and statutes that we could provide them, and I did provide them.

But what I also provided, whenever I sent to another country the regulations and the statutes that we had governing credit or any other rule that the Commission enforced or another agency enforced, I sent them the Commission policy statements on unfairness, substantiation,
and deception and told them that when we consider regulations here in the United States, we consider them against the standards of deception, substantiation and unfairness that are laid out in these relatively straightforward, relatively terse, policy statements of the Federal Trade Commission; and I urged my colleagues to consider whatever regulations they wanted to adopt in the context of those statements.

Was I successful in the credit area? I'm not so sure.

Was I successful in comparative advertising? Well, as a matter of fact, a directive has just come from Brussels in which the countries in the European Union are being instructed, being directed to accommodate their policies to allow more comparative advertising. I'll be glad to get into some of the details of that later on.

I found it fascinating that a French television station that was running a story on this had to come over here to the United States to find a consumer group that was supportive of this change, because all the consumer groups in Europe were on the side of the businesses who thought that denigrating competitors was not particularly good for consumers.

There remains a very serious unfair competition hangover in Europe, and that infects a number of consumer
protection policies where consumers, unfortunately, are not sovereign.

It is not just, of course, an example of policies that prevent truthful claims from being made. Lest I sound like I am Johnny One Note here, let me mention an area where we're also seeing some concern and that is in the areas of environmental claims, especially eco-seals, where we are seeing a number of generalized environmental benefits being claimed, which probably would not pass muster under the FTC's environmental guidelines today; but are, nonetheless, for some reason, passing muster in some of the European countries. For example, if you reduce the oils in your oil-based paints, you can earn yourself an eco-seal in some countries; but you can't put that eco-seal on latex-based paints that have very little oil and emit virtually no VOC's, the goal of the seal itself.

How does that communicate to consumers? Which is the best form of VOC-reducing paint to buy?

How do we influence these policies?

My thoughts, back in the times when I was debating with my colleagues at the OECD, was that far and away the most valuable tool that I had was a tool that the Federal Trade Commission was almost in a unique, in the world, position to provide; and that was the studies of a respected agency of the Bureau that combined both competition and
consumer protection philosophy. And that is the Bureau of Economics.

A very influential development that was occurring in the 1980s was the development of the emerging health claims for foods in food advertising that some would say experienced a renaissance in the 1980's and generated a great deal of excitement around the world.

A good deal of that excitement was substantiated and confirmed by studies originating here at the Federal Trade Commission demonstrating that the change that the policies the FDA and the Commission pursued in food advertising and labeling were policies that served consumers well.

So my recommendations to the Commission from where I failed and where I think I partly succeeded is to remember, number one, that policies are contagious, policies here in the United States; try to make those policies as defensible as possible when we go overseas because our policies themselves and not our criticisms of the policies is what sells to our trading partners.

Secondly, arm yourselves with documents of the victims and the beneficiaries of unsound policy on the one hand and sound policy on the other hand.

With every Bureau of Economic study, with every Commission comment weighing in on the benefits of

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substantiation and deception-driven consumer protection policy, we stand a better chance of finding harmonious standards around the world.

Thanks very much, Mr. Chairman.

Thank you, Madam Chairman.

COMMISSIONER STAREK: Well, thank you, Bill. Very thoughtful comments. Appreciate it.

We move now to Bruce Silverglade, who is the Director of Legal Affairs at the Center for Science in the Public Interest. Bruce is known to virtually everybody here at the Commission. He coordinates CSPI's legislative and regulatory activities in a wide variety of areas involving consumer protection.

Bruce is a frequent critic of the Commission, although I haven't heard any criticism lately. So maybe we'll give you an opportunity here.

Today he will speak about the importance of having strong consumer protection standards that can serve as the basis for international standards and will warn us, I think, about harmonization which could result in lower standards for U.S. consumers.

Bruce?

MR. SILVERGLADE: I thank you, Commissioner Starek, Commissioner Steiger.

Good afternoon. Today I would like to make two
points regarding consumer protection regulation in the new era of global competition.

First point is that consumer protection regulation is actually necessary to maintain U.S. economic leadership and international competitiveness.

If you look at traditional consumer group priorities whether it's ranging from honest labeling of food products to safety standards, these are regulations that are all necessary to help maintain U.S. economic leadership.

Oftentimes just the opposite is talked about; consumer protection regulation is called a barrier to competition.

But in reality, the consumer rules help maintain the high standards that American products and services are often known for. And when we haven't had high standards, we paid the price in the loss off international competitive position.

For example, if you look at American automobiles, which have, until recently, had a reputation for poor quality, we certainly suffered in the international marketplace.

Much of my time is spent in the area of food regulation; and if you look at food additive regulation, consumers in Japan will not buy many of our processed foods because they contain particular additives that are
considered not appropriate or safe in Japan.

There was a controversy over growth hormones used in cattle. Consumer groups in the U.S. and in Europe did not want to see these growth hormones used just as a matter of consumer preference. The European Union, in fact, prohibited the use of the growth hormones. We didn't. It was difficult for us to sell our cattle in Europe.

So by maintaining high consumer protection standards, it will actually help increase our international competitive position.

The FTC, obviously, has a big role to play here. Lots of FTC activities -- current activities as well as prior activities -- could be reinvented to create the appropriate economic incentives to increase product quality and, again, maintain our leadership position and our international competitive position.

My second point is how the FTC should go about doing this. And I'm recommending that the Commission develop a formal policy for strategic participation in international forums to ensure the upward harmonization of consumer protection requirements around the world.

U.S. regulations, ranging from nutrition labeling of foods to fuel efficiency requirements for automobiles, have been called the "technical barrier to trade." And in order to defend the attacks on U.S. consumer protection
standards, the FTC must be very proactive. This is a situation where the Commission is going to have to step in and weigh in very actively.

The Commission should develop a strategic policy for participation both in governmental and private sector regulatory activities and standard-setting forums on the international level.

And by encouraging the upward, as opposed to the downward harmonization of consumer protection requirements, the Commission can help ensure that U.S. standards remain the leading standards in the world and set the trend and the scope of the debate.

I have some specific suggestions for elements of a Commission policy in this area.

The first element of the Commission policy should be to preserve and enhance the Commission's ability to accomplish its statutory responsibilities to protect consumers from unfair and deceptive practices. It obviously has to be the guiding light, whether the Commission is working on domestic issues or participating in international forums.

The second element of the Commission's policy that I would suggest would be to ensure that U.S. consumer protection regulations and standards are maintained except when a regulation or standard of another nation provides
consumers with a greater degree of protection from unfair
and deceptive trade practices.

And, of course, I suppose that's open to
interpretation: What is a greater degree of protection?

I was meeting with a delegation of Japanese health
food manufacturers who were really appalled to see the
Kellogg's "All Bran" label in the United States actually
mention the word "cancer." They thought that was bordering
on fraud. And they were health foods manufacturers in
Japan. So whether health claim rules here have been
beneficial or not, I think, is open to debate on an
international level.

The third element that I'd like to see in a
Commission policy is to provide for and encourage the use of
international consumer protection regulations or standards
only when such action will not result in the downward
harmonization of consumer protection requirements. That's
the converse of what I previously stated.

And, lastly, a procedural point, the FTC's input
into international regulatory and standard-setting
activities must be ... "transparent" is the word that's
being used in the context of this type of debate.

In other words, it should be open to public
scrutiny. And the Commission should provide all interested
parties with an opportunity to participate. And this is, of
course, logistically difficult, since we're talking about international forums and international conferences, meetings, and so forth.

If sum, the FTC has an important role to play in international activities. And by defending U.S. consumer protection standards when they are the highest, the FTC can further its statutory mission as well as advance U.S. economic interests and improve consumer welfare at home and abroad.

COMMISSIONER STEIGER: Can I ask a question?

COMMISSIONER STAREK: You sure can. We should have you send this statement to our trade press, since you think it's important that we participate in international forum.

COMMISSIONER STEIGER: Bruce, nobody knows our budget constraints better than we do unless maybe it's those who have watched us for as long and with as great an interest as you do; so, obviously, we have a few barriers here ourselves.

I know you have concentrated most recently on food advertising and nutritional areas. But as you were listening to your counterparts and to other government officials in a global setting, could you rank the areas of concern where it is felt we are, A, too strict or, B, where we are too lax?
Is there any kind of consensus in the consumer protection area?

MR. SILVERGLADE: Well, I think there are differences. As a general matter, we have the strongest rules, I'd say, if you had to generalize. But there are important exceptions.

In tobacco marketing, our rules are weaker.

In alcoholic beverage marketing, our rules are weaker.

Even in the area of food marketing, in Canada, until, I don't know, about five years ago, every food advertisement that was broadcast on Canadian television was precleared by the government, by the Department of Health and Welfare.

Now they have since delegated that to an entity similar to the National Advertising Division of our Council of Better Business Bureaus, a similar organization that operates in Canada.

So they still look at every food ad before it's broadcast, because they consider it so important to health that this preclearance process be undertaken.

So in those areas, we certainly have less strict regulation. And I would argue, that we do not protect consumers as well. Bill MacLeod might argue with that.

COMMISSIONER STEIGER: Thank you.
Thank you, Roscoe.

COMMISSIONER STAREK: Thank you. That was very interesting. I think there is a legitimate fear that by engaging in international discussion on standards, you know, somehow you reach a lowest common denominator for everybody in order to reach an agreement. And that is something, it seems to me, that is not in the best interest of consumers in any country.

Our next speaker may have a different view on all of that. She is Mari Ann Blatch, who is the Vice President of Governmental Affairs at Readers Digest where she has served in that capacity since 1974.

She has worked with Readers Digest companies in 33 countries to support and encourage the establishment of local direct marketing associations.

And today she will speak about how legal standards differ from country to country, the difficulties this poses for businesses and companies trying to do business internationally; and she will share with us her views on the appropriate direction for harmonizing consumer protection standards.

Mari Ann, thanks for coming.

MS. BLATCH: Thank you very much.

And I just wanted to say that, on behalf of Readers Digest, which is a global company, some of my
comments I believe will be relevant to other marketers that are fully invested in the countries in which they are doing business.

We talked earlier in this session about exporters or importers. My remarks are directed towards companies that are actually operating in the local market, with local staff, in our case local editors, in the local language. Our books, our music, and all of our advertising campaigns are created on site.

One of the ways that I, as Director of Consumer and Government Affairs, have built my grid of regulations from around the 40 countries where we do business has been by working with the local trade associations. And we can do that because we are present there.

But for those American companies that are not present -- and we're the only magazine that is present in each country and has unique products. Most others ship them from the United States. For those companies, what they have turned to in order to be able to build global campaigns is basically to follow the rules set by the FTC.

So perhaps you won't be surprised to hear that I absolutely agree with Mr. Silverglade that the FTC must continue to participate in the international forums, both the formal ones and your bilateral mentoring and coaching, and the new developments of the U.S.-EU transatlantic
dialogue.

At the same time, I absolutely, 100 percent, agree with what Bill MacLeod has said, which is that while we are talking with our partners and particularly the continental European partners and particularly those that are influenced by the German system of unfair competition, we need to have a better understanding about what we mean when we use the word "competition."

In the U.S. we gave up fair trade laws years ago. In Germany when we have discussions with our German colleagues about consumer protection, they say, oh, yes, we have consumer protection; we have our unfair competition law.

I just came back from a visit to the European Union's Commission Number 15. And the reason I was visiting there last week is that they announced, in July of last year, a specific project to look at the regulations which should be harmonized in Europe on commercial communications.

Now they define commercial communications as all forms of advertising, direct marketing, sponsorship, sales promotion and PR.

In their first newsletter, which was just issued this year in July, the lead article focuses on sales promotion which they define as gifts, premium discounting, and similar sales incentives.
In this article, they point out that there are such vast differences in the national laws in Europe that there is an acute problem for transporter -- advertising and transporter marketing in Europe.

At one end of the spectrum, you find the UK and Ireland whose rules are very similar to those in the United States.

At the other end is the heavily regulated German market where the law imposes complete prohibitions in the name of unfair competition.

At our meeting, Readers Digest Europe, led by our German lawyer, documented the differences and our experience with the differences in those laws.

I will leave the document which I gave the Commission for the Federal Trade Commission as part of these hearings.

On Tuesday I was told that the current timetable for the release of this green paper on commercial communications is January or February of next year.

Directorate 15 and Commissioner Bangeman, who is, you know, the father of the European information superhighway, is very concerned that we should lift restrictions in the name of unfair competition so that there can be -- so that the advent of on-line, digital, broadband communications would increase in Europe and would allow
further opportunities for the reception and use of transporter commercial communications.

They have told me that they are willing to assess in a completely objective manner, as Bruce would approve, in the highest consumer protection standards and, as Bill and I are arguing, not in the name of competition standards, all regulatory barriers to commercial communications in Europe.

In our discussions with the Commission we at Readers Digest listed the burdens that we currently face operating in Europe as a direct result of these differing legal restrictions.

Of course, first would be the extra cost of having to plan and produce separate marketing material for each market.

But more importantly the loss of business in one market because, for example, in the UK, to introduce our magazine to new subscribers, we can offer a half-price introductory subscription and we can also offer a premium of any sort that we would like to offer and of any quality we would like to offer.

In recent discussions with our operations people in Europe, they tell me, because of the restrictions on not being able to discount a magazine offer and not being able to offer premiums in German, our business, although it is huge -- and it's certainly a good part of 50 percent of our
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businesses out of Europe and 50 percent of our European business is Germany -- nevertheless, it has not been able to reach the potential it would have if we look at our operations in Canada, in Australia, in the United States, the UK, or Ireland.

I'm really encouraged and I'm really excited, and I think we have some good news and some good fun in front of us. Because the EU commission is determined to remove these barriers. I was told last week, quote: "No where in the Rome Treaty will you find any provision for protection of competition." And continuing the quote: "A country must justify its competition laws on the basis of consumer protection. And in meeting that objective, the law should not have a disproportionate affect on international trade."

It would be very important for the success of American marketers, both in the traditional and in our ventures into the new media, if the FTC would support the European Commission and would work with them when their green paper is released for comments.

I firmly believe that if the United States and the European Union were to release studies from the FTC's Bureau of Competition and from the EU Commission Directorate 15 stating that unfair competition laws in the field of commercial communication are harmful to consumers and bad for the information flows, that countries like Japan, which
have modeled their laws on Germany, and countries like
Taiwan and other emerging countries that are still trying to
decide which model they will follow, will definitely be
influenced; and we have a definite chance to make a
difference.

I was also asked, when I was invited here, what
specifics I could recommend for the Federal Trade
Commission's future actions.

And I think basically what I'm trying to say is
the same thing that's been said. I would just add one more
factor, and that is that global business has been working
for so many years in trying to develop self-regulation and a
sort of private sector harmonization. And particularly I
think you're aware, the International Chamber of Commerce
has issued codes on advertising practice, on sales
promotion, and direct marketing. We're in the process now
of updating the code on direct marketing to include
interactive advertising.

Carla Michelotti, who testified here the other
day, is the chairwoman of that subcommittee. And what is so
good about something like the International Chamber of
Commerce, it's a place where companies, not only U.S.-based
multi-nationals, but Japan and Australia and Germany and so
forth can get together and talk about what we think are
common agreements on certain principles of consumer

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And I think you'll find that we'll be allies as you move forward. And we certainly wish you the best. Thank you.

COMMISSIONER STAREK: Well, thank you very much. I had occasion about a year and a half ago, very early on in this process, to meet with three of the European Union staff who were assigned to this project. And at that time, the debate was which directorate was this project going to be in. And fortunately it ended up in DG-15. And fortunately the people who are working on this effort are economists, who, you know, have a bent against the traditional European lawyerly regulation approach.

So I was somewhat assured, after an evening of conversation with these folks, that maybe we will see a good product. And the first draft of the green paper, of the initial submission, I thought was very promising.

MS. BLATCH: I agree with you entirely. In fact, in my conversations on Tuesday, I had come with all the lawyers for Readers Digest in Europe to provide some hard data on existing law. And instead I was given a lecture that we should be really concerned about any obstacles like unfair competition, restrictions which would not allow Readers Digest to attract people onto our on-line site.

They know that we have been developing, with...
Microsoft, a Readers Digest home site. And he said: How
are you going to get the customers to come and look at your
site? You're going to need sales promotion; you're going to
need half an hour free time offers; you're going to need to
use direct mail and say here's where my home site is and
here's a gift or here's a discount for time.

And I said, yes, yes, I believe you. I'm glad
your doing this.

So the only other thing was he did ask that all of
us who have any opportunity to have any contact with Europe,
please do keep in all our discussions with Europe saying,
where's the green paper? They're just worried that other
priorities might mean that it won't come out in January or
February. So it would be most welcome if the U.S.
Government continues to hope that it comes out and once it
comes out enters into dialogue.

Thank you.

COMMISSIONER STAREK: Thanks. Well, they have a
lot to overcome. I can recall once in an OECD meeting one
of the German delegates, we were talking about the
relationships between competition policy and consumer
policy, which is something that is difficult for some
Europeans to grasp; although, I must say, the international
consumer organizations have grasped it and understand it and
are trying to educate folks, both government officials and

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consumers in Europe, about the direct relationship.

But anyway, this fellow said that competition policy begins where consumer policy ends. And I still haven't figured out what that means.

Our next witness is Steven Spivak, who is a Professor at the University of Maryland here at College Park and serves as the Chairman of the Consumer Policy Committee, International Organization for Standardization.

Since I'm having trouble talking, I'm not going to go through all of this. However, I think what he's going to talk about today are International Standards Organization standards; how they're developed, as well as the role that they play in international trade.

Dr. Spivak, thank you for coming.

MR. SPIVAK: Thank you, Commissioner Starek, very much. And I'll take over and give you the opportunity to save your voice.

COMMISSIONER STAREK: Thanks.

MR. SPIVAK: Since I'm a university professor, if you'll bear with me, I'm going to, as is customary, work from the overhead projector.

I might say in opening that I'm not an economist and I'm not a lawyer, but I am an engineer.

Thank you. I may be the only one in the room.

Commissioner Starek mentioned the OECD. I have
brought a copy -- if you have not seen it, I call to your attention the OECD publication on Consumer Product Safety Standards and International Trade.

Although it's 1991 -- which may sound a bit dated in this time of fast-moving trade developments and mutual recognition agreements -- it is available from the OECD bookstore in Washington, D.C. It's still, I think, very timely.

I have brought information on the ISO Consumer Policy Committee proposal. And I've prepared -- and I believe it's outside on the table -- a small annotated citation list with reference to standardization, globalization, consumers, and international trade. And these are available outside.

What I'd like to do today in the short 15 minutes is go through what I hope will be helpful. I will focus on standards and standardization, but an overview and a structure of company, state and local, national, regional, and international standardization.

So I will build us up that structure, focusing eventually on the ISO International Organization for Standardization and its Consumer Policy Committee and then work back down in summary to where I believe there can be value to the Federal Trade Commission in its policy development and future work in regard to learning from other
examples of national and international standardization.

This cartoon says: If things don't fit, you have a standards problem.

I guess it's -- if any of you have fought with either incompatibility or lack of the appropriate sizes in computer diskettes or information storage units, that's a classic example. It certainly happens in our office, and I'm sure it's happened in yours.

It is, however, an example being dealt with by international standardization.

I bring you a particular -- premier good example. In fact, I believe this is from a Canadian publication, Public Consensus. But it says: Standards to enhance the international compatibility of credit cards. And it's a reference to ISO-2894, for the standardization of international credit cards.

It is one of many, many examples of international standardization to allow you to move through almost any country in the world, take the credit card, almost without thinking, out of your pocket, put it into a machine and be able to have it read at almost any bank machine around the world, an example of international and national standardization.

Since textile care labels were mentioned earlier and I happen to be both a textile engineer and now Chair of Heritage Reporting Corporation

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the Department of Fire Protection Engineering at Maryland, with interests in textiles and furnishings, I give you some examples.

Mr. Hall mentioned the exquisite French -- an example of the exquisite French labels, examples that I've dealt with. Care labels, whether they are in French or German or English or Spanish or Japanese, in the United States, an example, of course, that was mentioned and may come up later with more expert colleagues than myself -- although I have been heavily involved as well -- of the development of international standards. This happens to be ISO-3758 for international care labeling symbols, one example of the use of symbols in international standardization.

What I'd like to focus on, however, for perhaps the next five minutes is a hierarchy or a structure for standardization. I believe it's very important to put into perspective all these standards that we speak about.

Where do they come from? Where do they stand in terms of their relationship, their interaction?

And when I say hierarchy, because I'll bring it back, I don't necessarily mean to imply, as I go up this important axis, that higher is necessarily better. I will express some of those opinions later, but I want you to realize that, certainly in the United States, all of these
standards coexist.

This is an adaptation from Lyle Verman (Phonetically) from his excellent book on standardization, in which, in three dimensions, standards are put in perspective. And let me just summarize those for you.

One of the axes is the subject of standardization. And we, of course, heard mention today standards for textiles and clothing, standards for food, for medical equipment, for communications, for consumer products.

So one of these axes talks about the products or systems that are covered by standardization. Another axis speaks about the aspect of standardization as mentioned by Rich Meier and others, whether these are quality standards, whether they are legislation, trade regulations, rules of the Commission, safety standards, packaging and marketing. We've heard about testing, inspection, environmental standards, codes, whether they're fire or electrical codes; purchase specifications, such as quality product lists.

All of these different uses, if you will, or examples of standardization apply to all of these products.

But in addition -- and it's the focus of the discussion today, one raises the fundamental question: What is the level, if you will, or the scope of the development of standardization?

And I think I have, I hope, an important message
to say that in the United States -- and forgive me if you're well aware of this -- we have a very large body of company standards, in-house corporate standardization, usually used between buyers and sellers who work with those companies, tens of thousands of them.

We have industry standards, standards of the trade of a particular industry. An example, Association of Home Appliance Manufacturers, AHAM, will have it's industry standards on labeling of consumer products.

We have cities -- the City of Boston, the City of New York -- who will have their own fire codes, electrical codes, elevator codes and safety standards.

We, of course, have state regulations. Almost every state will have its own purchase and procurement regulations that are mandatory to do business with the state.

But some key examples, California, that has its own emissions standards. California has its own home furnishings -- upholstered furniture flammability standards.

So there are unique state regulations in the United States.

There are, of course, voluntary national standards. And I mentioned but two examples. In the United States you can count up to 400 different standard developers in the United States, not necessarily exclusive, with no
offense to those not mentioned, but ASTM is one example, Underwriters Laboratories, Society of Automotive Engineers. Hundreds of these that developed national standards. They are coordinated in the United States by ANSI, the American National Standards Institute. And of the more than 100 countries in the ISO, International Organization for Standardization, there are two that have a private sector national bodies. And that's ANSI, is the U.S. member body, and Switzerland also has a private sector body. So ANSI is our private sector coordinator in the national voluntary arena. In the national mandatory arena, of course, the development of the Federal Trade Commission, trade reg. rules, the Code of Federal Regulations, all of the -- GSA, General Services Administration, and Defense Procurement Standards, if you will, are national mandatory standards. At the regional level, the key examples, already well mentioned, are European Regional Standardization, whether they're EN's, European Norms, maybe voluntary; whether they're voluntary; whether they're European directives, such as product safety directives that would be mandatory. At the international level, we have voluntary standardization, such as the ISO, International Organization for Standardization; the IEC, its counterpart, in the

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electro-tech area; and now the ITU, in telecommunications. So effectively we have, at the least, a tripartite, three partners, in voluntary international standardization. International mandatory, there are a number of these. One was mentioned, of course, the GATT standards code on technical barriers to trade and what will be its successor, the World Trade Organization also with a standards code. Signatories, the OIML is a legal methodology. So there are international mandatory or treaty organizations. And all of these play simultaneously. In the United States we are unique in that we probably have the most decentralized, many say the strongest and most competitive national standards body because there are so many players involved. Canada, not quite as decentralized as ours with a coordinator, the Standards Council of Canada, equivalent, in our case, to ANSI. And then six accredited standards developers. And we have Canadian experts who may address that.

We are focusing on national standardization. Let me simply remind you, our voluntary ISO member, private sector coordinator, the American National Standards Institute; it coordinates the voluntary standards activities
in the U.S. It approves standards from other developers, as
American National Standards. ANSI represents the United
States' interests in international standardization, and it
is a source of information and access on worldwide technical
standards.

Very quickly, examples. Who needs standards?
Well, both American National and ISO, International
Standards Organization for photographic film. Many of you
who simply put 35 millimeter film in your camera, your
automatic cameras, if you look closely enough, you'll see
that the film speed is an ISO standard, whether it's ISO
400, 200, 100. Okay? An international standard works so
transparently well that we don't hardly appreciate.

SAE, ANSI American national standards for oil, for
the viscosity of the oil in your automobile, again a premier
example, nationally and internationally.

And in this particular time of political
campaigns, I brought one -- this happens to refer to the
fact that the glasses that we're all wearing are made and
conform to safety standards, in compliance with American
National Standards. And this particular campaigner doesn't
to have his glasses fitted properly in that he's shaking
everyone's hand who comes by.

Back to the more important issue at hand. Let me
now move up the ladder through national, regional, to
international standardization. And I will refer to the
International Organization for Standardization and its
Consumer Policy Committee, affectionately known as COPOLCO.

The ISO is structured with approximately 200
technical committees; but there are four policy committees,
one of which is CASCO, Conformity Assessment; another of
which is the Consumer Policy Committee of which I have had
the great honor of being able to serve the past five years.

The Consumer Policy Committee reports to the full
ISO general assembly, but it holds formal liaisons with the
OECD, which has been mentioned. It has a close liaison with
what was the International Organization of Consumer Unions,
now Consumers International, their new name.

And what do we do? What we do is we study issues
of assisting consumers in national and international
standardization. We promote from the consumer's point of
protection, the information and training of consumers,
provide a national and international forum for the exchange
of ideas and, maintain liaison with other important
organizations.

Some of the key things that we will do that I will
focus in the last few minutes are — the COPOLCO played a
key role in setting up the first clarion call on the
confusion over the lack of ecological labeling or
environmental labeling standards, which eventually led to
major efforts by the ISO and other partners in beginning to
develop the body of international standards for the
environment.

COPOLCO has taken the lead, I believe worldwide as
well as at the ISO, in the development of standards for
services and service quality. And I will give you some
specific examples of that.

COPOLCO has been working on using a summary of all
of its national standardization members, including the U.S.,
in developing criteria on priorities for selling services.

And the COPOLCO members recently prioritized a
list of 15 items that they believe, as consumer experts, are
key for national and international standardization. And I
bulleted just several of interest to the Federal Trade
Commission.

Air and water quality; medical and hospital
services were mentioned; smart cards, including banking
services; environmental management systems and environmental
labeling; energy labeling, which we'll hear about; public
information symbols, okay? whether they're road signs or
textile labeling.

The Consumer Policy Committee has -- this is not a
complete list. It now has 64 members, of which most recent
members have been Mexico, Lebanon, Mauritius, and others.
So we have a very broad base of the entire structure of
international standardizers.

On the references, there is lot of information about how ISO serves the consumer, so I won't belabor you; and I don't have the time to do so, but there are detailed articles in the ISO bulletin.

Let me close just with a few examples that I believe are of interest to the ISO.

One of the things that COPOLCO does is it participate in and also contribute to the development and publishing of ISO IEC guides. These are international guides, not formal standards per se. And one of these has just undergone a major revision. That's Guide 37: *Instructions For Use of Products of Consumer Interest*. That was approved by the ISO and the IEC in 1995. And I'm awaiting the formal receipt of the final printed document.


We publish a consumer communique twice per year. And, again, I brought you a specific example that I hope piques the interest of the FTC. This is the first page of the most recent example, an Australian national standard on complaints handling. They believe it to be a world's first in terms of a national standard for consumer complaints handling and resolution.
COPOLCO has been focusing on the very important issue of international standards for services, and we held a major meeting in Beijing, China. And one of the references is a recent issue of the ISO bulletin, a major feature article, 20 pages on service standards.

And I believe that's important to the FTC.

Let me give you some examples that I think would be of use in terms of national standardization, being worked intellectually by COPOLCO in service standards.

I've mentioned the Australian standard on consumer complaints handling.

I mentioned what is a final draft of the Canadian CSA standard on data protection and privacy for personal data and protection for consumers.

A New Zealand national standard, a new rating scheme for the entire hospitality industry, hotels and motels.

The United Kingdom, a new national code of banking practice, in part, for the protection of consumer.

APNOR, in France, new national standards established for the service industry. And the first national service mark has gone to a furniture moving company.

Again, issues of importance to the FTC.

The United States, the Toy Manufacturers of
America in concert with European toy manufacturers and the Council of Better Business Bureaus are working on a draft ISO-IEC guideline on guidelines for advertising to children, a very important and interesting area.

In summary, I bring you a different picture of this international organization. This is a different perspective. It happens to be a pyramid with company and national standards moving up through international. It's a different focus than the previous chart that I gave you, but it gives you a different way of thinking about what's really important, who is at the top of the pyramid, or is there no pyramid at all?

In the interest of time, Commissioner, I will stop at this point. And if there are any substantive questions, I would be pleased to address them.

COMMISSIONER STAREK: Well, thank you very much. I found that to be very educational. I was aware, generally, of how standards are set but not in such detail; and I found it extraordinarily interesting and helpful.

Our next speaker today is Susan Lord, who is Vice President of Government Relations for Springs Industries Inc., where she serves as the industry advisor on textile trade policy and negotiations.

And she also Chairs the Export Subcommittee of the American Textile Manufacturers Institute.
I think today she is going to speak about the need for harmonization of standards applying to textiles and how the FTC can contribute in this area.

Ms. Lord, thank you for coming.

MS. LORD: Thank you, Commissioner Starek.

Just by way of introduction, Springs Industries is one of America's largest textile and home furnishing companies. We currently have sales of just under $2.5 billion, and we employ approximately 24,000 people.

I'm a member of the International Trade Committee of ATMI, or the American Textile Manufacturers Institute, which is the national association for textile products. And I'm Chairman of both the Export Subcommittee and the Home Furnishings Subcommittee.

ATMI's members process 80 percent of all textile fibers processed in the United States and are engaged in every facet of textile manufacturing and marketing. ATMI members collectively employ 670,000 people.

So it's from this perspective that I am speaking this afternoon.

Two and half years ago when I left the world of marketing apparel fabrics up in New York for Springs Industries, I really had no idea how standards were set. I had never heard of ANSI or ASTM. I had heard of ISO but had no idea how it functioned. But I found, as I became an
advisor here in Washington, I quickly became aware of standards and their importance within the international trade community.

Beyond this, and most importantly, I found the need for industry to be involved.

During the NAFTA negotiations, the textile, apparel, yarn, and fiber industries fought hard to ensure favorable rules of origin -- though I'm not sure Rob would necessarily agree with me on that -- an acceptable schedule for the phase out of tariffs, and the elimination of non-tariff barriers.

One of the potential non-tariff barriers that were raised during the negotiations was the issue of standards and the need to work towards harmonization.

In 1991, at the request of the government's negotiators, the national standard organizations of the three countries met to discuss harmonization. The result of this meeting was the formation of a series of sector-specific industry groups.

For our industries, the specific need identified was label requirements for apparel and home furnishings. The Trilateral Labeling Committee was formed, and I became a member in 1993.

Each country requiring different information presented different levels of detail in different formats in
different languages. The task was large: How to conform, how to come to a consensus.

The labeling issues identified included fiber identification, country of origin, placement of labels, manufacturing or importer identification, and Care labeling.

With representatives from three governments and the private sector from each country, the committee has met numerous times with the goal of identifying all the issues and reaching consensus on solutions satisfactory to all parties.

While progress has been made, consensus solutions have not been achieved. And that's been four and a half years.

One of the largest issues facing the committee was Care labeling.

Let me just highlight -- give you a brief rundown of what we're facing.

In Mexico, Care labeling is required for both apparel and home furnishings. Care instructions may be expressed using a care code symbol system as you saw on the screen earlier or in Spanish.

Canada does not require care instructions for either; however, if instructions are included, they may either be expressed in the Canadian care code symbol system or written in the appropriate language. And as you know,
English is appropriate for all provinces except Quebec. And there it must be expressed in French.

The United States requires care instructions for apparel but not for home furnishings. And the instructions must be expressed in English. Care code symbols are currently not acceptable, though we're moving rapidly towards hopefully adopting some.

The result of the above is that companies selling products in these countries or retailers importing their own product directly must either maintain separate inventories by country or develop a single, large label that meets all requirements.

The label is often, as I said, large, confusing to the consumer, and expensive to produce.

The consensus of the committee is that the mutually acceptable care code system would greatly simplify labels by eliminating tri-lingual instructions, thus reducing manufacturers' cost and eliminating the need for apparel and home furnishing manufacturers to carry country-specific inventory.

Further, the committee feels that with some education, a label with care code symbols will be more consumer friendly.

In order for the United States to accept a care code symbol system, current labeling laws must be amended.
This effort is, in fact, under way. And the Federal Trade Commission, recognizing this need, requested comments last fall on the use of the care code symbol system and published just last week its proposed recommendations with requests for comments on a condition exemption allowing for the use of certain care code symbols.

The proposed system has been developed by ASTM during 1991 in response to ISO adopting a care code symbol system over the United State's vehement opposition.

The ISO system was developed by GINETEX an international care labeling organization that licenses the system to member countries and requires users, in most cases, to pay a fee.

The U.S. industry opposed this system as it required a licensing fee and does not meet the technical requirements of the U.S. law or consumer needs.

The industry needs a voluntary system that is simple and easy to understand and still conveys all the necessary information to the consumer. Our goal is to seek simplicity and flexibility. We need to ensure that the system the U.S. adopts meets our needs domestically and similarly can be used as the basis for harmonization internationally.

I want to take this opportunity to express the industry's appreciation for all the efforts put forth by the

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FTC in developing its recommendation for a care code symbol system.

It has taken industry comments and consumer needs into account and proposed the basis for a very usable system. With trade among the NAFTA partners in textile and apparel increasing over 30 percent to $5.4 billion in the first full year of NAFTA and with the greater emphasis on exporting within the industry, the need to harmonize our standards increases daily.

Once the United States adopts care code symbols, the basis for harmonization will be in place. Without symbols the chance for harmonization within NAFTA and on a global basis is non-existent within the care codes for textiles and apparel.

I would only add that there's a great urgency to move forward with care codes and to move onto other issues I mentioned before. The FTC is in a unique position to be able to help the industry domestically while considering the international trade implications and still meeting consumer needs.

While our immediate need is for harmonization under NAFTA, we need to continue to think globally. What happens when Chile joins NAFTA? Do we start over? What about the free trade agreement of the Americas and the possibility of free trade with the EU where GINETEX is the

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accepted system?

I would urge the FTC to continue its work to harmonize with the NAFTA countries but to continue to think about the need for global harmonization in all decisions.

Concurrent to the work on harmonizing care labeling within the NAFTA countries, several domestic sector members of the Tri-lateral Labeling Committee and members of the ASTM subcommittee on care labeling met with GINETEX last fall to try and work towards a system that would be mutually acceptable and hopefully could be proposed as the new international standard when ISO meets to review the current standard in 1996.

While GINETEX has expressed interest, much has yet to be done. The system the FTC proposed is a step towards meeting this goal.

The recommendation of the FTC to adopt a care code symbol system would be a major first step in gathering the support necessary to the work toward ISO adopting an international standard acceptable by the U.S.

As we all look to expand our markets beyond our borders, we're going to be faced with numerous challenges. International standards are going to play an increasingly important role in the world of international trade. We need to work to ensure the development of international standards support the needs of our industry and do not become

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non-tariff barriers. We must continue to share information
and work together to achieve this goal.

Thank you.

COMMISSIONER STAREK: Well, thank you very much.

And thanks for your -- I'll take them as very complimentary
comments. I appreciate it.

Our final group of speakers today -- we have a
tandem to conclude this round before we get into our panel
discussion. We will hear, as we did this morning, from the
Canadians. And we will hear the Canadian experience and
receive a Canadian perspective on all of this.

Our witnesses today are Mr. Zane Brown, who's the
Director General of Consumer Products Directorate at
Industry Canada; and Mr. Joseph Hoffman, who is the Director
of Policy for the Ontario Ministry of Consumer & Commercial
Relations.

They will speak today about the Canadian
experience in harmonizing provincial and national laws and
the lessons to be learned from this experience as well as
the potential future for U.S.-Canada efforts at
harmonization.

Gentlemen, thank you coming. I appreciate it.

Thanks for patiently waiting all this time.

MR. BROWN: Thank you, Commissioner.

First of all, let me say on behalf of Joseph and
myself how pleased we are to be invited here to address the
Commission today, and hopefully some of the comments that we
have will certainly help the Commission in the hearings.

Joseph and I are here in our roles as co-chairs of
the Consumer Measures Committee, which is a committee
established under Chapter 8 of the Internal Trade Agreement
which has just been ratified in Canada.

We would like to share with you some of the
lessons we have learned as co-chairs of the process and,
hopefully, some of the those lessons can be applied on the
international level as well.

Much of our experience has been accrued through a
process of formal negotiation among 13 jurisdictions to
eliminate barriers to trade, investment and mobility within
Canada through the agreement. Our particular focus has been
on harmonizing national provincial consumer policies.

If you bear with us for a few slides, we will
provide you with a very brief context for Canada's
experiences in this area. Slide 1, which I won't go into
for the purpose of time, simply outlines the structure of
Canada's internal agreement. And you will notice that the
--- if you are familiar with NAFTA and the GATT --- that the
subject matters are very, very similar to those in those
particular agreements as well.

Under specific rules, you will notice that we do
have a chapter which is titled "Consumer-Related Measures and Standards." And that's a chapter that Joseph and I co-chaired through the negotiation process.

Now, the inclusion of consumer protection in the agreement is especially noteworthy in two respects. The protection of consumers was recognized as one of the few legitimate objectives where the objective of protecting consumers is acknowledged as sufficiently important that it should prevail over trade rules under some circumstances.

The recognition that the effects of different consumer standards can create barriers to trade, internally intentionally or unintentionally, impose unnecessary costs to business as well as consumers, as well as provide consumers in a national marketplace for the confusing and variable degree of rights.

You will notice a similarity or the parallels between the national and international dimension.

The consumer chapter is noteworthy in one more respect: Each sector chapter was negotiated by a separate sectoral group. The sector negotiators for the consumer chapter were all consumer protection officials, few of whom had any previous exposure to trade negotiations. As a result, we enjoyed one of, unfortunately, infrequent occurrences in public policy, really being able to have it both ways.
Because of the consumer rather than the trade perspective shared by the group, we were able to reduce differing laws and standards while trying to use each opportunity to broadly improve the level of consumer protection.

The second slide simply gives you an outline and some of the areas and tasks that we have established under the Consumer-Related Measures Standard chapter. It gives you an overview of the objective and the look undertaken in the consumer chapter. And I just want to point out that this has all taken place within the last 12 months, so it's a fairly tight time frame.

Briefly, we have committed ourselves to action in several specific areas: Harmonization of direct sale and contract and consolation rights, the harmonization of registration requirements, adoption of uniform standards.

So far the most ambitious area in the harmonization of legislation is the governing of cost-of-credit disclosure. This includes fixed consumer credit, open credit, such as credit cards, mortgage of real property, supplier credit such as conditional sales agreements and long-term leases of consumer goods.

I'm happy to report that all of these tasks are proceeding quickly and on target.

The list of the harmonization commitments is not a

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closed one, however. New areas of harmonization may be added. Nor are we confined to harmonizing what already exists. Cooperative actions on new areas of consumer policy can be pursued.

We have also committed ourselves to the exploration of ways to improve cooperative enforcement of consumer measures.

We will also use the opportunity to establish a permanent Inter-government Consumers Measures Committee. This group, of which we are the current co-chairs, has several responsibilities.

We have to monitor the implementation of consumer aspects of the trade agreement.

We are charged with facilitating the process of reconciling consumer standards and identifying new areas for possible future harmonization.

We will act as a forum for intergovernmental discussions on any issues relating to consumer measures and facilitating dispute resolution if and when needed.

I will pass the rest on to Joseph.

MR. HOFFMAN: Thank you, Zane.

Commissioner Starek, I will just briefly, before I pick up where Zane left off, reemphasize what a pleasure it is to be here today.

If we could put up the third slide and our last
What I think we would like to do with the remaining time is talk a little bit about the lessons that we learned through this experience. And I think I should emphasize the lessons as perceived by Zane and I in our capacity as co-chairs, trying to keep somewhat of a broad look at things. And we've narrowed down a list to what we saw as really the six essentials.

The first is recognizing the meaning of harmonization. While a shared vision is, of course, very desirable as a point of departure, however, parties at the very least have to recognize the implications of committing to harmonizing differing standards. It may mean compromising. It may mean doing something differently. And, in fact, in some cases, it may mean doing something less.

The greatest fear we noted at the outset was that harmonization would result in lower levels of consumer protection, that pressure to harmonize would be pressure to harmonize to the lowest common denominator. And we tried, in negotiating the framework of the chapter, to address this at the front end by several means.

The first was explicitly stating in the trade agreement the legitimacy of consumer protection.

The second was recognizing each party's right to
establish consumer standards.

The third was agreeing that, to the greatest extent possible, any reconciliation that occurred under the agreement would be to a high and effective level of consumer protection.

And the fourth -- and I think in our shared view, the most important -- we agreed that no party would be compelled to lower the level of consumer protection that it had in place when the agreement was signed.

In effect, this last point means that we committed ourselves to consensus, that we chose consensus as opposed to a majority as the mode of operation. And I think the results of all of that was a level of comfort established, leveled out the group to focus on the merits of harmonization proposals more objectively.

In the Canadian context, our experience is that differing standards appear to be a far greater concern, both to consumers as well as to industries, than the presence of the high standard.

So far, our experience seems to be working out well. Where some provinces, in the case of the specific harmonization commitments that Zane listed, where some provinces have come down to a particular standard, it's been because the others have come up. And even in cases where the result might be the appearance of a lower standard in a
specific jurisdiction -- and we have 13 jurisdictions
involved in this exercise -- even in cases where the results
appears to be lower, for Canadian consumers, generally, in
every case, the marketplace standard is now higher or will
be at the end of this all.

The second lesson is choosing the right things to
harmonize. We learned that there is not necessarily a link
between the simplicity of a standard and the ease of
harmonization.

Apparently simple and straightforward issues --
what information, for example, should go on a label and
where to put it, picking a dollar threshold for door-to-door
sales -- proved almost more challenging than agreeing to
very complicated credit calculation formulas that would
apply to virtually ever individual consumer and ever
financial institutional nationally.

Connected to this issue of choosing the right
issue is the challenge of finding a balance between fixing
yesterday's consumer standard and focusing on a harmonized
approach to the consumer issues of tomorrow.

We found that, somewhat unfortunately, it is
easier to focus on a standard that may apply to a very
narrow slice of consumer transactions, really because it's
the one that's been regulated for years and the perceived
need for that measure is highly entrenched.
Third lesson, the importance of definitions. And this may seem very obvious to you as we talk about it, but to us it was somewhat of a surprise.

Despite being a group of consumer officials, we found very early on in the process that we really meant different things when we used terms like "consumer standards," "level of protection."

Initially, we discussed definitions almost because we were compelled to legally. We were, after all, negotiating a legal trade agreement. However, there came a point when we discovered how important a shared understanding of language was, not the least of which was because our group encompassed two languages as well as two distinct legal codes.

And we invite you to try it for yourself. Write down your own definition of "economic interests of consumers" and see how it compares with the definition of the person beside you or, in fact, compare it to ours.

The next lesson learned has to do with authoritative participation. Zane talked a little bit about the interesting attributes of the composition of our group in terms of their past experiences as consumer officials as opposed to the few of us who had any trade experience.

On a more practical note, we learned about the difficulties encountered when different members -- and we

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tend to avoid the term "negotiators" -- came to the table with varying authority to make decisions.

And I emphasis that this isn't a problem of gaining political approval. This is a practical negotiating issue right at the table, the challenges faced by some members getting approval from their respective bureaucracies to speak authoritatively.

On the other hand, as a group, we preferred to be informal and not take a fixed view about the level of representation sent by each government. We wanted the most knowledgeable people at the table. We were, generally, unconcerned if some were senior executives, if some were staff lawyers, if some were middle managers or, indeed, middle manager staff.

And I think our experience is that, well, this has been somewhat problematic from time to time in the negotiations, generally speaking, the quality of the discussion, the ability of the group to really focus in on the issues at hand from a consumer protection perspective was -- benefitted from this diversity of members.

But it did cause us some problems.

The next lesson had to do with advanced commitments to outcome. And our experience was that this was conjecture in the beginning. To assure success, the approach we needed was to deal with everything in,
essentially, three stages.

The first, to establish a firm and binding commitment in advance to a specific outcome.

For example, that we would complete negotiations on the element of harmonized cost-of-credit disclosure nationally by a fixed date even before we started debating the details.

The second stage, that we would achieve final political approval and determine the most appropriate step towards concurrent legislative change and other implementation considerations because some things can be done without legislation.

So far this sequencing appears to work; although, we have recognized a possible problem in accommodating some political realities.

Many of our governments are at different points in the political cycle, and that makes legislative scheduling somewhat uncertain. Cabinet ministers change, often very unexpectedly. And this may necessitate revisiting the time tables for briefings, for approvals, getting all of our ministers to a common table to consider and sanction work is seen as extremely important to this process.

Now, we also discovered that as political figures, as political leaders, our department heads' portfolios were really quite varied. All of them had consumer

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responsibilities; but some came to the table as representatives of ministers, responsible for trade or industry. Others had housing in there; some were responsible for recreation; quite a few were, I guess, the equivalent of state attorneys general.

The last point that I'd like to talk about is really the need for a strategic approach to consultation.

Among several lessons learned in this area, we discovered the difficulties and opportunities presented by work that was not seen as being owned by a single government.

The difficulty is really that consultation efforts need to respect the presence of stakeholders at both the national and provincial levels. However, in 11 or 13, if you include the territories, of the jurisdictions, each one of those jurisdictions conducting their own consultation is an awfully difficult and not necessarily source-efficient way of approaching consultation in a harmonic fashion.

On the other hand, we're a committee. We're not a secretariat. We don't have dedicated staff, so we have some limitations on our capacity to consult stakeholders directly. So we've tried, so far, to handle this important issue by taking a number of steps.

First, as part of our negotiating exercise, ensuring that we have developed a single consultation
document for common use in all jurisdictions.

Secondly, ensuring that all stakeholders at all levels are identified at least on some kind of master list so that there is awareness of who is being consulted and where.

The third, and connected with the one I just mentioned, is respecting the right of governments to conduct their own consultation but developing, in effect, some protocols for sharing the results of those findings.

And I'd like to maybe diverge here and point out that the cost-of-credit harmonization negotiations, which Zane mentioned, are extremely complicated.

I think there are really only two provinces that opted to do any of their own provincial-level consultations. Everyone else was very comfortable allowing the co-chairs of the negotiating team, which is a subcommittee of the group that Zane and I co-chair, to, in fact, conduct the consultation and do the kind of dialogue where it was necessary and to synthesize the results and share those amongst all of the parties.

Connected with this, really, was the need for developing common communications materials for use really anywhere in the country and designating the working group chairs as the primary external contacts.

And the last point in this area was providing our
political leaders with some distance from the direct issuers until the final proposals were reached at a working group level and developed for political approval so that we can take forward to ministers, really, the recommendations for a complete harmonization proposal, rather than delegate up, so to speak, disagreements.

And so far, we have been fortunate in that regard. Although, I should add a point that ties in with, perhaps, again the political realities. Many of our ministers, or at least some of our ministers, are conscious of the difficulty that the harmonization exercise presents to legislators.

In effect, as far as the legislators think, there's not much room to add value pushing through a piece of legislation. It's all done for them, in most cases, by a group of non-elected officials and dealing with that dynamic. And I think what we might find as we go forth down this road is the need for some thinking about how to blend a role at the political level into the harmonization exercise so that there is, in fact, some -- not only the appearance but the substantive value added on the political side as well as at the staff level.

And I'll turn it back to Zane at this point.

MR. BROWN: Thanks, Joseph.

One of the key elements in the negotiations that proceeded along with the discussions was the fact that, as
we achieved success on each chunk of the -- whatever we were
tackling -- it seemed to strengthen the relationship in the
parties. It also increased the trust level amongst the
parties. Or it made things easier as we went along.

And it bodes well for the future of the work of
the committee. We will be tackling, probably, stuff like
electronic marketing, some of the issues that we were
talking about today. Certainly some of the fall out, like
the privacy issue, negative option marketing. And one of
the things that we were moving ahead very fast on is
cooperative enforcement amongst the various parties within
Canada.

However, as we also have recognized, these issues
are universal in nature and any resolution should reflect
the international dimensions of today's trading patterns.

I could mention that we have a number of such
initiatives, of course, already well underway. Under
chapter 9 of NAFTA we are involved with textile labeling.
We have certainly commented on the care labeling proposals
put fourth by the FTC. We are also involved with the ISO
subcommittees working on eco-labeling or environmental
labeling.

We are members or participants in the NIST work
being done in terms of methodologies, tolerances, price
verification under weights and measures and so on.
So there is -- there are long-standing working arrangements that are in existence and will continue. 

Now there are several specific interests for further attention. 

Number one is looking at the role of legislatively recognized industry codes to provide greater flexibility in adjusting consumer regulations as the marketplace evolves. 

The second one is exploring opportunities for cross-border cooperation and consumer education in partnership with business and consumer agencies. 

Taking advantage of existing opportunities under chapter 9 of NAFTA to address other consumer protection and future issues. 

Similarly, to expand work on cooperative enforcement to look at opportunities for greater north/south action rather than action confined to state-to-state or province-to-province. 

More frequent, constant, collaboration in consumer policy development to follow up on issues such as those raised in these hearings. 

Establishment of a regular North American forum for consumer agency communication and project work. 

Recently the Canadian Consumers Measures Committee met in Toronto with the executive board of NACA; and this was the first meeting of its kind that brought consumer
agency officials together to compare the respective
priorities and plans and to share information. It was a
very successful meeting, I can add.

We hope that you will be able to benefit from our
experiences. We certainly intend to build on our experience
as we move forward to address other consumer-related
measures and standards in a much more flexible, proactive
manner.

I want to thank, again, the Commission for giving
us this opportunity.

Thank you.

COMMISSIONER STAREK: Well, thank you both for
just a fascinating presentation. I'm absolutely amazed that
you had the strength left to get on the plane and come down
here. If we were ever to undertake such an exercise in the
United States, with our 50-plus jurisdictions, in addition
to the Federal Government, I only could say I hope my term
has expired.

Well, I think it's fascinating. I think you have
laid a foundation for our discussion. And that is: How can
we, or should we, even begin to talk about harmonization of
both our standard-setting procedures on an international
basis and our law enforcement policies?

Should we seek harmonization and standardization?

And, if so, how? And how do we avoid the pitfalls that both
you and Bruce Silverglade have pointed out in this process?

Is the model that you have demonstrated for us
something we should encourage our friends in Europe to use
when they have to work out their problems?

These are things that I hope we can address when
we reconvene, after about a 10-minute break, for a
discussion where we will joined by some other panelists as
well.

So let's take about 10 minutes and come back for
what I think will be a fascinating discussion.

(Whereupon, a brief recess was taken.)

COMMISSIONER STAREK: All right. I think maybe we
can gather around and try to continue with our discussion.

For this part of the program, we are adding three
discussants. The first is Toni Guarino, who is Counsel to
the law firm of Buc, Levitt & Beardsley, who specializes in
food and drug law, advertising law, and consumer product
safety law.

Secondly, another additional panelist is Carl
Priestland, who is the Chief Economist of the American
Apparel Manufacturers Association. Mr. Priestland has been
in this capacity for 20 years and has represented AAMA and
its members at international negotiations on trade for the
past 20 years.

And, finally, Michael Thompson, who is the
Director of Governmental Relations for the Whirlpool Corporation, has joined us. Whirlpool manufactures in 11 countries and markets products under 10 major names in more than 120 countries.

I wonder if any of our new panelists would like to make a brief statement or add something or make a comment on what they heard, because I know you were all here for the first half of this afternoon's session.

Mr. Thompson.

MR. THOMPSON: Thanks, Commissioner Starek. I just wanted to make a few comments about the appliance labeling rule.

When I was asked to come here and speak as a discussant, Elaine asked me to identify areas where, perhaps, the FTC could work more closely with our counterparts in Canada and Mexico to help minimize the burdens and, therefore, the costs of labeling under three different national labels.

So I would like to give you a couple of minutes of a Whirlpool perspective on the appliance energy labeling program that the FTC has.

Whirlpool Corporation, as you indicated, is a global manufacturer of major home appliances. And you gave a pretty good overview of where we're -- you know, we're located in over 120 countries around the world.
In the United States we have 10 plants in 7 states; but we also have manufacturing facilities in Canada and in Mexico. And we manufacture all of the appliances that are currently covered under the FTC's energy guide labeling rules; and they include refrigerators, freezers, clothes washers, dishwashers, and room air conditioners.

When the FTC rule was originally crafted back in the late 70's, I was there at the very tail end of it. When the FTC -- as a commenter on behalf of the Whirlpool Corporation. When the FTC, in all subsequent invitations for comment on amending the rule, asked participants from the public, we also got involved. So we have been deeply involved with the labeling rule ever since its inception.

The purpose of the labeling rule is to, first of all, show what the cost right now is for operating that product on an annual basis. And you're transition this year to a new format that will show KWH per year, kilowatt hours per years, which we heartily applaud.

But the primary reason for the labeling rule is to give consumers choice. I brought a few labels. You're pretty familiar with them, I'm sure. But they do show, you know, the relative cost now. And that will change to show annual energy consumptions with ranges of comparability of the least efficient and most efficient at each end of the bar there.

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In the spirit of NAFTA, we strongly support the harmonization of labeling. Right now there is a lot of problems with that harmonization process.

And the problems are predominantly in the area of formatting. The United States has one format on which the energy descriptors are KWH per year, energy efficiency ratio, and annual operating cost. You know, that's where it is right now.

Mexico shows only KWH per year.

Canada has KWH per year and EER for room air conditioners.

There are different ranges of comparability, in other words, most and least efficient, in every nation.

Mexico does not have its own range of comparability but has some kind of identifier that shows different and more efficient products with A through D ratings.

The language is obviously different, and the format is considerably different.

The major obstacles to harmonization are basically the format itself, which we believe can be overcome. But some past interpretations by both the U.S. and the Canadian Governments with respect to dual labeling -- which is something we would like to do in the absence of a complete harmonization process -- in the past, the FTC has
interpreted certain provisions in the existing law, where we would like to maybe do back-to-back labeling, as being unacceptable because one provision says -- and I'll just kind of read it real quickly: "No marks or identification other than that specified in this part shall appear on or directly adjoining this label except for a part or publication number for indication."

Strictly interpreted, what that means is: You can't even dual label.

Now I know that you're leaning towards that right now. I would encourage more direct contact -- and I'm talking about face-to-face contact between the Federal Trade Commission, Natural Resources Canada, and the folks that are your counterparts in Mexico.

I would encourage a modification of sections that, strictly interpreted, would prohibit us from dual and tri-national labeling right now.

I would encourage, to the extent practical, that everybody within the FTC work with their counterparts to harmonize these labels.

To give you an idea of what some of the benefits are, at a minimum it's hundreds of thousands of dollars to us; but I'm not speaking just to Whirlpool Corporation, because those dollars ultimately translate in dollars that is saved by the consumer.

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We reduce our administrative burdens considerably. It's a 12- to something like 18-step process on just the approval of one of these labels. And if you would multiply that times three for each nation, it gets even more complex. Our printing and labor costs go down considerably if we can harmonize or dual label. SKU, Stock Keeping Units, the label numbers go down considerably. And even the model numbers, the number of model numbers that we produce, go down.

The dollar savings, we believe, can be translated into better, more worthwhile ventures if we had harmonized labeling or at least the ability to do a label through reinvestment and research and development, through improved consumer features investment, investments in our processes in our plants.

And that's one of the reasons why we have been so competitive over the years, as an industry, because we constantly improved our processes. And by doing so, we have maintained our competitive posture with other manufacturers and can bring those benefits to consumers.

So I would strongly encourage the harmonization and, in the interim, that the FTC consider bi-national or tri-national energy guide labeling.

There are a lot of obstacles over and above what I have mentioned to you right now, differing test procedures

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between Mexico and the U.S. that are largely harmonized between the U.S. and Canada.

But, ultimately, I believe that we ought to be able to come to a common energy descriptor that shows KWH per year. That would help. And that can be common to all three countries, with a common test procedure, hopefully, that would be readily identifiable by any consumer in each of those three countries.

COMMISSIONER STAREK: Another challenge raised by NAFTA.

Did any of our other speakers -- yes. Toni.

MS. GUARINO: Thank you, Commissioner Starek and Commissioner Steiger.

It's really good to be here. I appreciate the invitation.

I would actually like to answer the two questions that Commissioner Starek posed just before the break.

He asked: Should the FTC seek harmonization of its policies and law enforcement approaches?

And, if so, how?

And I have, to begin with, just very specific answers.

In answer to the first question, yes, I think harmonization is a good idea.

And very specifically in an ongoing proceeding on Heritage Reporting Corporation
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the leather guides, industry guides on leather products, I would propose that the things that are in the proposed guide out there, that was accepted, that was on the record for comment up until earlier this month, that the approach the Commission is taking to the use of the word "leather," in an unqualified sense, be reconsidered.

And, in fact, that the Commission reconsider the EU standard, which was pointed out in comments submitted by two commenters earlier, dealing with Distributors and Retailers of America and the Leather Industry Association.

The EU standard is a somewhat more expansive one toward use of the word "leather." And it takes into consideration changes that have taken place since the Commission's earlier guides for shoes and footwear were put in place almost -- or really more than 30 years ago.

And I think that it would be an opportunity for the Commission to put its energies into a practical application of what we're here talking about today, which is a very good kind of world view of regulations.

It would also be consistent with the Commission's approach in another ongoing proceeding, the "Made in the USA" proceeding where, again, the new global economy, as the Commission stated in its own proposal, is very important in reconsidering how the Commission will approach the "Made in the USA" terminology.

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So the comment I just made is contained in the formal comments that were filed on the 15th by the footwear Distributors and Retailers of America.

I have a couple of other observations. I was asked to comment briefly on an organization that I'm associated with, the International Bar Association. I serve as a Vice Chairman of one of the committees of the International Bar Association. And I would just briefly mention, I think the Commission is at least formally aware of this organization because there have been Commission representatives at some of its meetings.

I serve as a Vice Chairman of the Products Liability Unfair Competition Advertising and Consumer Affairs Committee of the International Bar Association.

COMMISSIONER STEIGER: In your spare time.

MS. GUARINO: In my spare time, yeah. And that's a very long title. And it's noteworthy that "unfair competition" is part of the title of that committee in the context that Mari Ann and Bill were talking about earlier.

The idea is an interesting organization. It's composed of individual lawyers and bar associations from countries, really, around the world.

And while it does not have as one of its goals "harmonization of legal standards," it is an excellent forum for learning about how other countries are doing things and
potentially affecting some of the approaches.

A couple of years ago, there was a session that
was a session of the committee I'm serving on that dealt
with advertising of environmental claims and claims for food
products and claims for cosmetic products and there were
representatives from a number of European countries as well
as the EU and Australia. And it was just an excellent forum
for hearing about the different laws and standards in those
areas that I know are of importance to the Commission.

And I would just give you a little preview of
another meeting that is coming up in October of next year.
I know that cyberspace issues were part of this hearing
earlier in the week, and my committee is actually planning
to co-sponsor a session in Berlin -- I'll be in Berlin in
October of next year -- that will deal with what is called
"consumer transactions in cyberspace," including an analysis
of the position of consumers and their protection, including
data protection and distant selling regulations, as well as
credit issues.

So that session, I think, is pretty well
established; and I would be happy to keep you all informed
on that and other dealings with the International Bar
Association.

It's just one more forum of the many that have
been suggested for the Commission to spend its resources on,
but it is a good association and some opportunities for
getting views expressed, if no tangible results can be
really be measured.

Beyond that, if I could just take a minute to
respond to a couple of comments that were made earlier by
the other speakers.

First of all, these are just in the nature of
observations. I was very much involved in the development
of the regulations to put the Nutrition Labeling and
Education Act into practice at the FDA. And when the new
regulations finally came out in, I believe, early 1993, I
participated in some seminars for Canadians up in -- I think
we did a session in Toronto, as well as a session in
Brussels. And the purpose was to explain to the Canadians
and to Europeans what these new regulations would do and
what restrictions would be imposed on food manufacturers
sending product into the U.S.

And I can tell you that the initial reaction was
disbelief.

Now, could FDA have done more to consider
international implication of those regulations? Probably
not a whole lot because of the underlying legislation. But
it's good to know that the Commission is taking more of a
world view than perhaps the U.S. Congress did back then.

But it was a rather astounding reaction that we
got and that, you know, maybe nothing could have been done,
but it is good to hear that, at least going forward, there
is more of a global consideration that's being given to the
development of new regulations.

COMMISSIONER STAREK: Yes, that was the experience
that I had in the OECD, the same thing. I mean, people
would say: Aren't you the deregulatory nation? This is the
most regulatory thing -- this was much more regulatory than
European or other schemes.

MS. GUARINO: And no consideration really given to
the international implications or the harmonization aspects
of it.

Again, that was kind of -- you know, in a sense,
it was a function of the statute.

MR. SILVERGLADE: I'd add that other countries,
ranging from Singapore to Israel now, are moving in our
direction. And this reaffirms the point that I was trying
to make, which you may want to refer, that this is the way
for the U.S. to maintain leadership and maintain our
position and maintain our standard of living and share it
with the rest of the world.

MS. GUARINO: In this case without consultation in
advance, but, nonetheless -- I mean, that was really just in
the nature of an observation.

But beyond that, on symbology, again, just as an
example, when the USDA Safe Handling regulations were coming out a couple of years ago, there was an interesting experience. One of the initially proposed symbols was, I believe, a cake of soap, which was -- there are symbols, as you may know from looking at your meat packages, associated with this Safe Handling regulations for meat and poultry.

And I think one of the initially proposed symbols was a cake of soap which was supposed to tell people: You're supposed to wash your hands before you -- or rather, after you handle meat.

And somebody observed that that may communicate to people that they were supposed to wash their meat with a cake of soap. So the final symbol came out with, I think, soapy hands or something like that.

But thank you for the opportunity to comment.

COMMISSIONER STAREK: Carl, did you want to offer any initial comments?

MR. PRIESTLAND: I would like to make one comment.

In the area of labeling, the U.S. was the only country of the three that did not have the ability to use the care symbol system. So we are very pleased now that the Commission has decided to, at least, look at this more specifically.

And with that, the possibility of harmonizing a care symbol system within NAFTA has increased considerably.
And also, because of the international structure, we think that that would be quite useful to all of the members of the U.S. and Canada and Mexico in terms of international trade of apparel and textiles.

So we are quite pleased that the care symbol system is getting a significant look at. And, hopefully, the Commission, when it finishes, will take care of the -- make the care symbol system part of the requirements or at least opportunity to use the care symbol system rather than written material.

I think this is very important to the whole community in terms of the retailers and the apparel manufacturers. And it's something that I think we need. And this is the best forum to start looking at things like that.

Thank you.

COMMISSIONER STAREK: Thank you.

Let me suggest this, since we've talked so much about the OECD, why don't we use one of their procedures, which is, if you would like to say something, take that little sign in front of you and stand it up like this; and then we'll know who wants to talk, and we can try to keep track and keep it in order.

Commissioner Steiger, I believe, has a question?

COMMISSIONER STEIGER: I would be interested in
whether any of you think that there are particular problems 
that are posed by some industries. 

One that comes to mind is the great variety it 
seems to me of treatment of marketing of pharmaceuticals. 

We are in an era here where you are seeing a lot 
of transference from formerly prescription medications into 
the over-the-counter market where consumers now have wider 
range of purchase options. 

But it seems to me that standards vary greatly as 
to, number one, what is and is not a prescription medication 
abroad? And as to what, if anything, can be said about a 
pharmaceutical product. 

Has this posed any particular interest for any of 
you? 

And are there similar industries where there might 
be such a variety of the current practice in marketing that 
it could create barriers?

Mari Ann. 

MS. BLATCH: I agree with you about the differing 
regulations on pharmaceuticals; and it's too bad there's not 
someone here from Pfizer because I know they chair all the 
international committees. 

But I would say, from the point of view of Readers 
Digest, when we are selling a page of advertising to a 
pharmaceutical company, we can never sell a global page.
We're always selling magazine by magazine because each country, they have to set the new page for the particular requirements; and the product will be considered an over-the-counter in one country and a pharmaceutical in another. It wouldn't even be allowed to be advertised in one if it's considered pharmaceutical.

And then the question of what other recommendations -- you know, what contraindications -- you know, in some places we sell an extra page, which we like; but our readers don't really like to see that extra page of print, to be honest.

And there's also -- my favorite topic, sales promotion. In the EU analysis of sales promotion, they point out that in many countries the pharmacist on the corner, the little pharmacies, are afraid that there should be no advertising and there should be no free gifts or free samples or anything like that.

And so in a lot of places in Europe, the small pharmacy, for unfair competition reasons, is extremely limited to what can be done.

COMMISSIONER STEIGER: Would the same single-page-per country apply to the example that we heard, for example, of an appliance that might have energy standards?

Do you run into that as well if Readers Digest has
someone wanting to advertise a washing machine, a dryer?

Do you find that there is this problem of how you can label or format in an ad, globally, what the energy requirements, for example, are?

MS. BLATCH: Well, in fact, what happens is that the advertiser and the advertising agencies have huge legal staffs that keep track of all that sort of thing; and then they come to you us, and in our case, because we have separate magazines, we can accommodate them and make sure that they abide.

If they're trying to buy into say Economist or Time Europe, there's greater difficulty because there's just one magazine going into several markets.

COMMISSIONER STEIGER: Thank you, Mari Ann.

COMMISSIONER STAREK: I think Bill wanted to comment on that, Commissioner.

MR. MacLEOD: Just a short comment on Commissioner Steiger's question. And that is the advertising regulations for prescription drugs are a perfect example where consumer protection has been the enemy of consumers. The regulations that the FDA imposes here are regulations that make it virtually impossible to advertise because one must buy almost an entire extra page of a publication like Readers Digest.

What's unfortunate is that those are the most
enlightened regulations in the world right now because in most places you can't advertise prescription drugs at all. Fortunately, the FDA is currently reconsidering its direct-to-consumer advertising policies. And the indications are is that they are going to be substantially revised. And there is a perfect example of where the United States could exert some leadership, because we can find, I am sure, many examples that are far more dramatic than those that were demonstrated in the cereal industry of therapies that can save lives that are disseminated far more rapidly throughout the economy as a result of the information being made available to the consumers.

COMMISSIONER STAREK: Thank you.

I think, Michael, you were next.

MR. THOMPSON: Thanks.

Commissioner Steiger, I'll just answer on the front end. We have not experienced a lot of problems in the appliance industry with respect to advertising energy. That area is fairly strictly regulated in a sense already by yourself as far as what we can say in the consumer catalogs, the literature that goes out to our retail dealers and our distributors.

I don't want to have a disparaging comment here about the guide itself, because we do support it, but we found in all of our surveys of consumers over a many-year
period, that energy isn't one of your primary sellers. They don't come in as consumers and ask: Give me the most efficient refrigerator you can find. It would be nice sometimes because we have some of the more efficient products out there. But it's usually fifth to eighth on the list before it ever come up.

COMMISSIONER STEIGER: Interesting.

COMMISSIONER STAREK: Thank you.

Toni?

MS. GUARINO: Just picking up, again, Commissioner Steiger's question, the International Bar Association meeting from two years ago that really focused on advertising for food products and environmental claims and things like that, really demonstrated the disparity and the need for not only changing the language in different public -- you know, in different countries where an ad was to be run but accommodating different legal requirements.

And there were representatives from individual companies as well as ad agencies demonstrating how they changed, for example, on television commercials some of the approach while trying to preserve as much of the visuals as possible.

Of course, you know, you always do have to deal with the language. So presuming that you're going to be putting your ad in the local language, you do have to make
that change. So I don't want to minimize the problem; but, of course, there are expensive legal staffs in the companies and agencies, which does add to the cost to consider not only the translation but the differing legal requirements.

On the prescription drug advertising, Bill's point was a very good one. And the FDA recently had public hearings on the possibility of, you know, whether or not it should change its currently very restrictive approach.

At that hearing, there was somebody from, I think it was Health Canada who testified about the Canada approach, which is just a total prohibition.

So even if we do change our current approach, there are still a lot of barriers in that area, and I imagine they will continue.

Although, there is some glimmer in terms of drug approval, I know there is a little bit of an increased willingness here in this country to accept studies that have been really done in other countries as part of the drug approval process here. So I think there's maybe a little bit of an opening up of a recognition that there is value in other systems as well as our own.

The CODEX value process, which was spoken about, is an effort certainly at harmonization on a lot of issues in the food area, but it is moving at a glacial pace and I think has been going on for decades would be not on
exaggeration. So it's just going to be very tough and very
lengthy, I think, for all of these products.

MR. SILVERGLADE: Two points. On the role of
CODEX, CODEX was originally was conceived to be an
international standard setting organization that could
benefit less developed countries who could not develop their
own food safety standards, for example, so that they
couldn't engage in international trade because their
products weren't up to par. And it was there to set a
lowest common -- a minimal standard for countries across the
globe.

But more recently it's being looked to as a
harmonization effort. And those two goals are not the same.
And CODEX may have to take on a new form to really live up
to harmonization and not just reduce the whole world's
standards to the lowest common denominator.

We are not here to discuss prescription drug
advertising, but I just wanted --

COMMISSIONER STEIGER: Can I just interrupt before
you go onto your second point?

How is the CODEX interacting or reacting with the
efforts by the EU to set standards or norms?

Is there a constant interaction there? Or don't
you know?

MR. SILVERGLADE: Well, the EU has a
representative on CODEX and speaks, you know, for the
European Union. And it depends on each issue, whether we're
talking about health claims or defining the term "natural"
or should a radiation be labeled and the positions somewhat
differ, depending on each situation.

COMMISSIONER STEIGER: Excuse me. And I
interrupted your second point.

MR. SILVERGLADE: Oh, no. That's okay. I needed
a little break there.

No, I just wanted to make a comment on
prescription drug advertising. CS is not directly involved
with that. But I think this is, again, something that the
FDA is going to have to move very slowly on. And the
consumer marketplace experience -- the actually experience
of the consumer in the marketplace may not match the
economic theories.

We've heard about the potential benefits of
prescription drug advertising. And I would urge everyone
just to talk to any friends or relatives, neighbors who have
gone to see their doctor because they saw an advertisement
for prescription drug and just anecdotally monitor what the
response of their physician was.

Usually the doctor will tell you, you don't have
any idea related to what this drug can do; and it's not
appropriate for you.
COMMISSIONER STAREK: Thank you.

Professor?

MR. SPIVAK: Thank you, Commissioners.

May I change the subject to more general comments, if we've discussed this sufficiently?

I'd like to summarize some of the discussion from my own personal perspective, if I may, this afternoon in a series of six or seven short thoughts.

One, simply a word of caution: I would like to say that we should not, in these hearings and on the public record, sound so jingoistic as to assume that the United States always has the best, the strongest, the most protective, the most innovative standards and regulations.

Although, I am equally proud of what it is we do and what the Commission has done with the U.S. regulations and the private sector standards, one can find numerous examples that the Commission can learn from and, indeed, does, from our partners in Canada and from other nations around the world that are superbly well done.

COMMISSIONER STAREK: Like the Scandinavians, for example.

MR. SPIVAK: Pardon me?

COMMISSIONER STAREK: Like the Scandinavians, for example.

MR. SPIVAK: That's correct. And there are many
regulators around the world, as you well know, from OECD who
don't understand the development of voluntary or
alternatives to regulations. And don't think our
regulations are high enough by comparison with some of
theirs in Scandinavia.

An equivalent example, number two, where I ended
my formal remarks, service area standardization.

The Commission can learn, as I hope you will, and
can contribute to the work of not only in international but
peer work with other national standardizers where I gave
some examples of service industry standards -- some of which
are voluntary, some of which may be adopted into mandatory
regulation -- that can be superb examples of the Commission
regulating and protecting consumers in service industries,
as I know you have considerable interests.

And many of those premier examples of service
industry standardization, pioneering work is going on not
only in the U.S. but with our the partners in Canada and in
France and in German and in Australia and others.

Item Number 3, the Commissioner's comment, which I
understand, but again, allow me a word of caution about -- I
disagree with the general statement or the off-term warning
that international standards are, or may be, lowest common
denominator standards.

Let me give you one example of an ISO standard

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that I am sure most of you are familiar with, the ISO 9,000 series of international quality management standards.

The most recent Mobil worldwide survey now shows over 95,000 will probably -- the world will quickly be over 100,000 plant sites or corporate certifications of quality management systems in compliance with third-party auditing of corporate quality management systems. And that's in compliance with the ISO 9,000 series.

Following on, it will be interesting to see what the ISO 14,000 series of environmental management systems that will be coming with an independent auditing system. The system is already operating in the United Kingdom under British standard 7750.

It is coming in the United States. And it will be interesting to see whether we can develop internationally harmonized labels for environmentally friendly or recycling aspects as the Commission has had been active, and others, and whether we can do that internationally.

Certainly the ISO is making every effort, and the U.S. is playing a key role.

In summary, the larger message for the Federal Trade Commission is that, no doubt -- and I commend you for having these hearings. We are in a global world. These are global markets not only for consumers but, as we have also heard, global markets for business and industry.
The Federal Trade Commission needs to represent
the best of your regulations, our regulations, in the
regional and global markets. And in a time of restricted
budgets and very little travel money and downsizing of some
of the government, that's the real challenge; and that's the
challenge for the Commissioners to deal with with your
staffs.

The possibility of providing some of this
international exchange on the Internet, in cyberspace, as we
have heard, amongst peer regulators in the U.S. and its
counterpart countries can be very helpful if that can allow
the interchange.

What the Federal Trade Commission, in my opinion,
should do with some of this global discussion is, as I
believe you are doing, maintain a broad, wide vision, pick
and choose amongst the best of what we can do and you are
doing not only in the United States, but pick and choose,
steal, plagiarize, adopt, where appropriate, other nations' national standards, international standards if appropriate,
and certainly international standards of the ISO and others
where they can help to provide a larger basis of appropriate
action and development by the Federal Trade Commission in
protection of U.S. consumers.

So my final comment is the thought that this is a
time of world markets. We all need to have that global

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vision. I hope that I am reflecting that as a part of the panel. And that the Federal Trade Commission, which I commend, is looking in the larger vein to maximize your efforts and protection nationally by also thinking globally and internationally.

COMMISSIONER STAREK: Thank you, Professor.

I think we have Bruce and then Michael.

MR. SILVERGLADE: Yes. I just want to clarify my remarks to say that I concur completely with Professor Spivak that, at times, other countries do have stronger consumer protection, environmental protection, occupational safety and health rules.

In Japan, for example, in a room this size, there would not only be an exit sign --a fire safety rule requiring an exit sign at the door, there would be one in the floor that would be lighted with an arrow pointing towards the door so in case the room filled with smoke and you couldn't see the exit sign at the top of the doorway, you could look on the floor and it would point you to the direction out.

The tone of my previous remarks I think is due to the fact, however, that all controversy in the United States seem to be pressing for lower standards.

You know, no one's ever clamoring -- I don't know any American trade associations that's clamoring for a
higher standard.

And so the tone of my remarks comes from my personal experience day to day in my office because the controversies that come before me on my desk are, you know, some association wants us to have as weak a pesticide standard as they have as somewhere else in the world.

So that is, unfortunately, the cause for the tone of my previous remarks.

Thank you.

COMMISSIONER STAREK: Michael.

MR. THOMPSON: Yes. With you your indulgence, I'd just like to show, in 30 seconds, a reason why I also agree with the professor regarding why we don't necessarily have a market on the best standards -- or in this case, the best label.

Our preference would be for simpler. That's the Canadian guide. And it isn't just in deference to our good friends here today.

Our experience has been that consumers can respond to something that's very simple to understand. It's very generic and it doesn't get real complicated.

We have cost grades currently in our labels. Again, we're graduating to different types of energy descriptors in the new label, which is an improvement over what we have.
But ideally, with a common denominator and a common energy descriptor, more along the lines of what the Canadians have, I think we’re better off than trying to build complexity into the labels that we have. Because confusion does result.

I'll give you one example of why we advocate this. Over the years, we have experienced a lot of -- I won't say it's a lot. But we have experienced consumer complaints with the annual operating costs being depicted on the label simply because we change those labels about every two years or so in response to the changes from the DOE's changes in annual unit energy cost for electricity and natural gas and the other common energy sources that we use to plug into equation.

We've had cases where consumers have brought our dealers and our distributors to the Federal Trade Commission for unfair advertising, buying one product, you'd save $51 a year; and then getting, in delivery, something that shows $65 or $70 dollars a year. It's the same model, and the only difference was the changes in the annual unit energy costs that we use in the equation to calculate annual energy costs.

So, in this case, I would take a hard look at it, if you would, sir.

COMMISSIONER STEIGER: Michael, uses less energy
than, what? More energy than? I can't see from here.

What was -- can we presume a common comparison base there?

MR. THOMPSON: Well, what I wanted to show you was ideally, in this label, you would have, say, 600 kilowatt hours per year in this box. And then there would be an arrow pointing somewhere along this bar to where that product fits in the same model and product classification with all the other competing models out there.

So maybe the most efficient would be on this end, uses least energy consumption; and the least efficient would be --

COMMISSIONER STEIGER: But we would have some numerical standard there as a reference?

MR. THOMPSON: Yes, we would. And it would reflect it in terms of annual energy use.

COMMISSIONER STAREK: Thank you.

I think Bill was next.

MR. MacLEOD: I wanted to respond to a point that Bruce made because I didn't want him to leave with the missimpression that the only complaints are about standards that are too high.

As a matter of fact, I mentioned one that I am hearing a great deal of people complaining about right now that are too low. And those are some of the eco seal
standards that are beginning to originate in Europe.

Right now, Canadian diaper manufactures have to
cut down more trees and deliver more wood to their plants in
order to add wood pulp to their diapers so they conform with
the Swedish eco seals for disposable diapers in Sweden.

That is not a deception-based standard.

One thing that we have to remember about standards
-- and this agency constantly reminds us of that fact -- is
that they cannot only be informative of consumers, but they
can also be anti-competitive, exercises by competitors
against one another.

That has happened a number of times. And it
wouldn't surprise me again, if you begin to depart from
deception-based standard, what you're more likely to find
behind it are a group of competitors and not folks who are
looking out for the interests of consumers.

COMMISSIONER STAREK: We have had that experience
here. And I suspect you did when you were directing the
Bureau of Consumer Protection.

I think Joseph was next.

MR. HOFFMAN: This is, to some extent, a reaction
to various comments that have been made so far.

It strikes me, listening to the discussion, and
just picking up on the comments that people who have heard
the discussion and the presentations over the last four days
that, at root here, is a question for the FTC of choice: What really can you afford with limited resources to engage in? And what can you afford to go buy? And, as a regulator, I have some sympathy for having to make that choice. And I don't want to overstate this as an example; but I thought the recent slide that was up there on the energy rating, which was a Canadian label, is a good case study. I think the evidence is pretty clear that it doesn't rank very high in terms of what consumers' choices are based on.

And, somehow, the challenge for the FTC is, perhaps, to figure out: What is the methodology that you use that helps you kind of measure the confluence of consumer priority with industry needs? And use that to guide you in making the decisions about where you invest, as a regulator, your energy or where you step back and say that there is, you know, sufficient evidence that industry itself can handle development of some kind of standard in this fashion, that our involvement needn't be more than the kind of passive observation.

And I'm not trying to suggest that energy ratings for appliance isn't an appropriate issue. But I think we've learned in our experience that these are incredibly costly exercises. Costly not so much in terms of the direct,
know, bottom line budget costs but costly in terms of time, costly in terms of the devotion of resources, and that it's very easy to use up an awful lot of energy harmonizing something that provides relatively little value-added to the consumer and being distracted, essentially, from identify what has the most value-added contribution that can be made to consumers that could be arrived at through a process of harmonization.

COMMISSIONER STEIGER: Can you give us any example where your think that your thinking and that of other Canadian consumer experts has evolved? Is there an area where you had extensive disclosures, say 10 to 15 years ago, or an area that had, perhaps, substantial regulation where you would now say: We have learned that we can do with less?

MR. HOFFMAN: I think it's a question not so much of concluding doing with less. But partly doing with less, partly doing very differently.

I think some examples have to do with direct selling, which is a good example. Direct selling. Door-to-sales is probably high on the kind of list -- everyone's list of regulations, at least at a state and province level, I don't know, but nationally and in the United States.

And I think if we look now at when those statutes
were developed and the investment that still is made in terms of registering people who are involved in sales, et cetera, et cetera, managing complaints, setting the thresholds for recision rights, that really direct selling, in the traditional sense of the word, occupies such a narrow slice of consumer transactions that it's questionable that it's still a valid investment of consumer agency's time, relative to some other priorities.

We talked earlier a little about bit about some of the efforts in Canada around harmonizing upholstery and stuffed article labeling and registration.

What's very interesting is we have a commitment to harmonize in that area -- in fact, it's only 4 jurisdictions out of 13 -- 3 jurisdictions. There were 4 jurisdictions out of 13 that concluded that as a matter of public policy, this was sufficiently important to deal with. And over the course of the negotiations, it became 3 jurisdictions because one of them concluded that their preferred to approach to harmonization was to just simply not legislate in this area any more because they had other priorities that they wanted to pursue from consumer protection point of view.

And although it's very easy to characterize this as a movement towards, you know, low standards or of somehow a gutting of concern for consumer policy, I think that if
you examine it carefully, it reflects a choice in terms of where governments want to be responsive to consumer policy, not necessarily an abandonment or an eschewing of the validity of consumer protection.

COMMISSIONER STEIGER: Thank you, very much.

COMMISSIONER STAREK: Any other comments?

Yes?

MR. MEIER: I just have a brief observation.

First of all, I agree with -- I always hesitate to say "all" -- but it might be all of Dr. Spivak's comments, since I didn't write them "all" down. He made some very good observations.

I just want to throw in one other point of view on this question of whether U.S. interests are looking for higher or lower standards aboard.

Certainly in my anecdotal experience, the thing that they seem to want most is identical standards, that frequently they are concerned when they see another country is doing something that's different. And they say, somewhat logically to them: Well, it's good enough for us and it works perfectly fine and it meets all the U.S. regulations. Why don't they accept it over there? And, particularly if "over there" is a lesser developed country, they say: It's got to be good enough for them.

And we have to explain, well, every country sets
its own regulations and standards.

So I would just make that observation.

So the corollary to that is change -- you know,

they say, well, last week we could get our product in

Country X against this set of standards; and this week or

this year, they have changed their standards; can't we do

something about that?

And, obviously, we can't on case-by-case basis.

And that's where the international cooperation development

of international standards comes into play.

I would also just observe that I note with some

interest that a great deal of the conversation and

discussion here today has been about labeling issues, and I

think they are very important. But they are, perhaps, the

most troublesome in our -- in the trade policy field.

Because our trade policy instruments don't really deal very

effectively with labeling. And I certainly take great pains

to move those labeling problems off my desk as fast as

possible, and they are very difficult.

And I certainly commend some of the efforts that

have been made by Mr. Priestland, for example, on trying to

address labeling issues, whereas, I noted in my remarks we

do have a little bit more of a mechanism to deal with some

of the more difficult issues.

Thank you.

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COMMISSIONER STAREK: Elaine?

MS. KOLISH: I sort of have a follow-up question for you.

There have been a lot of recommendations that we should harmonize more. And my question goes to process and that under the NAFTA model there was a tri-lateral committee set up, initially, in industry and government one and then a formal one set up under the agreement.

Should that be the process for all of our harmonization efforts? Or are there other models that we could use, such as the Canadian model where the, you know, the actual consumer regulators at each level got involved and hammered out the details?

What should our role be vis-a-vis your office?

MR. MEIER: Well, in fact, my office does not necessarily promulgate harmonization efforts. We are somewhat, you know, neutral on that except to the extent where we see that it addresses problems that have been brought to our attention.

I think NAFTA was somewhat the exception there because, one, it is a smaller group of countries; and, two, over the years, there have been a great deal of harmonization efforts between the United States and Canada; and I guess the third point is, there was a lot of industry involvement in harmonization and they brought those
suggestions to bear during the negotiating process.

Nonetheless, as we have heard from a couple of people on the panel, it's not a fast moving locomotive. So it's very difficult.

So I think it has to be done on a case-by-case basis, both in terms of countries involved and product sectors. And we would, as a general rule, look to international organizations as being the primary movers of that process.

I think that's the most efficient -- it's not the only way to go, but that's certainly, we think, the most efficient way to go.

COMMISSIONER STAREK: Well, thank you very much. This has been most fascinating and I think a fitting way to conclude our four very extensive days on consumer protection in the global marketplace.

I thank you all for coming and participating. It's been quite helpful, to me anyway, and I'm sure to my colleagues.

(Whereupon, at 5:30 p.m., the hearing was recessed.)

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I HEREBY CERTIFY that the transcript contained herein is a full and accurate transcript of the notes taken by me at the hearing on the above cause before the FEDERAL TRADE COMMISSION to the best of my knowledge and belief.

DATED: November 21, 1995

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