STATEMENT

OF THE

FEDERAL TRADE COMMISSION

BEFORE THE

CONSUMER SUBCOMMITTEE

COMMITTEE ON COMMERCE, SCIENCE

AND TRANSPORTATION

U.S. SENATE

MAY 2, 1990

Mr. Chairman and members of the Subcommittee: I am Janet Steiger, Chairman of the Federal Trade Commission. I appreciate this opportunity to appear before you today on behalf of the Commission to discuss our views on S. 2494 and S. 1441, introduced by Senators Bryan and McCain, respectively.[1]

These bills are aimed at combatting telemarketing fraud, a matter of serious concern to consumers and the Commission. It is estimated that consumers may lose over a billion dollars a year to telemarketing scam artists.[2] Recognizing this threat, the Commission has greatly increased its enforcement efforts in this area. In recent years, the Commission has brought over 50 telemarketing fraud cases in federal court, obtaining injunctions against companies having aggregate sales of over 766 million dollars.

Before addressing the bills, I should first mention two important areas of emphasis in our telemarketing fraud program.

First, we are increasing our efforts to attack the root of fraud, such as suppliers and other aiders-and-abettors. One problem in attacking only boilerrooms is their fly-by-night

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[1] Except as noted, the views expressed in this statement represent the views of the Commission. Commissioner Strenio does not agree with all of the discussion concerning the state enforcement provisions and will forward his views in a separate statement. My oral presentation and responses to questions are my own and do not necessarily reflect the views of the Commission or any individual Commissioner.

[2] This figure is based on industry information acquired by FTC staff developing telemarketing fraud cases. This figure is also consistent with estimates of other industry observers and law enforcement agencies. We recognize that by some estimates, the figure may even be higher.

nature. At times, boilerrooms will pull up roots and destroy documents upon suspecting detection, only to reappear elsewhere under other names. Recognizing this, the Commission, in the investment fraud area especially, already has brought cases not only against boilerrooms, but also against suppliers of rare coins and fake art, promoters of gold mining schemes, and other entities centrally positioned in fraudulent schemes. More can b done, however. In many types of fraud, there are companies that profit from providing knowing assistance to fraudulent boilerrooms in the form of financial assistance and guarantees, references, products for sale, and other critical items and services. If such firms know they may be held responsible for their own participation in the fraud, they undoubtedly will give more care to the decision whether, and on what terms, to deal with fraudulent telemarketers. Our goal is to create a situatio where unlawful boilerrooms have difficulty getting started because previously insulated businesses are unwilling to deal with them.

Another area of emphasis for the Commission in enforcing telemarketing fraud is increased cooperation with the states. The Commission fully supports the objectives of S. 1441 and S. 2494 to bring greater state resources to bear on the problem. We have enjoyed a close working relationship with the states on a host of fraud investigations and cases, routinely sharing information, referring cases to one another, and, in some cases, bringing suits in tandem. The Commission has further encouraged

federal-state cooperation through the establishment of a fraud data bank. We applaud the states for their efforts in this area.

We should mention one important aspect of state involvement, however. Federal and state resources are limited, and it is important that these resources be concentrated in the most effective manner. In this connection, it is critical that these legislative initiatives not have the unintended effect of drawing resources away from criminal enforcement by the states. Much telemarketing fraud is criminal activity offering huge profits to the perpetrators. Civil law enforcement actions can substantially hinder the activities of scam operators, but it is criminal prosecution that they fear most. Increased criminal enforcement by the states is indispensable to the war on telemarketing fraud.

The Commission already has submitted extensive written comments on S. 1441 to Senator McCain, by way of our letter of March 16, 1990. We have attached these comments on S. 1441 to this statement for inclusion in the hearing record. For clarity's sake and to avoid repetition, the text below will focus principally on S. 2494, comparing its provisions to those of S. 1441 as necessary.

Telemarketing Rule

Section 3 of S. 2494 requires the Commission to promulgate a telemarketing rule and to consider imposing requirements such as

refunds for delayed shipment of goods and a cooling-off period. There are similar provisions in S. 1441.[3]

As we stated in our comments on S. 1441, we question whether these provisions are likely to provide significant benefits to consumers who have been victimized by telemarketing scams. First, the Commission already is addressing the broader question of whether the protections of the Mail Order Rule should be extended to telephone sales. On November 28, 1989, the Commission published a Notice of Proposed Rulemaking to consider whether such an amendment of the Rule is desirable. 54 Fed. Reg 49,060 et seq. (November 28, 1989). Public hearings on the rulemaking have been held and the record remains open until June 4 for receipt of rebuttal comments by rulemaking participants. We believe that this rulemaking will provide the most comprehensive basis on which to decide whether the benefits of extending the delayed-delivery requirements of the Mail Order Rule to telephone sales would outweigh the costs. This may be a matter best left to normal Commission review and rulemaking processes.

More fundamentally, such extensions of the Mail Order Rule relate more to problems encountered in routine business transactions than to the target of both bills -- hard-core fraud. The typical telemarketing fraud does not involve delayed shipment. Rather, the heart of the fraud is deception regarding

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[3] S. 1441 requires the Commission to amend its Mail Order Rule, 16 C.F.R. 435 (1987), to cover telephone sales and to consider a cooling-off requirement.

the nature, value, quality, or cost of the products or services sold. It is this deception that has cost consumers billions of dollars over the years. Similarly, the cooling-off provision contemplated in § 4(a)(2) of S. 2494 would not affect the vast majority of fraudulent telemarketing transactions, because the consumer typically is unaware that he or she has been defrauded until long after the initial transaction.

S. 2494, in contrast to S. 1441, further requires the Commission to consider restrictions on the time of day that telemarketers can make unsolicited calls to consumers, as well as prohibitions on the use of computer equipment that does not permit consumers to immediately terminate calls. We recognize that harassing, abusive, and late night telephone calls are legitimate concerns. However, in our experience it has been the substance of the sales pitch and the resulting sale of overvalued goods and services that has caused significant consumer injury in telemarketing fraud cases. Scarce law enforcement resources should remain targeted at the core of the fraud.

The above notwithstanding, we appreciate the explicit authorization to conduct whatever telemarketing rule as may be required pursuant to the notice-and-comment provisions of 5 U.S.C. § 553. It would be difficult, if not impossible, to conduct the contemplated rulemaking within the 180-day deadline under the more complex procedures of The Magnuson-Moss Warranty - Federal Trade Commission Improvement Act, 15 U.S.C. § 2301. We urge one addition to S. 2494, however -- explicit authorization

for the Commission to seek civil penalties for violation of this section 553 rule. Currently, the Commission only has the authority to seek civil penalties for violations of rules regulating unfair or deceptive acts or practices that are promulgated under the authority of the FTC Act. The foregoing amendment would make clear that the Commission could seek civil penalties for violations of the rule contemplated in S. 2494, even though the bill, rather than the FTC Act, would have been the impetus for number of the rule's provisions.[4]

The State Enforcement Provision in S. 2494

Section 4 of S. 2494 would permit state attorneys general to bring a civil action in federal district court (1) to enforce compliance with the new Commission telemarketing rule and orders obtained thereunder,[5] and (2) to bring actions on behalf of their residents with respect to a new federal cause of action for "fraudulent act[s] or practice[s]."

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[4] An example is the language in the "Petroleum Marketing Practices Act," 15 U.S.C. § 2801 et seq. The Act required, inter alia, that the Commission promulgate the Octane Labeling Rule under the notice-and-comment procedures of 5 U.S.C. § 553. The Act went on to say that "[f]or purposes of the Federal Trade Commission Act (including any remedy or penalty applicable to any violation thereof) such a violation shall be treated as a violation of a rule under such Act respecting unfair or deceptive acts or practices . . .."

[5] Specifically, § 4(a)(1) provides for state actions with respect to telemarketing "which is a fraudulent act or practice or which violates any rule, regulation, or order of the Commission under this Act." "This Act" presumably refers to S. 2494, rather than the FTC Act.

From the Commission's standpoint, S. 2494 contains laudable improvements over other bills that have provided for direct state enforcement of broader causes of action incorporated in the FTC Act. In previous testimony on such bills, we had expressed our concern that direct state enforcement of broad causes of action incorporated in the FTC Act could result in inconsistent application of the Act nationwide. As the number of agencies enforcing the Act increases, so too does the potential for inconsistent enforcement and court decisions. In choosing cases and strategies, the Commission is in the best position to take into account the effect of precedent on issues affecting its other programs.

S. 2494, however, appears to provide for state enforcement only with respect to the proposed telemarketing rule and orders obtained thereunder. Assuming that the practices covered by the rule can be defined with specificity,[6] there should not be a significant problem of inconsistent enforcement of the FTC Act. Moreover, it appears that the broader "fraudulent act or practice" cause of action in S. 2494 is not intended to be incorporated in FTC Act doctrine.

We also note that S. 2494 only authorizes states to bring damages suits and other actions "on behalf of their residents."

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[6] As noted above, however, the specific prohibitions now contemplated for inclusion in the rule (e.g., cooling-off periods), are unlikely to significantly affect hard-core fraud. It may be that further rule provisions that more directly attack the problem would be difficult to define with specificity, raising some problems of inconsistent enforcement.

This parens patriae scheme should pose less chance of being challenged in court as unconstitutional under the Appointments Clause than statutes authorizing states to enforce broad federal rights in the same manner as the Commission. The Department of Justice, commenting on other bills, had opined that such provisions are unconstitutional, involving the exercise of "significant authority pursuant to the laws of the United States by persons not selected in accordance with the Appointments Clause (quoting Buckley v. Valeo, 424 U.S. 1 (1975)).[7]

In any event, further definition of "fraudulent act or practice" may improve the bill. That term, not defined in S. 2494, also has not been defined in consistent fashion in federal and state criminal and civil statutes and common law.[8]

The State Appointment Provision in S. 1441

While we applaud the improvements in S. 2494 over some previous bills, we believe that the state appointments scheme set forth in S. 1441, expanded as suggested below, would have great potential for increasing state-federal cooperation in attacking telemarketing fraud.

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[7] Letter from Thomas M. Boyd, Acting Assistant Attorney General, Office of Legal Policy, U.S. Department of Justice, to the Hon. John McCain, United States Senate, September 27, 1988.

[8] We also recommend that § 4(a)(3) of S. 2494 be amended to provide reasonable advance notice to the Commission of the filing of federal court actions by the states, to facilitate exercise of the intervention rights set forth therein.

Section 4(e) of S. 1441, rather than authorizing direct state enforcement of its proposed telemarketing rule, explicitly authorizes the Commission to appoint state attorneys general to assist the Commission in general rule enforcement. We believe such arrangements with the states could achieve much the same objectives as section 4 of S. 2494. In the attached comments on S. 1441, we have suggested an expansion of the appointments scheme to include permanent injunction cases brought under section 13(b) of the FTC Act against fraudulent telemarketers. The Commission ordinarily attacks hard-core fraud by bringing such section 13(b) cases, rather than by rule enforcement. We also urged that the Commission be authorized to appoint not only state attorneys general, but also other officials granted civil or criminal law enforcement authority under state law.

There are several advantages to this appointments scheme. The states would be in a position to participate in nationwide redress cases against hard-core fraud under the FTC Act. The Commission and the states could work out arrangements to ensure speedy joint action against fraud, while preserving consistent enforcement of the Act. We should also note that the appointments system does not pose the constitutional risks of alternatives that provide for full unilateral state enforcement of the FTC Act and its nationwide remedies.[9]

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[9] The suits "on behalf of their residents" by states to enforce the telemarketing rule, as contemplated in S. 2494, also pose less risk of constitutional challenge compared to these broader state enforcement schemes.

Private Right of Action

Section 5 of S. 2494 gives private citizens the right to bring a civil action in federal district court (1) to enforce compliance with the new Commission telemarketing rule and ord obtained thereunder, and (2) to seek relief for violations of new federal cause of action for "fraudulent act[s] or practice[s]."[10] Other than the requirement that the amount in controversy exceed $50,000, the private right of action provisions of section 5 parallel the state enforcement provisi of section 4.

As stated above with respect to the state enforcement provisions, we assume that the fraud cause of action is not intended as an addition to FTC doctrine. Nevertheless, the prospect of private parties enforcing a vague new "fraudulent or practice" cause of action may raise concern for legitimate telemarketers. In our previous testimony on similar provisions the Commission observed that there was risk that the bills woul have the effect of creating a new federal cause of action applicable to ordinary business transactions rather than to the intended target, i.e. quasi-criminal activity. This issue has surfaced in the considerable controversy over private plaintiff

[10] We assume that the reference in section 5 of S. 2494 to private parties bringing actions "on behalf of their residents" was unintended.

use of the RICO statute in litigation over garden-variety business disputes.[11]

One problem is the inherent difficulty of defining "telemarketer" and "telemarketing" with adequate specificity. While the bill makes a laudable effort in that regard, the intended scope of activity remains unclear. As defined in the bill, the term "telemarketing" means "a plan, program or campaign conducted to induce purchases of goods or services by significant use of one or more telephones through interstate voice telephone calls; the term does not include other use of a telephone in connection with business or personal transactions." "Significant" is not defined, meaning the court would have to decide whether one telephone call or one hundred satisfies the bill's definition.

Moreover, this problem is compounded by the vagueness of the term "fraudulent act or practice" itself. Without further definition, the term arguably applies in any instance where a person believes he or she was intentionally misled in an ordinary business transaction conducted over the telephone.

Venue and Compulsory Process

As discussed in the Commission's letter of March 16, 1990, to Senator McCain, we have experienced problems with the venue provisions of section 13 of the FTC Act, our most common tool in

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[11] Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. § 1961 (1982 & Supp. IV 1986).

attacking consumer fraud. There have been cases where staff, confronted with venue problems, could not bring meritorious claims against participants in fraud who did not reside or transact business in the forum state.

This problem will grow in importance as the Commission increases its enforcement efforts against suppliers of fraudulent instrumentalities and other aiders-and-abettors of boilerroom fraud. Frequently, the more complex schemes involve a network of firms and individuals spread over many states. Getting at the root of such frauds often will involve suing the principal aider-and-abettor in its home jurisdiction, and trying to join as defendants as many of the participating boilerrooms as possible, wherever located.

Section 6 of S. 2494, like section 4 of S. 1441, would remedy these venue problems by making it clear that the Commission may sue all such defendants in one district when a federal court finds that the ends of justice so require. This would be a welcome amendment to our statute. As in the case of S. 1441, we would recommend the addition of language to allow the court to serve its process on the defendant "wherever it may be found."[12] Without such a provision, service of a summons outside the state in which the court sits depends upon the vagaries of state long-arm statute requirements, which in particular instances may not be broad enough to reach out-of-state

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[12] Our specific proposed amendment can be found in footnote 2 of the letter to Senator McCain.

defendants. Congress has provided for such extraterritorial service of process in similar contexts. See, e.g., 15 U.S.C. § 22 (Clayton Act); 18 U.S.C. § 1965 (RICO); 15 U.S.C. § 77v(a) (SEC).

Both bills would further amend the FTC Act to address, for the first time, the manner in which the Commission may serve process in section 13 actions (section 6(b) of S. 2494 and section 4(a)(2) of S. 1441). Currently, the Commission serves process pursuant to the provisions of Rule 4 of the Federal Rules of Civil Procedure. Essentially, Rule 4 gives the Commission the service-of-process options set out in the Rule itself, or those provided by relevant state law. We have no objection to the substitute service-of-process provisions in these bills, but note that the current scheme has proved satisfactory. As with S. 1441, we would recommend one change to section 4(a)(2), however. The phrase "any process of the Commission" should be changed to "process of the court," to reflect the fact that section 13(b) cases are brought in federal court.

Finally, we strongly support section 7 of S. 2494, which, like S. 1441, would amend the FTC Act to enable the Commission to require the production of physical evidence pursuant to civil investigative demands. Currently, section 20 of the FTC Act only permits the Commission to require the production of documents or testimony. The above provision in the bill would enhance our ability to investigate telemarketing scams.

Clearinghouse

S. 2494, unlike S. 1441, would require the Commission t provide information to any person inquiring about telemarket through a clearinghouse to be established by the Commission. fully support the intent of this provision to enable consume obtain information on potential scams before they are defrau We also appreciate the bill's recognition of the Commission's need to protect the confidentiality and integrity of our investigations. Given this necessary exemption from disclosu provided in the bill, however, we question whether, in the no course, we could provide consumers with meaningful informatio about many companies with which they are dealing. For exampl we can not reveal whether a particular company is under investigation. Nevertheless, the clearinghouse could be a sou of centralized information regarding the existence of ongoing litigation and the results of completed cases.

Recommended Additions to S. 2494

As in our comments on S. 1441, we recommend that the Subcommittee consider a number of additional provisions that would assist the Commission in its fight against consumer fraud.[13]

[13] We note that the Commission also welcomed the requirements in S. 1441 that the Commission conduct studies in the life care nursing home industry and long-term health care insurance industry.

Criminal Contempt Authority

First, we recommend that the bills amend the FTC Act to clarify the Commission's criminal contempt authority with respect to orders it obtains in section 13(b) actions. Specifically, we recommend that section 16 of the FTC Act be amended to explicitly authorize the Commission, after consultation with the Justice Department, to bring criminal contempt actions for violations of orders obtained in such cases. This would be the same consultation procedure by which the Commission now brings civil penalty and other federal court actions as to which it does not now have exclusive litigating authority. As in civil penalty actions, the Justice Department would retain the right of first refusal to bring such actions, to be exercised within forty-five days of notification by the Commission.[14]

The proposed amendment would be an important complement to our enforcement powers under section 13(b) of the FTC Act. As stated before, scam operators are adept at resurfacing with new frauds under new names, and fear criminal prosecution more than civil suits. Staff has encountered instances where scam operators have hidden assets or re-opened new fraudulent businesses in violation of existing court orders. With the above authority, the Commission would be in a position to act quickly against violators of orders, while the Justice Department would retain the option to take action itself.

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[14] Our specific proposed amendment can be found in footnote 14 of the letter to Senator McCain.

Civil Penalty Authority

Second, we recommend that section 5(m)(1)(B) of the FTC Act be amended to extend the Commission's existing civil penalty authority. Currently, that section authorizes the Commission to bring civil penalty actions in federal court against persons who have actual knowledge that their conduct violates the FTC Act. A pre-condition to such suits is a prior Commission determination in a cease and desist order proceeding that the specific practice is unlawful. Such a Commission order, or synopsis thereof, can be sent to others in the industry who are engaged in the same practice, putting them on notice that they may be charged with civil penalties if they continue this practice.

The Commission cannot exercise this civil penalty authority if a federal court, rather than the Commission, has made the determination that a specific practice violates the FTC Act. We recommend that section 5(m)(1)(B) be amended to permit civil penalty suits where federal courts, as well as the Commission, have made such determinations.[15] This added civil penalty authority would be an important supplement to the existing injunctive and redress remedies in section 13(b) cases. Besides its general deterrent effect, civil penalty authority would provide the Commission with a monetary remedy where redress to consumers or other equitable remedies are impractical.

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[15] Our specific proposed amendment can be found in footnote 16 of the letter to Senator McCain.

Right to Financial Privacy Act

The Commission ordinarily tries to locate potential defendants' assets before suit is filed. The Commission then requests that the court grant ex parte asset freeze orders that immediately can be served on all relevant financial institutions before the defendants can hide their assets. Obviously, this pre-complaint search for assets must be conducted without alerting the target individuals. The Right to Financial Privacy Act,[16] however, makes this difficult with respect to the assets held by financial institutions for individuals and certain small partnerships. Currently, the Act requires that such customers of financial institutions be notified of federal agency inquiries, with certain exceptions. These exceptions are not specifically tailored to address situations where investigative targets are likely to dissipate assets obtained through fraud.

Section 4(d) of S. 1441 would remedy this problem by adding a new exemption applicable to the routine fraud case. Specifically, federal agencies could delay notice where a federal district court finds, inter alia, that there is reason to believe that notice will result in "dissipation, removal, or destruction of assets that are subject to forfeiture, seizure, redress, or restitution under any law of the United States by reason of having been obtained in violation of law."

We welcome this provision, and recommend its addition to S. 2494. We suggest only one modification to make the process

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[16] 12 U.S.C. § 3401 et seq.

less cumbersome. If the language of section 4(d) of S. 1441 we to be adopted without change, the Right to Financial Privacy Ac arguably, still would require the Commission to file an ex part sealed complaint in the home district of every financial institution from which it seeks information.[17] Often, individuals and small partnerships running consumer frauds maintain numerous financial accounts spread over the country. such circumstances, the search for individual and partnership assets would remain a difficult task. One solution would be to further amend the Right to Financial Privacy Act to permit the Commission and other federal agencies to file applications with "any district court of the United States within the jurisdictio of which such inquiry is carried on." This is the language in section 9 of the FTC Act that describes the courts to which the Commission may apply to enforce subpoenas.

This approach would retain judicial protection of the privacy rights of financial institution customers, while greatly reducing the Commission's time and travel burden. Headquarters staff often could obtain judicial approval in the U.S. District

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[17] Under 12 U.S.C. § 3409(a), the Government must obtain "an order of an appropriate court" granting the requested delay of notice to the customer and prohibiting the bank from disclosing the government inquiry to the customer. (emphasis supplied) Although "appropriate court" is not defined in the statute, this term could be read as requiring the Government to file the application in the federal judicial district within which the financial institution is located.

Court for the District of Columbia, and Commission regional staff often could obtain court approvals in their home cities.[18]

Thank you once again for the opportunity to provide our views on S. 2494, introduced by Senator Bryan, and S. 1441, introduced by Senator McCain. We would greatly appreciate the opportunity to comment further on any significant revisions, and stand ready to assist you in your further consideration of the bill.

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[18] Section 4(c) of S. 1441 would have the beneficial effect of granting the Commission access to mail covers, which, under current postal regulations are only made available to agencies in connection with criminal investigations. The language of section 4(c) is an improvement over that of the predecessor bill, S. 2326, in making clear that the Commission would have the same power to obtain mail covers as "law enforcement agencies investigating the commission or attempted commission of a crime." The corresponding reference in S. 2326 was "other law enforcement agencies," which arguably would have included some civil law enforcement agencies that do not have access to mail covers and, unlike the Commission, do not even investigate criminal fraud-type activities.

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

OFFICE OF
THE CHAIRMAN

March 16, 1990

The Honorable John McCain
United States Senate
Washington, D.C. 20510-6125

Dear Senator McCain:

Thank you for your letter of December 6, 1989, requesting the Federal Trade Commission's views on S. 1441, the Consumer Fraud Prevention Act of 1989. We believe the bill would be of substantial assistance to the Commission in its fight against consumer fraud, and commend you for your efforts. The views set forth in this letter are those of the entire Commission.

Below, we first describe some of the law enforcement problems we encounter in combatting consumer fraud, and then offer comments on the specifics of S. 1441.

As you observed in introducing the bill,[1] consumer fraud comes in many guises. Each year, consumers lose billions of dollars due to the fraudulent sale of goods and services. Many of these frauds present enormous difficulties for law enforcers.

An example is telemarketing fraud, specifically addressed in S. 1441. The classic example is the fly-by-night telephone "boilerroom" that peddles millions of dollars of worthless goods over the telephone and then disappears, reappearing elsewhere under a different name. If made aware of a government investigation, the individuals operating these scams often will close shop and flee, hiding assets and destroying incriminating records. Thus, effective law enforcement requires construction of the case without alerting the targets. This is a formidable task, given the difficulty of finding victims and former employees, establishing oral representations, and locating consumer monies without the targets being informed of the inquiry.

These investigations and subsequent lawsuits also can be complex and resource-intensive. For example, it may take sophisticated expert testimony to prove that the seller's

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[1] 135 Cong. Rec. S9142-45 (daily ed. July 31, 1989) (statement of Sen. McCain).

investments or other offerings are not as represented. To make case for consumer redress, the Commission also must present convincing evidence of a broad pattern of misrepresentations. This can be difficult where oral representations are the heart o the fraud. Finally, the Commission often must send teams of lawyers to the target's home jurisdiction to file suit and assis in the seizure of records and assets. Litigation can be protracted, sometimes extending to bankruptcy court where the Commission is seeking consumer redress and competing with other creditors for the company's assets.

The Commission is proud of its efforts in combatting consumer fraud. The Commission has brought some 48 cases in federal court since 1983 against fraudulent telemarketers alone. The target companies had sales of over $740 million, involving a wide variety of scams -- the fraudulent sale of gemstones, oil leases, government lottery application services, oil and gas drilling ventures, silver and gold ore processing contracts, rar coins, vacation packages, fake art, business equipment and supplies, and employment services.

A cooperative federal-state law enforcement approach using both civil and criminal weapons can go far towards controlling telemarketing fraud. In general, we believe that legislative efforts in this area should be consistent with the following two principles.

First, it is important to facilitate the use of criminal enforcement tools in combatting consumer fraud. These frauds, for the most part, are a highly lucrative criminal activity. Many perpetrators have criminal records and no qualms about bilking consumers, including widows on pensions. Many scam artists become millionaires through this activity. Although civil law enforcement can substantially hinder their activities, scam operators fear criminal prosecution above all. We believe that increased criminal law enforcement is indispensable to controlling consumer fraud, and encourage criminal law enforcement by appropriate federal and state authorities whenever we find evidence of criminal fraud in our cases.

Second, civil law enforcement should focus principally on stopping the most egregious practices -- the deceptive tactics that induce purchasers to buy goods and services that, if not worthless, are worth far less than represented. We recognize that other problems may be of concern to consumers, such as phon calls late at night, abusive computerized calls, and so forth. However, it is the fraudulent sale of goods and services that ha cost consumers billions of dollars. At a time of budget constraints, law enforcement resources should remain targeted on attacking these core violations.

We believe that S. 1441 is true to these principles and would substantially assist the Commission and the states in combatting consumer fraud. Below, we comment on the specific provisions in the bill.

Venue and Compulsory Process

The Commission ordinarily attacks consumer fraud using its permanent injunction authority under section 13(b) of the FTC Act, 15 U.S.C. § 53(b). The most efficient route is to bring all charges against all potential defendants in one lawsuit. However, section 13(b) now requires that suit be brought in the district where each defendant "resides or transacts business." This creates a potential problem where some targets, though participants in the fraud, have transacted much of their business outside the judicial district where suit is brought. There have been cases where staff, confronted with venue problems, have felt it necessary to abandon meritorious claims against such participants.

This problem will grow in importance as the Commission increases its enforcement efforts against suppliers of fraudulent instrumentalities and other aiders-and-abettors of boilerroom fraud. Frequently, the more complex schemes involve a network of firms and individuals spread over many states. Getting at the root of such frauds often will involve suing the principal aider-and-abettor in its home jurisdiction, and trying to join as defendants as many of the participating boilerrooms as possible, wherever located.

Section 4(a)(1) of Senate Bill 1441 would remedy these venue problems by making it clear that the Commission may sue all such defendants in one district when a federal court finds that the ends of justice so require. This would be a welcome amendment to our statute. We also would recommend the addition of language to allow the court to serve its process on the defendant "wherever it may be found."[2] Without such a provision, service of summons

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[2] Specifically, we recommend the following revisions to the amendment to section 13 already contained in the bill:

> Sec. 4. (a) Venue and Process. -- (1) Subsections (a) and (b) of section 13 of the Federal Trade Commission Act (15 U.S.C. 53) are each amended by adding at the end thereof the following: "All process of any court to which application may be made as provided in this subsection may be served upon the defendant wherever it may be found.

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outside the state in which the court sits depends upon the vagaries of state long-arm statute requirements, which in particular instances may not be broad enough to reach out-of-state defendants. Congress has provided for such extraterritorial service of process in similar contexts. See, e.g., 15 U.S.C. § 22 (Clayton Act); 18 U.S.C. § 1965 (RICO); 1 U.S.C. § 77v(a) (SEC).

Section 4(a)(2) of S. 1441 would further amend the FTC Act to address, for the first time, the manner in which the Commission may serve process in section 13 actions. Currently, the Commission serves process pursuant to the provisions of Rul 4 of the Federal Rules of Civil Procedure. Essentially, Rule 4 gives the Commission the service-of-process options set out in the Rule itself, or those provided by relevant state law. We have no objection to the substitute service-of-process provisio in S. 1441, but note that the current scheme has proved satisfactory. We would recommend one change to section 4(a)(2) however. The phrase "any process of the Commission" should be changed to "process of the court," to reflect the fact that section 13(b) cases are brought in federal court.

Finally, we strongly support section 4(b) of S. 1441, whic would amend the FTC Act to enable the Commission to require the production of physical evidence pursuant to civil investigative demands. Currently, section 20 of the FTC Act only permits the Commission to require the production of documents or testimony. The above provision in the bill would enhance our ability to investigate telemarketing scams. For example, where a company

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[2](...continued)
Whenever it appears to the court that the interests of justice require that any other person, partnership, or corporation should be a party in such suit, the court may cause such person, partnership, or corporation to be summoned without regard to whether they reside or transact business in the district in which the suit is brought, and to that end process may be served ~~in any district~~ wherever the person, partnership, or corporation may be found.

The Commission would also favor changing the word "shall" the venue language in Sections 13(a) and (b) [i.e., the final sentences in these provisions that recite that "Any such suit shall be brought in the district in which such person, partnership, or corporation resides or transacts business."] to "may" so as to make clear that the venue provisions do not foreclose application of the general venue provisions found in U.S.C. § 1391. The permissive "may" is typically used in other special venue provisions, e.g., section 12 of the Clayton Act, U.S.C. §22.

allegedly is misrepresenting the value of rare coins or lithographs, the Commission would be in a better position to obtain samples of these items from suppliers or other third parties and have them appraised by experts.[3]

Right to Financial Privacy Act

The Commission ordinarily tries to locate potential defendants' assets before suit is filed. The Commission then requests that the court grant ex parte asset freeze orders that immediately can be served on all relevant financial institutions before the defendants can hide their assets. Obviously, this pre-complaint search for assets must be conducted without alerting the target individuals. The Right to Financial Privacy Act,[4] however, makes this difficult with respect to the assets held by financial institutions for individuals and certain small partnerships. Currently, the Act requires that such customers of financial institutions be notified of federal agency inquiries, with certain exceptions. These exceptions are not specifically tailored to address situations where investigative targets are likely to dissipate assets obtained through fraud.

Section 4(d) of S. 1441 would remedy this problem by adding a new exemption applicable to the routine fraud case. Specifically, federal agencies could delay notice where a federal district court finds, inter alia, that there is reason to believe that notice will result in "dissipation, removal, or destruction of assets that are subject to forfeiture, seizure, redress, or restitution under any law of the United States by reason of having been obtained in violation of law."

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[3] Section 4(c) of the bill would have the beneficial effect of granting the Commission access to mail covers, which, under current postal regulations are only made available to agencies in connection with criminal investigations. The language of section 4(c) is an improvement over that of the predecessor bill, S. 2326, in making clear that the Commission would have the same power to obtain mail covers as "law enforcement agencies investigating the commission or attempted commission of a crime." The corresponding referent in S. 2326 was "other law enforcement agencies," which arguably would have included some civil law enforcement agencies that do not have access to mail covers and, unlike the Commission, do not even investigate criminal fraud-type activities.

[4] 12 U.S.C. § 3401 et seq.

We welcome this provision, and suggest only one modifica to make the process less cumbersome. If section 4(d) of S. 1 were to be adopted without change, the Right to Financial Pri Act, arguably, still would require the Commission to file an parte, sealed complaint in the home district of every financi institution from which it seeks information.[5] Often, individ and small partnerships running consumer frauds maintain numer financial accounts spread over the country. In such circumstances, the search for individual and partnership asse would remain a difficult task. One solution would be to furt amend the Right to Financial Privacy Act to permit the Commis and other federal agencies to file applications with "any district court of the United States within the jurisdiction o which such inquiry is carried on." This is the language in section 9 of the FTC Act that describes the courts to which t Commission may apply to enforce subpoenas.

This approach would retain judicial protection of the privacy rights of financial institution customers, while great reducing the Commission's time and travel burden. Headquarter staff often could obtain judicial approval in the U.S. Distric Court for the District of Columbia, and Commission regional st often could obtain court approvals in their home cities.

Assistance of State Attorneys General

The Commission and state law enforcement authorities have enjoyed a close working relationship in a host of fraud investigations and cases. The states and the Commission routinely share information, refer cases to one another, give another logistical assistance, and divide law enforcement responsibility in cases of overlapping jurisdiction. S. 1441 would promote even closer cooperation by authorizing the Commission to appoint state attorneys general to assist the Commission in enforcing Commission rules.

We not only support the state-appointment provision in S. 1441, but also recommend that it be broadened in two respect First, we recommend that the state-appointment authority be

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[5] Under 12 U.S.C. § 3409(a), the Government must obtain " order of an appropriate court" granting the requested delay of notice to the customer and prohibiting the bank from disclosing the government inquiry to the customer. (emphasis supplied) Although "appropriate court" is not defined in the statute, thi term could be read as requiring the Government to file the application in the federal judicial district within which the financial institution is located.

granted not only for the enforcement of Commission rules, but also for permanent injunction cases under section 13(b) of the FTC Act against telemarketers engaged in fraudulent practices. Although state participation in enforcing Commission rules is desirable, rule enforcement is not the weapon of choice with respect to the target of the bill -- consumer fraud. Typically, the essence of the fraud is the misrepresentation of the value of goods and services sold, a practice ordinarily attacked through section 13(b) lawsuits.[6]

Second, we urge that the Commission be authorized to appoint not only state attorneys general, but also other officials granted civil or criminal law enforcement authority under state law. One such law enforcement authority is the Florida Comptroller's Office, which brings enforcement actions against a wide range of consumer frauds, including the types of investment frauds investigated by the Commission.[7] The Commission also works closely with a number of district attorney's offices in attacking consumer frauds. We see no reason to limit appointments to attorneys general offices, especially if the appointment authority is extended to telemarketing fraud actions brought under section 13(b) of the FTC Act.[8]

As the Commission stated in its comments on S. 2326, introduced by you in the last Congress, we believe this approach of appointing state attorneys general is preferable to direct

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[6] Specifically, we recommend that section 4(e)(1) be amended as follows: "When the public interest so requires and the Commission has reason to believe that any person, partnership, or corporation subject to its jurisdiction is violating any Commission rule or is engaged in telemarketing fraud, the Commission may appoint State attorneys general, or any other officials granted civil or criminal law enforcement authority under state law, to assist Commission attorneys in enforcing such rules or in bringing permanent injunction cases under section 13(b) of the FTC Act against such telemarketers."

[7] See e.g., Fla, Stat. Ann. §§ 20.12 and §§ 517.01 et seq. (giving the Florida Comptroller's Office the power to intercept various investment frauds).

[8] We note that the fifteen-day deadline for Commission response to requests for appointment sometimes will be impractical in complex matters. However, this should be little problem if, as we expect, the appointments scheme encourages the states to consult with Commission staff early in the investigative process.

enforcement by the states of the FTC Act or Commission rules.[9] The appointments approach, while promoting federal-state cooperation, would ensure consistent application of the FTC Act. Furthermore, the appointments approach would pose less risk of being challenged on constitutional grounds. The Department of Justice, commenting on the direct-state-enforcement provisions in two other telemarketing bills last year, expressed the view that these provisions would run afoul of the Appointments Clause.[10]

Mail Order Rule

Section 5 of S. 1441 would require the Commission to amend the Mail Order Rule, 16 C.F.R. § 435, to apply to sales made over the telephone. Section 5 would further require that the Commission, as part of this rulemaking, consider a number of other provisions, including a three-day cooling-off provision applicable to telemarketing sales.

We question the need for section 5 of the bill on several grounds. First, the Commission already is formally considering the one provision that would be mandatory in section 5(a) of the bill -- the extension of the Mail Order Rule to cover telephone sales. On November 28, 1989, the Commission published a Notice of Proposed Rulemaking to consider whether such an amendment of the Rule is desirable. 54 Fed. Reg. 49,060 et seq. (November 28, 1989). Public hearings on the rulemaking are now scheduled for March 28, 1990. We believe that this rulemaking will provide the most comprehensive basis on which to decide whether the benefits of extending the Mail Order Rule to telephone sales outweigh the costs.

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[9] Statement of the Federal Trade Commission Before the Consumer Subcommittee, Committee on Commerce, Science and Transportation, U.S. Senate, September 13, 1988, at 9-10, 17-18.

[10] Letter from Thomas M. Boyd, Acting Assistant Attorney General, Office of Legal Policy, U.S. Department of Justice, to the Hon. John McCain, United States Senate, September 27, 1988 (commenting on S. 2213 and H.R. 4101, both entitled the Telemarketing Fraud Prevention Act of 1988.) The issue is whether states, in enforcing Commission rules, would be acting as "Officers of the United States" when enforcing federal laws that vindicate public rights. Only persons appointed pursuant to the Appointments Clause may exercise such functions. See Buckley v. Valeo, 424 U.S. 1 (1975).