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H.R. 3402, THE CALLING CARD CONSUMER PROTECTION ACT

HEARING

BEFORE THE

SUBCOMMITTEE ON COMMERCE, TRADE, AND CONSUMER PROTECTION

OF THE

COMMITTEE ON ENERGY AND COMMERCE

HOUSE OF REPRESENTATIVES

ONE HUNDRED TENTH CONGRESS

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CONTENTS

	Page
Hon. Bobby L. Rush, a Representative in Congress from the State of Illinois, opening statement	1
Hon. Ed Whitfield, a Representative in Congress from the Commonwealth of Kentucky, opening statement	2
Hon. Joe Barton, a Representative in Congress from the State of Texas, opening statement	4
Hon. George Radanovich, a Representative in Congress from the State of California, opening statement	4
Hon. Eliot L. Engel, a Representative in Congress from the State of New York, opening statement	31
Hon. Edolphus Towns, a Representative in Congress from the State of New York, prepared statement	70
Hon. Marsha Blackburn, a Representative in Congress from the State of Tennessee, prepared statement	70

WITNESSES

William E. Kovacic, Chairman, Federal Trade Commission	5
Prepared statement	8
Sally Greenberg, Executive Director, National Consumers League	34
Prepared statement	36
Yvette Zaragoza, Small Business Program Manager, Latino Economic Development Corporation	49
Prepared statement	50
Julia Marlowe, Professor Emeritus, Department of Housing and Consumer Economics, University of Georgia	51
Prepared statement	54
John Eichberger, Vice-President, Government Relations, National Association of Convenience Stores	60
Prepared statement	62

H.R. 3402, THE CALLING CARD CONSUMER PROTECTION ACT

TUESDAY, SEPTEMBER 16, 2008

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON COMMERCE, TRADE,
AND CONSUMER PROTECTION,
COMMITTEE ON ENERGY AND COMMERCE,
Washington, DC.

The subcommittee met, pursuant to call, at 10:07 a.m., in room 2322 of the Rayburn House Office Building, Hon. Bobby Rush (chairman) presiding.

Members present: Representatives Rush, Schakowsky, Barrow, Whitfield, Radanovich, and Barton (ex officio).

Also present: Representative Engel.

Staff present: Consuela Washington, Judith Bailey, Christian Tanotsu Fjeld, Valerie Baron, Shannon Weinberg, and Chad Grant.

OPENING STATEMENT OF HON. BOBBY L. RUSH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ILLINOIS

Mr. RUSH. The hearing will come to order. The chairman will recognize himself for 5 minutes for opening statements and then will recognize other members including my friend, the ranking member, for 5 minutes of opening statement.

In this advanced age of telecommunications, many Americans might be surprised to find out that pre-paid calling cards is an estimated $6 million a year business, and this business is still growing. Calling cards offer consumers an informal means of long-distance communications and play a prominent role in the telecommunications sector, particularly with immigrant populations and those who need to place phone calls overseas.

Unfortunately, the waters of the calling card business are infested with sharks, meaning calling card companies, whether they are distributors or telecommunications carriers, practice outright fraud on unsuspecting consumers by deceiving them with false information. These bogus cards are sold at gas stations, bowling alleys, or out of boxes on the streets; and some are also sold in prominent retail chains.

No matter which population is served or where they are sold, these fraudulent calling cards have all one common theme: they misrepresent an outright lie to consumers about the rates, charges, and terms that apply to their products. Consumers too often buy cards that are advertised as having 500 minutes only to discover that they really only have 200 minutes or that they face a battery of hidden fees and connection charges that significantly reduce

their minutes. Unfortunately, these fraudulent practices are widespread and have a disproportionate impact, mostly on poor and immigrant communities, as well as the elderly.

To combat this plague on communities, my friend from New York, Mr. Engel, introduced H.R. 3402, the Calling Card Consumer Protection Act. H.R. 3402 will require providers and distributors of calling cards to accurately and fully disclose all the rates, all the charges, and all the terms to consumers at the point of purchase. Calling card companies that do not comply with these disclosure requirements shall be in violation of a deceptive act or practice as prohibited by rule under Section 18 of the Federal Trade Commission Act.

Lastly, in addition to the FTC, the bill empowers the States' Attorneys General with the authority to enforce this new federal law. Today's legislative hearing will deliberate on the merits of H.R. 3402. It is my intention to hold a subcommittee markup on this bill later on this afternoon. I hope members of the subcommittee will be informed by our panel, including the distinguished chairman of the FTC, for the purpose of us all working together in a bipartisan fashion to report effective legislation. As I have stated in other hearings and markups, this subcommittee has a proud tradition of producing quality, bipartisan bills, and I hope to continue that trend this afternoon. With that, I yield back the balance of my time.

It is now my pleasure and privilege and honor to recognize the ranking member of this subcommittee for 5 minutes for opening statement.

OPENING STATEMENT OF HON. ED WHITFIELD, A REPRESENTATIVE IN CONGRESS FROM THE COMMONWEALTH OF KENTUCKY

Mr. WHITFIELD. Chairman Rush, thank you very much, and we appreciate this hearing today on the Calling Card Consumer Protection Act; and as you stated, this is a large industry in this country: $4 to $6 billion a year. And the appalling thing is that it is estimated that up to $2 billion of that revenue is obtained by fraud each year, and unfortunately, over the last few years, more and more companies it appears have been selling cards that actually do not contain the number of minutes for which the card buyer has paid. This practice has become so common that consumers of these cards now expect to get much less for their money than advertised, and that is simply unacceptable.

While we all agree that something must be done to stop such blatant fraud, I know that many of us have reservations about this bill. First thing is that the FTC does not currently have jurisdiction over common carriers, and I know that they have suggested maybe a carve out to take care of a part of that problem; but I myself am concerned about that because we have not had a deliberation of the consequences of doing that, either in this subcommittee or jointly with our colleagues on the Telecommunications and Internet Subcommittee.

I am also very much concerned about how the requirements of this bill will function in the real world. We require a number of disclosures which is certainly a good thing. We need transparency on

the packaging of the card. The problem with packaging is that it is typically thrown away as consumers walk away from the retail store, and then the problem with the card is the size. There is simply not enough room to list all of the fees and rates as they apply to each country for which a single card is valid.

And that leads me to a third issue, and that relates to preemption. Without preemption, the disclosure requirements will only become, in my view, less manageable. We have essentially no preemption on the bill as it was introduced. I think it is essential that we require a strong federal preemption standard, and unless we have that, states are going to be free to go beyond the minimum standards set by the Federal Government and in doing so, we are going to have potentially 50 different disclosure statements, perhaps required in multiple languages on each card. On top of that, these disclosure statements will likely need to change on a monthly basis due to changing fees and rates as is the nature of this market.

Finally, Mr. Chairman, I am curious to find out whether legislative action is really necessary. The FTC has taken action against a number of distributors in this arena under their current jurisdiction, and while the FTC may not currently pursue actions against common carriers, it is my understanding that the FCC, the Federal Communications Commission, has all the jurisdiction necessary to proceed against any allegations of wrongdoing. Why that agency has not acted in this arena, it seems to me it is an issue ripe for the subcommittee of jurisdiction to investigate, and I would encourage Chairman Markey and Ranking Member Stearns to look at that.

Beyond that, Mr. Chairman, I would say that we stand behind you 100 percent in your efforts to stem the tide of fraud, particularly when directed at vulnerable populations and undeserved communications; and as always, we appreciate your strong leadership in all these issues. I yield back the balance of my time.

Mr. RUSH. The gentleman would just like to acknowledge that with friends like that, I don't need enemies.

The chair now recognizes the gentleman from the great State of Georgia, my home State, Mr. Barrow, for 5 minutes of opening statement.

Mr. BARROW. I thank the chair, and I thank him for acknowledging our home State. It just goes to show that many fine things claimed by others were first conceived of in Georgia.

I don't want to take any time. I want to get to the witnesses, but I do want to acknowledge the presence of a representative of my alma mater, Dr. Julia Marlowe, who is a leader in this field who will be a part of the second panel. I want to thank you for being here and bringing your expertise to bear on this.

Mr. Chairman, thank you for your acknowledgment, thank you for your leadership in calling this hearing, and I yield the balance of my time.

Mr. RUSH. The chair thanks the gentleman for the brevity of his comments.

The chair now recognizes the ranking member of the full subcommittee, my friend from the great State of Texas, Mr. Barton, for 5 minutes of opening statement.

OPENING STATEMENT OF HON. JOE BARTON, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

Mr. BARTON. First of all, Mr. Chairman, it is good to see you back in the chair.

Mr. RUSH. Thank you.

Mr. BARTON. Secondly, as Mr. Whitfield said, the Republicans are behind you. The question is, how far behind you? We do support the basic purpose of the bill. We certainly want to prevent fraud. We think you and Mr. Engel have put together a good bill. We do need to perfect it. We need to work together between now and whenever you mark it up on preemption and the scope of the bill. To be really effective, it is going to have to apply to common carriers, and you and your staff know that. So we have got several outstanding issues, but if we can resolve those as Mr. Whitfield said, we know that you have addressed an issue that needs to be addressed, and you have been a great chairman in looking some of these issues straight up and trying to address them. So hopefully we will have some bipartisan staff agreements and member agreements before we go to markup so we can be not only behind you but standing beside you in moving the bill.

Mr. RUSH. Thank you very much. Now, the chair recognizes the gentleman from the great State of California, Mr. Radanovich for 5 minutes for opening statement.

OPENING STATEMENT OF HON. GEORGE RADANOVICH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA

Mr. RADANOVICH. Thank you very much, Mr. Chairman, Mr. Ranking Member. I do want to thank you, Mr. Chairman, and also Mr. Engel for introducing this legislation and bringing attention to this important issue.

The abuse of pre-paid calling cards harms consumers across the Nation. Consumers have a right to receive the services and calling card minutes for which they pay, and fly-by-night companies seeking to make a quick buck must not be allowed to rip them off.

The federal regime governing pre-paid calling cards and services would provide clarity and consistency and would be the most effective method to address the problems and confusion surrounding pre-paid calling cards. These calling cards are primarily used for domestic long distance, international calling, completely transcending state boundaries and jurisdictions. So ensuring that disclosure requirements are the same for one state to another not only makes sense from an enforcement perspective but will also be most beneficial to the consumers who utilize these products. states should be able to enforce a federal regime, but inconsistent state laws or rules on pre-paid calling cards and services would undermine the very purpose of having a federal standard.

As a member of the Telecommunications Subcommittee, I have reviewed this issue extensively in the context of regulation on the wireless phone industry, and I have learned that with a product that so clearly exceeds any state boundaries, the most sensible and consumer-friendly approach is to create a single federal standard. As is, the legislation before us simply adds another layer of regula-

tion at the federal level without addressing the need to create and ensure consistency.

We need one set of rules governing disclosures for these credit card services, and if Congress permits, multiple jurisdictions to create rules, law-abiding pre-paid calling card service providers and distributors would spend countless resources just trying to figure out what rules apply in every state, rather than focusing on improving services to consumers. The unnecessary costs stemming from the compliance with potentially 50 regimes instead of one would undoubtedly be pass onto consumers, and we should be trying to make these credit cards more accessible.

I am also concerned about how a pre-paid calling card company would provide all the disclosure forms on an item the size of a credit card and avoid creating even more confusion. This would be completely contrary to the authors' worthwhile goal with this bill.

I strongly believe that there is a need for this legislation. I just want to make sure that in addressing that problem that we create the most effective system possible that will both protect and benefit users of pre-paid calling cards. I commend the author of the bill and the subcommittee for bringing this up and look forward to working with my colleagues on both sides to address these concerns and create a bill that we can all support because it utilizes a federal standard for disclosures that will ensure that calling cards are as safe, affordable, and user-friendly as possible.

Thank you so much, Mr. Chairman, Mr. Ranking Member. I yield back.

Mr. RUSH. Thank you so very much. Now it is time for us to hear from the chairman of the Federal Trade Commission, the Honorable William E. Kovacic. Chairman Kovacic was sworn in as Commissioner of the Federal Trade Commission in January of 2006, and President Bush designated him as chairman on March 30, 2008. This is his first time testifying in front of this subcommittee as chairman.

Mr. Chairman, we certainly want to welcome you to this subcommittee. We know that you will be very informative and enlightening to the subcommittee in your testimony, and we look forward to hearing from you. We promise to be on the best of behavior during this, your first testimony as chairman. Can't promise you the second one, now, but the first one we will be nice to you. You are recognized, Mr. Chairman, for 5 minutes of opening statement.

STATEMENT OF WILLIAM E. KOVACIC, CHAIRMAN, FEDERAL TRADE COMMISSION

Mr. KOVACIC. Thank you, Chairman Rush, Ranking Member Whitfield, and members of the subcommittee. I am not only enormously grateful to be here for the first time for what I hope is one of many conversations with this subcommittee but also to talk about a matter that all of you have described this morning as being a matter of great pressing concern.

We are concerned with the phenomenon you have described for two reasons. First, serious instances of deceit and misrepresentation are among the greatest offenses in our commercial system. If consumers cannot have confidence in the fairness and truthfulness of representations that suppliers of goods and services make, that

is a serious blow to our system of commerce, and misrepresentations with respect to the number of minutes that a card provides or the charges that will be imposed are extremely serious limitations on the operation of the pre-paid calling card system.

The second reason is one that several of you have mentioned as well, and that is the victims of the misconduct in this instance I think overwhelmingly are individuals who might be characterized as being beset by serious economic disadvantage. I regard a special responsibility of our agency is to deal with victims who fall in exactly that classification. These are individuals who frequently are not able to identify what their rights are in advance, and for a variety of historical and social reasons might not feel inclined to report to public agencies of any type the fact of wrongdoing. So our efforts in this area are part of a larger program at this agency to ensure that victims of serious economic disadvantage are not exploited in the marketplace.

For both of those reasons, this is a high priority. I would like to shortly describe for you what our program now entails and to comment briefly on the bill that you will be considering.

The first element of our program is litigation. For basically over a period of a decade now, we have been bringing cases to deal with this phenomenon. Earlier this year, we brought two cases, the Clifton Telecard Alliance case and Alternatel, which deal with major distributors of pre-paid calling cards dealing with precisely the forms of misconduct we allege and that you have been describing at the hearing today. It is our hope that if we are successful in these matters that this will have a significant effect beyond the distributors involved and will demonstrate to the industry as a whole standards that ought to be abided by by service providers in this field.

The second element of our program is to deepen cooperation with other public authorities that have responsibility in this field. We established last year a Federal-State task force that engages the energies of my agency, the Federal Communications Commission, State Attorneys General, state Public Utilities Commissions, and other government bodies. The reason for doing this is the realization that individually, if we do not collaborate effectively with other public instrumentalities, we will not solve the problem. This is a series of problems that has great cross-border features, across jurisdictions, within our own republic and outside of the United States; and the only way to achieve a truly effective resolution to this problem and related forms of misconduct is to have an effective form of cooperation.

And I would add that the two matters that I described a moment ago profited enormously from a measure that this committee was deeply involved in promoting and that is the SAFEWEB legislation that was adopted in December of 2006. We were able to develop our cases because we could work with foreign consumer protection authorities in countries such as Panama, Peru, Mexico, and others to identify the fact of the misconduct and to formulate specific allegations to challenge it.

So I want to thank this committee for their efforts less than 2 years ago to give us a platform on which we could build a more effective program.

The last element is education. We have been working to improve outreach materials, both in English and Spanish, for users of calling cards to educate them to be wiser consumers, and, very importantly, to tell them what they can do if they think they are the victims of fraud and to inform us or other public institutions about the fact of fraud. If we can be alerted to instances of misconduct by reason of a variety of reforms that this committee has sponsored well over the past decade, we now have the capacity to respond almost in real time to instances of misconduct. So encouraging victims of fraud to tell us about fraud is an extremely important element of our program and we use consumer education as a means to do it.

Last, I want to thank the Committee for its proposal, H.R. 3402. We think there are a number of very useful measures that will improve enforcement in this area. We do have specific improvements which we welcome the opportunity to discuss with you and your staff in any form that you wish involving the jurisdictional limits involving common carriage where we think it would be very useful to be permitted to enforce the law against the complete range of actors in this area.

Other measures dealing with pre-paid wireless services, the knowledge requirement for obtaining injunctions, there are a variety of areas in which again we would be quite happy to work with your staff and continue the discussion we have had with the Committee about areas of possible improvement.

We look forward to working with you as this measure advances through the Congress, and I welcome your comments and your questions. And again, I thank you very much for the chance to be part of the hearing today.

[The prepared statement of Mr. Kovacic follows:]

PREPARED STATEMENT OF
THE FEDERAL TRADE COMMISSION

on

PREPAID CALLING CARDS

Before the

SUBCOMMITTEE ON COMMERCE,
TRADE AND CONSUMER PROTECTION
of the
COMMITTEE ON ENERGY AND COMMERCE
UNITED STATES HOUSE OF REPRESENTATIVES

WASHINGTON, D.C.
September 16, 2008

I. Introduction

Chairman Rush, Ranking Member Whitfield, and other members of the Committee, I am William Kovacic, Chairman of the Federal Trade Commission ("Commission" or "FTC").[1] Thank you for giving the Commission this opportunity to testify before the Committee about consumer protection issues associated with the sale of prepaid calling cards.

The Commission appreciates the Committee's decision to hold a hearing to shed light on deceptive practices in the calling card industry. Over the last decade, the prepaid calling card industry has grown into a multi-billion dollar a year industry. Prepaid calling cards can provide consumers with a convenient and inexpensive way to call friends and family at home and abroad. Unfortunately, however, purchasers of prepaid calling cards often do not receive the number of calling minutes advertised for the cards they purchase and are charged undisclosed or inadequately-disclosed fees and surcharges that reduce the value of the prepaid calling cards they have purchased.

As the nation's consumer protection agency, the FTC is committed to protecting consumers from deceptive marketing of prepaid calling cards. The FTC recently brought two cases alleging that distributors of prepaid calling cards had been deceptively marketing such cards; the Commission also has other active prepaid calling card investigations.

This statement provides the Committee with background information about the prepaid calling card industry and describes the FTC's recent law enforcement actions against distributors of prepaid calling cards. It also discusses the FTC's consumer education and outreach efforts.

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[1]The written statement presents the views of the Federal Trade Commission. Oral statements and responses to questions reflect the views of the speaker and do not necessarily reflect the views of the Commission or any other Commissioner.

Additionally, it offers comments on H.R. 3402, the "The Calling Card Consumer Protection Act." Finally, the Commission reiterates its support for the provision of the FTC reauthorization bill that would amend the FTC Act to repeal the exemption for common carriers subject to the Communications Act. Repealing the exemption for telecommunications carriers would ensure that the Commission can bring law enforcement actions against all participants in the prepaid calling card industry that are engaging in deceptive and unfair practices, including those companies that provide the underlying telecommunications services for these cards.

II. Background

Calling card providers market their cards for a variety of uses. Some cards are marketed primarily for use by consumers making calls within the United States. Such cards usually offer consumers the ability to make domestic long distance calls for pennies per minute. Other cards are marketed to U.S. consumers who want to call the United States when they are traveling or working in other countries. Indeed, many such cards are marketed to members of the United States armed forces serving around the world. In addition, a substantial number of prepaid calling cards are sold to recent immigrants to the United States who depend on calling cards to stay in touch with family and friends abroad.[2] Such calling cards, which typically retail for between $2 to $10 each, are generally sold in small retail outlets, including grocery and convenience stores, gasoline stations, and newsstands.

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[2]See Susan Sachs, *Immigrants See Path to Riches in Phone Cards*, N.Y. TIMES, Aug. 11, 2002, *available at* http://query.nytimes.com/gst/fullpage.html?res=9800E7D6123AF932A2575BC0A9649C8B63&sec=&spon=&pagewanted=2; *Talk Isn't So Cheap on a Phone Card*, BUSINESS WEEK, July 23, 2007, *available at* http://www.businessweek.com/magazine/content/07_30/b4043079.htm; Mark E. Budnitz, Martina Rojo & Julia Marlowe, *Deceptive Claims for Prepaid Telephone Cards and the Need for Regulation*, 19 LOYOLA CONSUMER L. REV. 1 (2006).

To advertise prepaid calling cards directed to consumers making international calls from the U.S., companies distribute eye-catching posters that are displayed on the walls and windows of the stores where such cards are sold. One hallmark of such posters is bold claims, made in large, colorful type, about the number of calling minutes the advertised cards provide for calls to particular countries. In stark contrast to the claims about available calling minutes that dominate the posters, the bottom of the posters generally contains small print disclaimers about a wide variety of fees and surcharges that reduce the value of the cards. The disclaimers are frequently in type so small as to be nearly illegible and in language so vague as to be effectively incomprehensible.[3]

Consumers typically use their prepaid calling cards as follows: the consumer dials an "access number" printed on the back of the card. A recorded message then prompts the consumer to enter the card's authorization code or Personal Identification Number ("PIN"),

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[3]For example, in *FTC v. Alternatel, Inc., G.F.G. Enterprises LLC, also d/b/a Mystic Prepaid, Voice Prepaid, Inc., Voice Distributors, Inc., Telecom Express, Inc., Lucas Friedlaender, Moses Greenfield, Nickolas Gulakos, and Frank Wendorff*, 08-21433-CIV-Jordan/McAliley (S.D. Fla. filed May 19, 2008), the FTC has alleged in its complaint that: "in numerous instances defendants' posters contain vague disclosures about fees in tiny font on the bottom of the poster, stating in relevant part:

> by using this card you agree to the following: Prompted minutes are before applicable charges and fees, application of surcharges and fees have an effect of reducing total minutes on cards. One or all of the following may apply: 1) A weekly maintenance fee ranging between .49 and .79. 2) A hang-up fee between .05 and $1 depending upon length and destination of the call. 3) A destination surcharge of between 0% and 100%. – minutes and/or seconds are rounded to multiple minute increments. – International calls made to cellular phones are billed at higher rates. – Toll free access numbers are subject to an additional fee of up to 4 cents per minute. – Prices are subject to change without notice. – This card has no cash value. – Card expires 3 months after first use or 12 months after activation."

which is printed on the card. Next, the consumer usually hears an announcement of the monetary value of the card. The consumer then enters the phone number he or she is trying to reach and hears an automated "voice prompt" announcing the number of minutes of time ostensibly available on the card.

As discussed in more detail below, the FTC, our state law enforcement colleagues, and third parties who have tested a wide variety of prepaid calling cards have found that prepaid calling cards offered by a number of industry participants routinely fail to deliver the minutes promised in their advertising and voice prompts. As alleged in two cases recently brought by the FTC, our testing showed that the defendants' prepaid calling cards delivered about half the number of promised minutes.

III. Law Enforcement Actions

The FTC works closely with the offices of State Attorneys General and other state agencies. In the fall of 2007, the FTC established a joint federal-state task force concerning deceptive marketing practices in the prepaid calling card industry. The task force members include representatives from the offices of more than 35 State Attorneys General and other state and local agencies, and the Federal Communications Commission ("FCC"). Working cooperatively allows us to share information and facilitate law enforcement activity in the prepaid calling card area.[4]

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[4]Representatives from the following Offices of Attorneys General are members of the task force: Alabama, Arizona, Arkansas, California, Colorado, Connecticut, District of Columbia, Florida, Georgia, Hawaii, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Maryland, Maine, Massachusetts, Minnesota, Missouri, Montana, New Mexico, Nevada, New Hampshire, New Jersey, New York, North Carolina, North Dakota, Ohio, Oregon, Pennsylvania, Rhode Island, South Dakota, Tennessee, Texas, Virginia, Washington, Wisconsin. In addition, the New York State Consumer Protection Board and the New York City Department of Consumer Affairs have participated in the task force.

Currently, the Commission is litigating two actions in federal district court, alleging that the defendants deceptively marketed their prepaid calling cards. In addition, as discussed below, the Attorneys General for the states of Florida and Texas recently have taken action against prepaid calling card companies for their allegedly deceptive practices.

A. FTC Enforcement Actions

Under Section 5 of the FTC Act, the FTC has authority to bring cases against companies and individuals for engaging in deceptive or unfair acts or practices in or affecting commerce.[5] Since the 1990s, the FTC has used this power to bring enforcement actions against entities for deceptively selling prepaid calling cards. The Commission brought its first two prepaid calling card cases against companies that the FTC alleged were deceptively marketing prepaid calling cards by, among other things, misrepresenting the per-minute rates consumers would be charged when using the cards and by failing to clearly and conspicuously disclose connection and maintenance fees associated with the cards.[6] Since then, the FTC has brought several cases alleging that telemarketers deceptively marketed calling cards to consumers and charged consumers without their authorization.[7]

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[5] 15 U.S.C. § 45(a)(2).

[6] *FTC v. PT-1 Comm'cns, Inc.*, 99-CIV-1432 (S.D.N.Y.) (Stip. Final Order filed Feb. 25, 1999) (order requiring monetary relief and barring defendants from misrepresenting the value of its prepaid calling cards and from failing to clearly and prominently disclose fees and charges); *FTC v. Trans-Asian Comm'cns, Inc.*, 97-CIV-5764 (S.D.N.Y.) (Stip. Final Order filed Mar. 17, 1998) (order requiring $1 million performance bond before defendants can advertise or sell prepaid calling cards and barring future material misrepresentations about prepaid calling cards).

[7] *FTC v. 9131-4740 Quebec, Inc.*, CV-02242 (N.D. Ohio) (Compl. filed July 25, 2007) (pending); *FTC v. T2U, Inc.*, 101-CV-811 (N.D. Ohio) (Stip. Final Order filed Sept. 13, 2001); *FTC v. Enhanced Billing Servs., Inc.*, 101-CV-1060 (D.D.C.) (Stip. Final Order filed Aug. 1, 2001).

This spring, the FTC filed two cases against major distributors of prepaid calling cards. On March 25, 2008, the FTC sued Clifton Telecard Alliance, a national distributor of prepaid calling cards based in New Jersey, and the company's principal.[8] The FTC alleged that the defendants, which market their cards chiefly to recent immigrants, engaged in deceptive marketing practices by: (1) misrepresenting the number of calling minutes provided by their cards; (2) failing to adequately disclose fees and charges associated with their cards; and (3) failing to adequately disclose that the value of their cards may be reduced even when a call does not connect. In support of its case, the FTC tested 46 of Clifton Telecard Alliance's calling cards purchased at various retail outlets.[9] In the FTC's tests of these cards, none delivered the number of calling minutes advertised in posters displayed at the point of sale. Three of the 46 cards failed to work at all, and, on average, the remaining 43 cards delivered only 43 percent of the advertised calling minutes. On April 2, 2008, the federal district court in New Jersey granted the FTC's motion for a temporary restraining order.

On May 19, 2008, the FTC filed a similar action, *FTC v. Alternatel*, against several companies alleged to act as a common enterprise in distributing prepaid calling cards out of

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[8]*FTC v. Clifton Telecard Alliance One LLC, d/b/a Clifton Telecard Alliance and CTA, Inc., and Mustafa Qattous*, 2:08-cv-01480-PGS-ES (D.N.J. filed Mar. 25, 2008).

[9]The FTC has been able to test prepaid calling cards thanks in part to the invaluable assistance of El Salvador's Defensoría del Consumidor, Colombia's Superintendencia de Industria y Comercio, the Egypt Consumer Protection Authority, Mexico's Procuraduría Federal del Consumidor (PROFECO), Panama's Autoridad de Protección al Consumidor y Defensa de la Competencia, and Peru's Instituto Nacional de Defensa de la Competencia y de la Protección de la Propiedad Intelectual (INDECOPI). In this area, as in so many others, international cooperation has proved to be vital to the Commission's law enforcement actions.

Florida, Massachusetts, and New Jersey.[10] In the *Alternatel* case, the Commission alleged that the defendants violated Section 5 of the FTC Act by misrepresenting the number of calling minutes their cards provide and failing to adequately disclose fees and charges associated with their cards. As in the *Clifton Telecard Alliance* case, the FTC conducted extensive testing of the *Alternatel* defendants' prepaid cards and found that the actual number of minutes provided by the cards fell far short of the defendants' advertising claims. In tests of 87 of the defendants' cards, the cards delivered on average only 50.4 percent of the minutes advertised on posters at the point of sale.[11] On May 23, 2008, the federal district court for the Southern District of Florida entered a temporary restraining order in the *Alternatel* matter.

In both the *Clifton* and *Alternatel* actions, the defendants have moved to dismiss the FTC's case on the grounds that the underlying telecommunications carriers are necessary parties

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[10]*FTC v. Alternatel, Inc., G.F.G. Enterprises LLC, also d/b/a Mystic Prepaid, Voice Prepaid, Inc., Voice Distributors, Inc , Telecom Express, Inc., Lucas Friedlaender, Moses Greenfield, Nickolas Gulakos, and Frank Wendorff*, 08-21433-CIV-Jordan/McAliley (S.D. Fla. filed May 19, 2008).

[11]The results of the FTC testing of the defendants' cards in the *Clifton Telecard Alliance* and the *Alternatel* cases are consistent with the testing results of the Hispanic Institute, a non-profit organization that has issued a report on its testing of a wide variety of prepaid calling cards. The Hispanic Institute reports that, on average, the cards it tested delivered only 60% of the minutes promised in voice prompts. *See* http://www.thehispanicinstitute.net/research/callingcard/qa (visited June 18, 2008). They are also consistent with testing results that have been offered in private litigation. *See IDT Telecom, Inc. v. CVT Prepaid Solutions, Inc., et al.*, Civil Action No. 07-1076 (D.N.J.) (Pls. Mem. In Supp. of Their Order to Show Cause Why a Prelim. Inj. Should Not Issue, at 6-10; Ex. 1 to Suppl. Aff. of Gabi Schechter, dated Mar. 26, 2007) (alleging the defendants' calling cards delivered on average only 60% of prompted minutes); *IDT Telecom, Inc. v. Voice Distributors, Inc., d/b/a Voice Prepaid, et al.*, Civil Action No. 07-2465 (Mass. Sup. Ct., Middlesex Cty.) (Compl. ¶ 16) (alleging that the defendants' calling cards delivered on average only 65% of prompted minutes); *IDT Telecom, Inc. v. Diamond Phone Card, Inc., et al.*, Index No. 3682-08 (N.Y. Sup. Ct., Kings Cty.) (Compl. ¶ 15) (alleging that the defendants' calling cards delivered on average only 59% of prompted minutes).

that the FTC cannot join because of the exemption in the FTC Act for common carriers subject to the Communications Act. The FTC has opposed defendants' motions, and is confident that it will win on the merits. As final relief in both cases, the FTC seeks a permanent injunction and consumer redress and/or disgorgement of ill-gotten gains.

B. State Law Enforcement Actions

Two states recently brought law enforcement actions against a number of prepaid calling card companies. Over the last few months, the Florida Attorney General has announced that he has entered into Assurances of Voluntary Compliance ("AVC") with eleven prepaid calling card companies doing business in Florida.[12] These settlements are the culmination of a broad investigation into the prepaid calling card industry launched by the Florida Attorney General in July of 2007. Notably, while the FTC has brought its lawsuits solely against distributors of prepaid calling cards, the Florida Attorney General entered into AVCs with eleven companies that include both distributors and telecommunications service providers for prepaid calling cards.

On May 23, 2008, the Texas Attorney General filed a lawsuit against Next-G Communication, Inc., a telecommunications service provider that produces, sells and distributes

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[12]*See McCollum Announces Prepaid Calling Card Settlements, Industry-Wide Reform* (June 11, 2008) *available at* http://myfloridalegal.com/newsrel.nsf/newsreleases/79C6666DB24608D785257465004EC901 (visited on August 27, 2008) (announcing settlements with IDT America, Inc.; Union Telecom Alliance; Total Call International, Inc.; Blackstone Calling Card, Inc.; CVT Prepaid Solutions, Inc.; Dollar Phone Enterprise, Inc.; STi Prepaid, LLC; Alternatel, Inc; and Cristel Telecommunications, LLC); *Prepaid Calling Company Reaches Settlement with Attorney General* (July 2, 2008) *available at* http://myfloridalegal.com/newsrel.nsf/newsreleases/1439BD5308D470588525747A006423B8 (visited on August 27, 2008) (announcing a settlement with Touch-Tel Partners USA, LLC); *Attorney General Reaches Settlement with 11th Prepaid Calling Card Company* (August 21, 2008) *available at* http://myfloridalegal.com/newsrel.nsf/newsreleases/C410C546EB409C93852574AC006C9499 (visited on August 27, 2008) (announcing settlement with Cinco Telecom Corp. d/b/a Orbitel).

prepaid calling cards.[13] The Texas lawsuit alleges that Next-G Communication has marketed and sold prepaid calling cards throughout Texas that fail to deliver the number of minutes it advertises to customers and that the defendant has failed to disclose fees and charges associated with its calling cards. The Texas Attorney General alleges that Next-G's prepaid calling cards consistently delivered only 40 percent of the minutes claimed on the Next-G's advertising posters and confirmed by Next-G's voice prompt given at the beginning of each call.[14]

The FTC applauds the actions of the Florida and Texas Attorneys General and is grateful for the participation of all of our law enforcement partners in the joint federal-state calling card task force.

IV. Consumer Education and Media Outreach

In addition to bringing enforcement cases, the Commission has made consumer education and outreach a high priority. The FTC recently updated its consumer education brochure on calling cards, which is available in both English and Spanish on the Commission's website.[15] The Commission also has done extensive outreach about prepaid calling cards to media outlets that cater to non-English and English speaking consumers. The FTC wants to make sure consumers know that it is unlawful to advertise calling cards that misrepresent the number of minutes that the calling cards provide or to fail to clearly and conspicuously disclose

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[13] *State of Texas v. Next-G Commnc'n, Inc., Taj Khwaja*, 2008CI08149 (Bexar County, TX) (Pet. filed May 23, 2008).

[14] *See Attorney General Abbott Takes Legal Action Against Prepaid Calling Card Company* (May 23, 2008) *available at* http://www.oag.state.tx.us/oagNews/release.php?id=2479 (visited on August 27, 2008).

[15] *See Buying Time: The Facts About Pre-Paid Phone Cards* (2008) *available at* http://www.ftc.gov/bcp/edu/pubs/consumer/products/pro04.pdf (visited on August 27, 2008).

the fees and charges that reduce the value of the calling cards. The FTC also wants consumers to know that they can and should complain to the FTC if they do not get what they pay for.

V. The Proposed Legislation

As described above, the FTC Act's prohibitions on deceptive and unfair practices provide the Commission with a powerful tool to bring enforcement actions against the distributors of prepaid calling cards. H.R. 3402, the proposed "Calling Card Consumer Protection Act" (the "Act"), would add an important remedy to those already available to the Commission by authorizing the FTC to seek civil penalties for violations of the Act or of rules issued by the FTC pursuant to the Act.

Generally, H.R. 3402 requires prepaid calling card providers and distributors to clearly and conspicuously disclose, among other things, the dollar value of their calling cards, or the number of minutes provided by their calling cards, and material terms and conditions pertaining to their cards, including all fees and limitations on use of their cards. The bill prohibits prepaid calling card providers and distributors from assessing fees or imposing charges if such fees or charges are not adequately disclosed. It also prohibits providers from providing fewer minutes than advertised, and prohibits distributors from distributing cards that they know provide fewer minutes than advertised. The bill gives the FTC discretionary rulemaking authority to carry out the Act. It further provides for the FTC to bring suit alleging violations of the Calling Card Consumer Protection Act as if they were violations of an FTC rule, thus enabling the agency to seek civil penalties for violation of the Act and any FTC rule promulgated pursuant to the Act.

The FTC supports the goal of H.R. 3402 and appreciates the proposed authority to seek civil penalties. Three aspects of the bill raise concerns, however. First, the bill apparently does not give the Commission authority to enforce the provisions of the Act against common carriers

providing prepaid telecommunications services. Although the Act would prohibit providers of prepaid telecommunications services from engaging in certain deceptive practices, the bill provides for FTC enforcement "in the same manner, by the same means, and with the same jurisdiction" as the FTC Act. Common carriers subject to the Communications Act are excluded from the FTC's jurisdiction under the FTC Act. Therefore, the Calling Card Consumer Protection Act would appear to exempt common carriers acting as providers of prepaid calling services from FTC enforcement of the Calling Card Consumer Protection Act.

Second, the Calling Card Consumer Protection Act would include a knowledge standard for holding prepaid calling card distributors liable if they violate the Act by distributing calling cards that provide fewer minutes than advertised or announced on the voice prompt given when a consumer places a call.[16] Incorporating a knowledge standard into the law could create an additional -- and potentially very challenging -- evidentiary burden on the FTC when seeking injunctive relief in a civil case.[17]

The Commission's final concern is that the bill explicitly exempts from its coverage prepaid wireless phone services where the consumer has a pre-established relationship with the

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[16]The bill does not have a parallel knowledge requirement for prepaid calling card service providers.

[17]Indeed, under general consumer protection principles and traditional jurisprudence under Section 5 of the FTC Act, 15 U.S.C. § 45, the Commission need not show knowledge or intent in order to stop an entity from engaging in unfair or deceptive practices. Notably, however, Section 5(m)(1) of the FTC Act includes a knowledge standard for instances where the FTC is seeking civil penalties for violations of an FTC Rule, as opposed to equitable relief, such as an injunction. 15 U.S.C. § 45(m)(1) ("The Commission may commence a civil action to recover a civil penalty in a district court of the United States against any person, partnership, or corporation which violates any rule under this chapter respecting unfair or deceptive acts or practices . . . with actual knowledge or knowledge fairly implied on the basis of objective circumstances."). Eliminating the knowledge threshold from the bill would not change the Commission's elevated burden for obtaining monetary relief in civil penalty cases.

wireless carrier or creates a customer-carrier relationship by purchasing a wireless phone. The Commission is concerned that the bill's exception for some wireless prepaid services would provide a powerful incentive for the worst actors in the prepaid calling card industry to migrate their business practices to prepaid wireless handsets and refill cards, and thereby avoid the mandates of the proposed law.[18]

To enable the Commission to address problems with deceptive conduct involving prepaid calling cards more effectively, the Committee might also consider giving the Commission authority to bring actions seeking civil penalties in its own right against prepaid calling card providers and distributors rather than through the Department of Justice. Giving the FTC authority to bring its own civil penalties cases in this area would help ensure that the Commission does not have to forego quick relief in order to seek civil penalties.

The Commission recognizes that the agency and the Committee share the same goal: stopping unscrupulous calling card companies from defrauding vulnerable consumers. The Commission looks forward to working with the Committee regarding the language of the legislation as the Committee moves forward.

VI. The Common Carrier Exemption

On several occasions, the Commission has testified in favor of the repeal of the common carrier exemption.[19] The Commission continues to endorse its repeal, and thanks the Committee

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[18]Some participants in the prepaid calling card industry are beginning to offer prepaid wireless services. As the cost of providing cellular phones and calling minutes continues to decrease, the incentive to move consumers to prepaid wireless accounts from more traditional prepaid calling cards has increased.

[19]See *Prepared Statement of the Federal Trade Commission*, Before the Subcommittee on Interstate Commerce, Trade, and Tourism Committee on Commerce, Science and Transportation United States Senate (April 8, 2008), *available at*

for its continued support for this measure. As previously noted, the FTC Act exempts from the FTC's jurisdiction common carriers subject to the Communications Act. This exemption originated in an era when telecommunications services were provided by highly-regulated monopolies. The Commission believes that the exemption is now outdated. In the current marketplace, firms are expected to compete in providing telecommunications services. Congress and the FCC have dismantled much of the economic regulatory apparatus formerly applicable to the industry. Removing the exemption from the FTC Act would not alter the jurisdiction of the FCC, but would give the FTC the authority to protect consumers against unfair and deceptive practices by common carriers in the same way that it can protect against unfair and deceptive practices by non-common carriers involved in the provision of similar services.

Prepaid calling cards are a case in point. In contrast to the State Attorneys General, who are able to bring enforcement actions to stop both telecommunications providers and distributors offering prepaid calling cards from engaging in unfair and deceptive practices, the FTC has targeted only the deceptive practices of prepaid calling card distributors, because of the FTC Act

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http://www.ftc.gov/os/testimony/P034101reauth.pdf; *Prepared Statement of the Federal Trade Commission*, Before the Subcommittee on Interstate Commerce, Trade, and Tourism Committee on Commerce, Science and Transportation United States Senate (Sept. 12, 2007), *available at* http://www.ftc.gov/os/testimony/070912reauthorizationtestimony.pdf; Prepared Statement of the Federal Trade Commission On FTC Jurisdiction Over Broadband Internet Access Services, Before the Committee on the Judiciary, United States Senate (Jun. 14, 2006), *available at* http://www.ftc.gov/opa/2006/06/broadband.shtm; *The Reauthorization of the Federal Trade Commission: Positioning the Commission for the Twenty-First Century: Hearing Before the Subcomm. on Commerce, Trade and Consumer Protection of the H. Comm. on Energy and Commerce*, 108th Cong. (2003) ("*FTC 2003 Reauthorization Hearing*") (statement of the FTC), *available at* http://www.ftc.gov/os/2003/06/030611reauthhr.htm; see also FTC 2003 Reauthorization Hearing (statement of Thomas B. Leary, FTC Commissioner), *available at* http://www.ftc.gov/os/2003/06/030611learyhr.htm; *FTC Reauthorization Hearing: Before the Subcomm. on Consumer Affairs, Foreign Commerce and Tourism of the S. Comm. on Commerce, Science and Transportation*, 107th Cong. (2002) (statement of Sheila F. Anthony, FTC Commissioner), *available at* http://www.ftc.gov/os/2002/07/sfareauthtest.htm.

common carrier exemption. Furthermore, even when the Commission has identified and brought enforcement actions against non-common carriers, the common carrier exemption can impose additional litigation costs on the FTC. For example, as noted above, in both the *Clifton Telecard Alliance* and *Alternatel* cases, which the FTC has brought against distributors of prepaid calling cards, the defendants have moved to dismiss the FTC's cases on the grounds that the FTC has not sued and cannot sue the underlying carriers, which defendants allege to be necessary parties. While the Commission is confident that it will prevail in its opposition to these motions, the burden of having to respond to such motions is not insubstantial.

To enable the Commission to enforce H.R. 3402 more effectively and to create a level playing field, we recommend that the bill be amended to clearly grant to the FTC jurisdiction over the activities of common carriers providing prepaid calling card services. More fundamentally, the FTC respectfully continues to recommend that Congress repeal altogether the FTC Act exemption for common carriers subject to the Communications Act. The FTC has extensive expertise with such areas as advertising, marketing, billing, and collection, areas in which significant problems have emerged in the telecommunications industry.[20] In addition, the FTC has powerful procedural and remedial tools that could be used

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[20]For example, the FTC has brought numerous cases involving the cramming of unauthorized charges onto consumers phone bills. *See, e.g., FTC v. Verity Int'l Ltd.* 335 F. Supp. 2d 479 (S.D.N.Y. 2004), *aff'd in part, rev'd in part*, 443 F.3d 48 (2d Cir. 2006), *cert. denied*, 127 S. Ct. 1868 (2007); *FTC v. Audiotex Connection, Inc.*, C-97 0726 (DRH) (E.D.N.Y. 1997); *FTC v. Int'l Telemedia Assocs., Inc.*, 1-98-CV-1925 (N.D. Ga., 1998); *FTC v. Sheinkin*, 2-00-363618 (D.S.C., 2000); *FTC v. Mercury Marketing of Delaware, Inc.*, 00-CV-3281 (E.D. Pa. 2000); *FTC v. Epixtar Corp.*, 03-CV-8511 (DAB) (S.D.N.Y. 2003); *FTC v. Nationwide Connections, Inc.*, 06-80180-CIV-Ryskamp/Vitunac (S.D. Fla. 2006); *FTC v. Websource Media, LLC*, Civ. No. H-06-1980 (S.D. Tex. 2006).

effectively to address developing problems in the telecommunications industry if the FTC were authorized to reach them.

VII. Conclusion

The Commission will continue its aggressive law enforcement and consumer outreach and education programs in the prepaid calling card arena. The Commission thanks this Committee for focusing attention on this important issue and for the opportunity to discuss its law enforcement program.

Mr. RUSH. Thank you very much, Chairman Kovacic. The chair recognizes himself now for 5 minutes for questioning.

Mr. Kovacic, H.R. 3402 as introduced leaves the FTC's jurisdiction as is currently stated in the FTC Act, which exempts common carriers from FTC jurisdiction. How effective would the bill be in cleaning up industry if the FTC can't enforce violations against common carriers? I have two questions. Secondly, is there a precedent given the FTC jurisdiction to enforce and screen consumer protection laws against common carriers?

Mr. KOVACIC. Chairman Rush, there are of course a number of other public institutions that would be able to enforce the law if we were not involved. We think of ourselves because we have unsurpassed experience in identifying and challenging unfair deceptive practices—to leave us off the field is to leave someone with a good batting average and a lot of production on the bench. We think that would be a serious limitation, and we do urge you and your colleagues to consider the possibility that if we are engaged in the enforcement process, the enforcement of these measures will be greatly enhanced by reason of this larger body of experience that we would bring to the process.

There are specific instances in which the Congress has given us specific ability to work in areas involving common carriage. A number of specific statutes that Congress has adopted have allowed us for specific purposes to address the behavior of common carriers. For example, in the area of unauthorized billing. If the billing for non-common carrier services is included on a consumer's bill, even if the bill is provided by a common carrier, Congress many years ago recognized that it would be useful for us to address unauthorized billing in that context. I would be happy to provide for the Committee a full description of the specific areas in which Congress has permitted us to be active.

So I think there are good illustrations where this has worked, and again, I think to allow us with our experience, and I would say our good batting average, to come off the bench and be in the lineup, I think the team would be a lot stronger.

Mr. RUSH. I have a few more moments on my time. Should wireless services be included on the bill for required disclosures or is that service somehow different because of the disclosures, when the consumer signs up for that service initially?

Mr. KOVACIC. Our serious concern is that if wireless is excluded, that that will become an attractive avenue to which wrongdoers migrate over time. We are seeing already in the course of our law enforcement that firms engaged in misconduct have identified this as a promising possibility and that that is where they will move their business in the future. My concern would be that this would be a seam through which the misconduct that the Committee is so wisely seeking to address would ultimately flow so that to eliminate that possible carve-out from the bill we think would be a useful thing for the Committee to consider and adopt.

Mr. RUSH. We have heard concerns that Federal law and State law could require different and even inconsistent disclosures on these pre-paid phone cards, all to fit on, as was indicated earlier, a small wallet-sized card. This could cause confusion for the industry and, even worse, for the consumer. Should we consider a nar-

row preemption of state requirements on specific disclosures for these cards?

Mr. KOVACIC. I think, as you and your colleagues have pointed out already this morning, the question of preemption is a difficult matter. There are unmistakably costs for business operators to have to respond to an array of different commands from both national and state regulators. At the same time, the states have often been a stimulus for providing ideas that I think have given great vitality to our system. It has often been the states that have provided the ideas that have moved us ahead, and in my conversations with my colleagues, I would say that my view, though I speak for myself in this capacity in speaking with our staff, I am not sure that we know enough about the likely effect of preemption in this specific instance to suggest that Congress adopt a measure that would achieve preemption. I would say that in approaching specific preemption measures, it would be very useful to study carefully how states, through their own policymaking, have contributed to the formulation and development of ideas that we now accept as being useful. To freeze in place any single solution runs the risk that the innovation that the states have provided would be forestalled. We would see this as a very important measure to be pursued, and of course, the bill itself does continue to provide dual enforcement at the state level and the federal level. That seems to be a consensus position within the Committee. We certainly endorse that part of the enforcement regime in the bill, too.

Mr. RUSH. Thank you. My time is up. The chair now recognizes the ranking member, Mr. Whitfield, for 5 minutes for questioning.

Mr. WHITFIELD. Thank you, Chairman Rush.

Mr. Chairman, you had mentioned that the FTC has engaged in litigation on this issue in at least a few cases. I was just curious. What is the maximum penalty that you can impose on a company that is found to have violated these fraudulent practices?

Mr. KOVACIC. We can achieve injunctive relief which tells firms to stop the misconduct. The other existing monetary penalty for most purposes that we can obtain is to seek the disgorgement of ill-gotten profits and, where possible, to return ill-gotten gains to consumers. In many instances, that is very difficult to do. It is hard to recover the funds. In some instances, it is hard to identify the precise amount of the funds that ought to be surrendered. We think that a very useful part of H.R. 3402 is that it would give us the ability to obtain civil penalties for each offense. It would allow us to achieve a much more powerful deterrent for individual offenses so that rather than being pressed to go through the expense of identifying the specific harm attributable to each specific violation, it would permit us, as Congress has allowed us in a number of other settings, to obtain civil penalties for individual offenses. I think that would be a very useful addition to the injunctive relief and the equitable relief in the form of disgorgement and restitution that we can now seek to pursue.

Mr. WHITFIELD. But as of this time, you have not been able to obtain disgorgement profits from any of these firms?

Mr. KOVACIC. We are seeking them in the matters that we have before us now. I would like to consult my memory better, if you permit, in our previous cases, to see if we actually obtained funds

that have been recovered for consumers. This is something we typically seek. We are seeking them in the cases that we have now.

Mr. WHITFIELD. One of the concerns expressed about this bill is the inability to go after a common carrier because you all do not have that jurisdiction. You did point out where unauthorized billing, you have been able to do that an so forth. But has the FCC been vigorous in trying to address this issue from your knowledge?

Mr. KOVACIC. I would say that they have an interest in this area. We have been the one who has been bringing the cases.

Mr. WHITFIELD. OK.

Mr. KOVACIC. That is, I think that whatever the combination of effort that would be provided, we are the ones who have had the most experience in the field. A difficulty I would mention in the two cases that I have referred to before is that already the defendants in those cases have raised the argument that the cases cannot be tried unless telecommunications carriers are joined in the action, that they are indispensable parties. We believe we will prevail in those arguments. We think their arguments are incorrect. They are being urged against us. Even in areas where we think we are not dealing with true common carrier exemptions, we have to spend a lot of resources in the routine execution of our business trying to deal with these specific matters.

So I would say even for the things where we think we are clearly on side, but as well for other areas where telecom services providers are involved, we think we have the wealth of experience. Unashamedly, we would say we are the experts in litigating these cases and devising the remedial scheme. That is why we would urge that we would be a useful addition to the mix, and in doing it, we would use all of the cooperation approaches we have used with other federal and state agencies in which we share jurisdiction to make sure we are not crossing wires.

Mr. WHITFIELD. So you support this legislation? You think the Federal Government should take steps in this area?

Mr. KOVACIC. Yes, sir.

Mr. WHITFIELD. But would you just quickly elaborate some suggested changes that you would make to this bill to make it more effective from your perspective?

Mr. KOVACIC. Very specifically, we would eliminate any indication in the bill that the FTC cannot enforce its provisions against common carriers.

Mr. WHITFIELD. OK.

Mr. KOVACIC. That is, we would seek to make absolutely clear that the Federal Trade Commission has authority to enforce the provisions of the bill with respect to any actor, be it a common carrier, be it a non-common carrier. That is our first recommendation. The second is that the bill now includes a knowledge standard that would require the FTC to show that alleged wrongdoers had actual knowledge of misconduct as a precondition for obtaining injunctive relief. I am only talking about relief that says stop the practice. And we would suggest that for injunctive relief that this provision be eliminated. The whole body of law that we enforce now dealing with deceitful advertising does not require us to show actual knowledge in order to get an injunction and say stop it. We have to show knowledge when it comes to getting money. That's a dif-

ferent issue. But with respect to obtaining injunctive relief, telling the firm whether you knew it was wrong or not—you have to stop the behavior because we can show that it involves misrepresentation—that requirement I think would hopefully be withdrawn from the bill.

The third is the matter that the chairman asked me about before and that is the treatment of prepaid wireless services. We think it is not healthy for the bill to leave that out. Why? That will become a gap through which those bent on misconduct will travel, that is, it will create an inviting opportunity for firms to move their business in the direction of wireless services so that we think to create the fence that we think the Committee is trying to build around the bad practices, that would be a hole in the fence and we suggest that you consider eliminating it.

Mr. WHITFIELD. My time has expired, Chairman.

Mr. RUSH. The chair thanks the gentleman. The chair recognizes the fine gentleman from Georgia, Mr. Barrow, for 5 minutes for questions.

Mr. BARROW. I thank the chair, and thank you, Mr. Chairman, for coming and testifying today. I certainly understand your point about wanting to eliminate the knowledge requirement as a precondition for getting injunctive relief. You know, where I come from we know that even a dog knows the difference between being kicked and being tripped over. So intent is important for some purposes.

Mr. KOVACIC. It certainly is.

Mr. BARROW. But if you are constantly getting tripped over, constantly, over and over and over again, you want to do something about that, too. It is not a matter of no consequence whatsoever. It seems to me also that if you bring the action, the knowledge requirement ought to be satisfied at least from that point forward. So I want to explore that issue a little bit further when circumstances permit. You might want to address that later on because while knowledge before you bring the action might be something that might be difficult to prove or might be missing. Once you bring the action, it seems to me that you have brought notice of the conduct to the fore and it is certainly out in the record now. So certainly there ought to be a basis for injunctive relief from that point forward at least.

But I want to return to the subject you made about trying to assess the situation the way things are working currently right now because in order to assess where we ought to go, we have to have a better understanding of how we are actually doing things. In other testimony, both today and elsewhere, you have made the point that your agency is working with the FCC, with Attorneys General, with other state agencies to try and divvy up responsibility for working with the patchwork of regulations and laws we have in place right now. I want to know, how are you all doing that? How are you dividing up these responsibilities in a way to avoid duplication of effort? How actually are you working with the existing patchwork of regulators and regulations? How do you all do that?

Mr. KOVACIC. If I can start, Congressman Barrow, just with a comment about the knowledge requirement. I think you and I

agree completely that if you have this recurring type of behavior and there is some notice from an enforcement agency or from some other source that this is considered to be improper, you can't smack yourself on the forehead afterwards and say, oh, my goodness, I had no idea.

Mr. BARROW. More importantly, you can't say from that point on, I don't know about it now so therefore there is no basis for a court telling me I can't continue to do this.

Mr. KOVACIC. Exactly right, and I think if we were to pull out the first year tort law framework of knowledge, reckless disregard, and lack of knowledge, we would say that this would easily be called reckless disregard and we would put it in the knowledge basket. We are also interested in cases in which people innocently transgress and those happen. But they have transgressed. They weren't aware of it, but they did. We would like in those instances as well to be able to go to a court and say, tell them to stop.

Mr. WHITFIELD. What I am saying, when you bring the action, though, you are serving them with notice——

Mr. KOVACIC. Yes.

Mr. WHITFIELD [continuing]. So they can argue they did not know about it before, but they can't say they don't know what's in the pleading.

Mr. KOVACIC. Quite so. Quite so. Just a——

Mr. WHITFIELD. The fact that they didn't know before is not a safe harbor for continuing to engage in this after you bring notice.

Mr. KOVACIC. No question. A couple of comments about the cooperation effort.

Mr. WHITFIELD. Right.

Mr. KOVACIC. One thing we do through the task force is to make sure that we are all aware of what the other party is doing so that in the first instance, we don't take action that would in some way frustrate or impede the completion of a useful investigation or enforcement matter that is now in progress. Second, where we can combine efforts, sometimes we carry out programs called sweeps where on a single day we will announce a bundle of enforcement matters that all of our agencies have pursued. We had one of these earlier this year involving telemarketing. The collective announcement of those matters can make a much bigger impact in imprinting on the minds of the public but in providing deterrents to wrongdoers, that a certain form of conduct will not be tolerated.

A third thing we can do and we pursue through this process is to see how we can improve any single enforcement action by sharing information, by reformulating the specific allegations that any one of us might have pursued so that we can identify instances in which a particular case or matter can be brought more effectively; and last, by sharing information that comes from our investigations we are able to identify patterns of conduct. It goes back to the point we were touching upon before about the importance of being able to identify complaints and patterns of misconduct as fast as we possibly can. If we pull the body of complaints that we all have and encourage the sharing of information, we are likely to be in the courtroom much faster than we would have been otherwise.

Mr. WHITFIELD. Do you rely on a consensus model within the task force to decide who is going to bring what action where? And

are there any instances where that consensus model is broken down? Were there turf disputes or disagreements about how best to proceed?

Mr. KOVACIC. I think there are always some instances in which tensions associated with organizations that have a great deal of pride in what they do, a great deal of confidence in their abilities that those tensions arise. We haven't seen them arise in a significant way in this instance, that is, this has been a very healthy form of collaboration. I think in many ways it is coming from the fact that we all see, given the resources that we have, that if we want to stand alone and try and address the relevant behavior in question, if we want to have an archipelago of public institutions that do not have good ferry service and that do not connect the individual islands in the archipelago, we are going to fail. I think that has created a perceived imperative to cooperate in ways that will achieve good, collective solutions. That is a very heartening side of a force that will perhaps overcome the impediments you described before.

Mr. WHITFIELD. Thank you, Mr. Chairman. Mr. Chairman, I yield back.

Mr. RUSH. The chair thanks the gentleman. The chair now recognizes the gentlelady from the great State of Illinois, the vice-chair of this subcommittee, Ms. Schakowsky, for 5 minutes of questioning.

Ms. SCHAKOWSKY. Thank you, Mr. Chairman. I am proud to represent a district that is incredibly diverse. In fact, almost a third of my constituents speak a language other than English. I think it is actually even more. At home, about 40 percent of the districts speak another language other than English. So all of them are calling to their home countries, and it is not just Spanish we are talking about, at my high schools, maybe 60 languages that are spoken.

So there is a very short section in your written testimony about consumer education and media outreach. So if you could tell me what the FCC has done and is doing and if it is realistic to think that these immigrant communities under current law at least are going to actually protest the problem.

Mr. KOVACIC. Let me mention a couple of things we are doing right now and a couple of things we are working on to deal with this phenomenon. We have taken in the case of Spanish language material, Spanish language speakers to begin producing our materials in Spanish as well as English. So we have begun to develop and we have now electronic and print versions of our brochures and our consumer alerts that are now in Spanish as well as English. This is part of the Spanish language initiative that we started about 5 years ago. Another is to make sure that our materials reach media that are most likely to reach the affected populations, that is——

Ms. SCHAKOWSKY. And what is the remedy that you are suggesting to them?

Mr. KOVACIC. First and foremost to be wise shoppers when they use the services. Second——

Ms. SCHAKOWSKY. What does that mean?

Mr. KOVACIC. To be very careful about representations, to look at what the merchants are saying they will do; and if they don't

do what they are supposed to do, to make readily accessible complaint communications links to us or to our counterparts. We have an excellent consumer response center where by phone and by Internet individuals can complain to us. The more complaints we get——

Ms. SCHAKOWSKY. But before purchasing, how does a consumer beware? If the card says 250 minutes, how do you beware before you purchase a card that it is going to do what it says it does?

Mr. KOVACIC. Some of the cards contain—in what is admittedly fine print that would probably defeat my prescription—some disclosures. And one step that we recommend is to go through the difficult and laborious process of actually looking at that card because if one has the patience to do it, and I am not saying that the disclosures they provide are adequate, by any means, Madam Vice-Chairman, but if one looks at the disclosures, one identifies that these cards have charges that will be imposed that dramatically diminish the value of the card. So one thing that we suggest is that people have the patience to look and see exactly what they are saying they will do. But because we regard those disclosures as being inadequate because they are often provided in fine print, one cannot reasonably be expected in the ordinary course to see them. What we regard as a critical strategy now is for consumers to tell us when they have been cheated, because we have greatly increased our ability from the time of the first complaint to the day we are in the courtroom to do something about it and again, by working with our counterparts at the state and local level, to learn what they are learning about patterns of misconduct as well and perhaps to formulate better education programs. Again, a thing we are doing looking ahead is we are expanding our program to work with community groups that work with especially disadvantaged communities, non-English speakers, immigrant communities, that ordinarily are not going to pay a great deal of attention——

Ms. SCHAKOWSKY. How many complaints do you get and have you seen them increase as a result of your educational outreach efforts?

Mr. KOVACIC. It is hard for me to link them to the outreach efforts themselves, but something we are asking as part of this effort is how do we measure the effectiveness of the outreach programs.

Ms. SCHAKOWSKY. Well, how many complaints do you get?

Mr. KOVACIC. I would say this year, and I can check this for the record, I think in this calendar year we received several hundred, probably on the order of 500 or 600 complaints. I can get you a more specific accounting of that but that is something we regard as a lot of complaints.

Ms. SCHAKOWSKY. And how many were from Spanish language as a result of your Spanish language outreach?

Mr. KOVACIC. I don't know offhand but I can check that for you.

Ms. SCHAKOWSKY. I would be interested in that, and certainly would encourage that you do outreach in other languages as well. I can't see the time. Am I out of time? OK. Thank you.

Mr. KOVACIC. And I think that is an excellent suggestion for us, and I think to take the Hispanic language program and to use that as a template for building out in other directions would be very helpful.

Ms. SCHAKOWSKY. Well, make sure that it is working, too.

Mr. KOVACIC. Absolutely. I think the assessment of actual effects is very important. My general impression of the Hispanic language program is that when we look in all areas in which we have been active, many of the cases we have been bringing are directly related to the pursuit of that program.

Mr. RUSH. The chair asks for unanimous consent to recognize the author of the legislation, who is a member of the full committee but not a member of the subcommittee, Mr. Engel. The specific unanimous consent request is that Mr. Engel be allowed 5 minutes for questioning. Is there any objection? Hearing none, Mr. Engel is recognized for 5 minutes of questioning.

OPENING STATEMENT OF HON. ELIOT L. ENGEL, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW YORK

Mr. ENGEL. Thank you very much, Mr. Chairman, and I want to just say how very happy I am to see you back here leading this panel. It is good to see you, and we are delighted you are feeling so much better. Thank you for holding this hearing on my legislation, H.R. 3402 which for all the reasons that everyone has said on both sides of the aisle is important legislation. I want to also say hello to my friend, the chairman of the FTC. He and I testified before the Senate Committee on this bill last week, and I think it is fair to say that we are really in sync.

I just want to tell you that the suggestions that you have made for changing the bill I have no real objections to. My concern would be passing this bill identically in both houses and get it signed by the end of the session which is only obviously 2 weeks more. And my only concern would be that if we start complicating it by changing it, it may imperil the passage of it and the signing of it because I wouldn't want it to wait another year until the new Congress and then we are just way behind. So I was just wondering if you could comment on that because that is a major concern of mine. And again, not that I objected to anything that you said because I think you want to strengthen the bill and so do I, and the bill is not identical with the Senate bill, although it is very, very similar. And I do agree with Senator Nelson, who is the sponsor of the bill in the Senate. We all want the same thing. I just don't want it to get embroiled in what always happens in Congress and we wind up not getting it done because we have been too busy crossing every T and dotting every I.

Mr. KOVACIC. I think you know better than I that some of our greatest legislative achievements have come from incremental improvements and that waiting for the perfect complete bill is sometimes the equivalent of waiting forever. So I would never discourage you from—I would respect your judgments about the appropriate balance between pursuing the greater complexity and making the changes and having the simpler text that could be adopted. I would only suggest, Congressman Engel, and thank you for your question on this, that with respect to the specific matters that I had in mind that those involve very modest drafting adjustments and that those could be accomplished with I think a great measure of simplicity. Those who think my ideas are wrong-headed would

probably say they could only be achieved with enormous complexity, impossible complexity. But I think they do involve, a slogan I will use, precise surgical adjustments that would not damage the healthy tissue at all but would leave the body of the bill in much better shape.

Mr. ENGEL. Well, thank you. I am glad to hear you say that because I think that is certainly something with which we all agree. Mr. Chairman, I would like to ask unanimous consent to have my opening statement entered into the record.

Mr. RUSH. Granted.

Mr. ENGEL. Thank you. And I just want to highlight some of the things I know that has been said here. But I introduced this bill because some of my constituents had been complaining to me, and then I went and purchased my own card and found that everything they said was true. If a company advertises that they give 60 minutes of time for calls, the consumer has a right to believe when he or she purchases the card that they are getting the full 60 minutes. When they don't, because there are so many hidden clauses where it can take away three or four units just for a connection fee, even if the line is busy or somebody hangs up or the card expires 2 months after it is used or there is more charging for peak hours and the only hours that are not peak are from 2:00 a.m. to 4:00 a.m., or as Ms. Schakowsky points out, things are done in a language—they may be marketed, for instance, in Spanish but then clauses on the card are in English and the person obviously cannot understand it and it is marketed in poor communities, this should not happen. And the other point I want to raise as well is that it undermines legitimate companies who are legitimately issuing these cards and legitimately give 30 or 60 minutes of time because the card of the dishonest company appears to be cheaper and the consumer will buy that card thinking they can save a dollar or two when in reality that card is much more expensive because if you are paying $1 less but you are getting only half the time, it is actually a more expensive card.

So these are the things that we have found from time to time, and I just hope we can pass this in this Congress, have the Senate do it as well, and have the President sign it. Thank you very much, Mr. Chairman, for letting me speak at this subcommittee.

Mr. RUSH. The gentleman is quite welcome. The chair is going to entertain the unanimous consent request from the ranking member for one additional question. Are there any objections? Hearing none, the chair recognizes the ranking member for an additional question.

Mr. WHITFIELD. Mr. Chairman, thank you very much and this won't take but a minute. Mr. Chairman, in the technical comments of the Federal Trade Commission to this legislation, you specifically asked for rule-making authority, provide more flexibility, and so forth. My question would be with that rule-making authority, would that reduce your concern about a strong federal preemption standard because you are dealing with the states on a regular basis anyway, and if they come forth with some way to better protect against consumer fraud, wouldn't this rulemaking authority diminish your objection to a federal preemption standard?

Mr. KOVACIC. I think it does help, Representative Whitfield. I think it does help because that interaction is likely to continue. I would say that one thing that is also often informative to us in the rulemaking process is to see that an experiment has been tested and has worked elsewhere. And the experiment often involves a state measure to actually apply a specific standard and come back to us and say, you don't have to take the idea on faith alone. We have got some data to show that it works. I would certainly count on the states to be bringing us their ideas. But I would also say that some of the best ideas they bring us comes from actually having tested something on their own, which is why I hesitate to jump in the direction of thinking complete preemption would be right. It is a consideration that I ask you to consider.

Mr. WHITFIELD. Thank you.

Mr. RUSH. Thank you. The chair thanks the chairman, Mr. Kovacic, for your fine testimony. We certainly will take your statements to heart in the markup this afternoon, and if you have any additional insights or any additions to your testimony, would you please provide them to the chair as quickly as you can? We intend to go to markup this afternoon. Thank you very much, and you are dismissed.

Mr. KOVACIC. Thank you very much again for the opportunity to be here, and I look forward to many, many more. Thank you, Mr. Chairman.

Mr. RUSH. I think excused is a better word. The chair now invites the second panel to appear to take a seat at the witness table. The witnesses on the second panel, we welcome you before this subcommittee.

I am going to introduce the witnesses from my left to right, and the first witness is Ms. Sally Greenberg. She is Executive Director of the National Consumers League. She has testified before this committee before in a different capacity, so I hope this is a promotion that you received, and welcome again. The National Consumers League is the oldest consumer organization in the United States. It is active in the area of consumer financial fraud and operates a national fraud center.

Our second witness is Ms. Yvette Zaragoza, Small Business Manager for the Latino Economic Development Corporation. Ms. Zaragoza has personal knowledge of the pre-paid calling business, both as an active user of the cards and as a former business manager for a phone card wholesaler. Ms. Zaragoza should not be under the burden of identifying the company that she used to work for, and I admonish all members to not try to pinpoint through her testimony the name of the company that she worked for.

Next witness is Dr. Julia Marlowe, who is Professor Emeritus for the University of Georgia, another fine Georgian. Dr. Marlowe is an academic with a background in consumer economics and has done research and published articles on deceptive marketing of prepaid calling cards.

And last but not least, Mr. John Eichberger, who is the Vice-President of Government Relations for the National Association of Convenience Stores. The National Association of Convenience Stores is an international trade organization representing the convenience store industry. Many retail outlets are major sellers of

pre-paid calling cards worth $350 million in sales of the cards in the year 2007.

Again, we welcome you. We will ask that you restrict your opening statements to 5 minutes, and we will begin the opening statements with Ms. Greenberg. Ms. Greenberg, you have 5 minutes.

STATEMENT OF SALLY GREENBERG, EXECUTIVE DIRECTOR, NATIONAL CONSUMERS LEAGUE

Ms. GREENBERG. Thank you, Mr. Chairman, and I really appreciate the opportunity to be here today representing the National Consumers League.

This area of pre-paid calling cards is what we have described in testimony as a really wild west of sellers and merchants who too often prey upon the most vulnerable consumers, consumers who are promised minutes that are not redelivered. They are loaded with hidden fees and charges, undisclosed charges, that not even a savvy consumer—I consider myself one of them, a savvy consumer. I use these cards, and I have no idea what kind of value I am going to get from them. I picked up a few from my gas station yesterday, and I know that when I use those cards I am not going to get the value that I expect, and I think many consumers have gotten accustomed to not getting the value that they expect.

I want to commend Congressman Engel and other sponsors of the bill for the leadership in offering H.R. 3402, the Calling Card Protection Act of 2008. Consumers rely on all of you as outspoken defenders of consumers' rights and protections to look out for their interests.

This is an industry that is notorious for shady practices, so much so that the writers of The Sopranos, the HBO series, had Tony Soprano discussing how to defraud consumers through the sale of prepaid calling cards. In episode 26, Tony Soprano says, so, telecommunications once again fails to disappoint. What is this thing? Telephone calling cards. You find a front man who can get a line of credit, you buy a couple million units of calling time from a carrier. You become Acme Telephone Card Company. Then he laughs. Acme. Now you are in the business of selling prepaid calling cards. Immigrants especially, no offense. They are always calling back home to whoever, word deleted, and it is expensive, right? You sell thousands of these cards to the, word deleted, cards at a cut rate, but you bought the bulk time on credit, remember? The carrier gets stiffed, he cuts off the service to the cardholders but you already sold all your cards. That is, word deleted, beautiful, laughing. It is a good one.

Now, we aren't suggesting the pre-paid calling card industry is controlled by organized crime. We have no such evidence. But this vignette from The Sopranos demonstrates how easy it is to get into the industry, rip off consumers, and disappear with no accountability whatsoever. And that must change. This is a $6 billion industry. Those are the projected revenues for 2008. The average calling card delivers only 60 percent of the minutes promised with hang-up fees, periodic maintenance fees, destination charges, and high billing increments. Lax enforcement and rapid growth from the industry has enabled consumer fraud to flourish, and the most frequent victims are the most vulnerable consumers, immigrants,

the working poor, students, military families, and those lower-income Americans who either can't afford or obtain regular phone service. They rely on these cards to stay in touch with family and loved ones.

Yes, the cards provide users with an alternative means of calling home, but they use false and deceptive practices in the process. Fraud is fraud. If a car is sold with the promise of a sun roof and chrome wheels, it better have a sun roof and chrome wheels. If a phone card promises 500 minutes to call El Salvador, it should deliver those 500 minutes.

So we support H.R. 3402's requirement that pre-paid calling card providers and distributors disclose the terms and conditions of the cards, including per-minute rates, preferred international destinations, and any fees or surcharges in its advertising.

Transparency and full disclosure would help to level the playing field. With all these rules in place, I think we would have a minimum floor of requirements stating what practices won't be permitted. But we also support strongly H.R. 3402's preservation of the right of individual states to provide further protection for their residents. That provision acknowledges that states have been the incubators for groundbreaking legislation. NCL recommends that once this legislation is enacted, and I do hope it will be marked up by the House and passed before Congress goes out, within some period of time, perhaps a year, we recommend that the FTC report to Congress whether full disclosure is actually working or more needs to be done to protect consumers.

Many of the fees and charges on these cards we believe are unconscionable. The text and the fine print on the back of my Africa Sky card says, all the following fees will reduce the number of available minutes: use of a toll-free number from a pay phone, incur 99 cents per calling fee. Some of these cards are $2 cards. You take a 99 cent fee out, it is gone, and I use them, as I said, myself all the time and find that I don't get the value that I am looking for.

I have also had the experience of using these cards in other countries. I lived in Australia for a year. The cards there actually deliver the value. They don't have connection fees, they are not loaded on with a bunch of other fees. Consumers have no real way of predicting. So we like the bill, I think there is a lot in here that will be really useful to consumers. I think certainly we should extend the additional jurisdiction to the FTC, but I am just not convinced that disclosure is enough. It is a minefield out there. I think we really have to crack down on this industry, and I, even what I regard as quite a savvy consumer, I have no idea what I am getting from any of these cards. So this industry needs to be cleaned up. Thank you very much, Mr. Chairman. I appreciate being here.

[The prepared statement of Ms. Greenberg follows:]

Testimony of
Sally Greenberg, Executive Director, National Consumers League
Before the U.S. House Energy and Commerce Committee
on HR 3402, the "Calling Card Consumer Protection Act"

September 16, 2008

Introduction

Good morning, Mr. Chairman. My name is Sally Greenberg and I am Executive Director of the National Consumers League. I appreciate this opportunity to appear before the House Committee on Energy and Commerce to discuss the need for greater consumer protections in the purchase and use of prepaid calling cards. This largely unregulated consumer product is a "Wild West" of sellers and merchants who too often prey upon the most vulnerable consumers by promising minutes they don't deliver and loading up on hidden or undisclosed charges and fees. In an industry like this, with low barriers to entry and a totally unregulated market, you can be sure there will be unscrupulous operators who will take the money and run.

The National Consumers League, whose founding in 1899 makes us the oldest consumer organization in the United States, has a longstanding interest in protecting consumers from fraudulent practices and is the only consumer group that operates a national fraud center. (The NCL's Fraud Center is described at www.fraud.org).

I want to commend members of this Committee for giving scrutiny and attention to the issue of prepaid calling cards and to Congressman Engel for offering HR 3402, the "Calling Card Consumer Protection Act." Consumers rely on this committee to defend consumer rights and protections and to look out for consumers' interest. I will address some of the facts and figures describing the magnitude of the prepaid calling card industry and the large amounts of money involved. I'll discuss the fraud and deceptive practices associated with that industry and actions taken at the state and federal levels in response to fraud. I'll discuss why NCL supports the Engel bill, and I'll make some policy recommendations. Our written testimony also includes a timeline detailing the growth of the industry and the rise in fraud associated with that growth.

Let's start with the industry. It is illustrative that the shady practices of the prepaid calling industry were featured prominently on the HBO series, *The Sopranos*. In Episode 26, Tony is discussing the mob's work with prepaid cards. I've deleted the obscenities:

Tony Soprano: "So, telecommunications once again fails to disappoint. What's this thing? Telephone calling cards. You find a front man who can get a line of credit, you buy a couple of million units of calling time from a carrier. You become "acme telephone card company". "Acme". You're now in the business of selling prepaid calling cards. Immigrants especially, no offense. They're always calling back home to whoever (deleted) And it's expensive, right? You sell thousands of these cards to the (deleted), cards at a cut rate. But you bought the bulk time on credit, remember? The carrier gets stiffed. He cuts off the service to the card holders, but you already sold all your cards. That's (deleted) beautiful! (Laughing) it's a good one."

Of course, we're not suggesting that the whole prepaid calling card industry is controlled by organized crime: we have no such evidence, but this vignette from *The Sopranos* demonstrates how easy it is to get into the industry, rip off consumers, and disappear with no accountability whatsoever. That must change.

Prepaid Calling Card Facts

- Prepaid cards are a $4 billion a year industry, responsible for 11 billion calls in 2004[1]
- The industry is estimated to reach $6.4 billion in revenue in 2008.[2]
- Examples of fraudulent practices used by the prepaid companies include "hang-up fees," periodic maintenance fees, destination surcharges, and high billing increments.[5]
- Companies that try to "play by the rules" are often punished by a loss of market share due to fraudulent carriers.[6]
- Only 11 states, including California, Connecticut, Florida, and Illinois, currently have laws pertaining to calling card fraud, specifically. Most turn to generic consumer protection statutes, but enforcement has been extremely light.[7]
- Hispanic consumers may be losing up to $1 million per day because of fraudulent phone cards.[4]
- The average calling card delivers only 60% of the minutes promised, according to the Hispanic Institute, a non-profit research group.[3]
- The Federal Trade Commission's (FTC) survey of prepaid calling cards confirms the

Hispanic Institute's findings. For instance, one calling card tested by the FTC claimed to offer 360 minutes to Panama, but only delivered 23 minutes of calling time. The FTC said that in 87 tests of the prepaid cards, the cards delivered an average of only 50 percent of the advertised minutes.[8]

- The cost-per-minute rates for prepaid phone cards can be up to 87 percent higher than expected. An expected call rate of 15 cents per minute, for example, may end up costing 28 cents per minute.[9]

Customer service representatives for prepaid calling cards are often unavailable or not knowledgeable regarding the prepaid phone cards their employers are selling. A 2005 University of Georgia study found that in a third of the calls to prepaid calling card customer service lines, callers couldn't reach a representative. When they did make contact, the representative often was unable to answer basic questions about fees or rounding up of minutes.[10]

Why We Need To Protect Users of Prepaid Calling Cards

The rapid growth of the prepaid calling card industry combined with, until recently, a lax enforcement of consumer protection statues at the state and federal levels, has enabled consumer fraud to flourish. Like so many other scams, the most frequent victims of the fraud and deception are the most vulnerable consumers: immigrants and the working poor; and those lower income Americans who often cannot afford or obtain regular phone service. These consumers rely on calling cards to stay in touch with friends and loved ones in the US and abroad. Sadly, we believe that military families are also likely victims of the prepaid card scams and rip-offs.

Yes, the cards provide these users with an alternative means of calling home, but many use false and deceptive practices in the process, and impose unconscionable terms. Fraud is fraud—if an automobile is sold with the promise of a sun roof and chrome wheels, it better have a sunroof and chrome wheels—if a phone card promises 500 minutes to call El Salvador, it should deliver those 500 minutes.

Some state attorneys general –have done a commendable job in prosecuting fraudulent prepaid card companies, including in Florida and Texas. The Federal Trade Commission has also conducted investigations and brought important cases against individual prepaid phone card

providers. Unfortunately, these scattered efforts are insufficient. We need basic federal protections to stem the tide of the many deceptive practices in this industry.

NCL believes that giving the FTC greater authority, as called for in HR 3402 would help to level the playing field for all phone card providers. Such regulations include requirements that prepaid phone card providers and distributors disclose the terms and conditions of the cards, and list the per minute rates, preferred international destination rates, and any fees or surcharges, in their advertising,

We need a national floor of minimum requirements stating what industry practices won't be permitted. We applaud HR 3402's provisions preserving the rights of states to go forward with their own civil cases—as Florida did. The federal government should set minimum standards and permit states to go forward with provisions that don't conflict with the federal law. That's a pro-consumer position and acknowledges the important role states have played in enacting and enforcing consumer protections. But we also recommend that Section 7 in HR 3402 acknowledge and support the ability of state utility commissioners or other authorized state consumer protection agencies to look into the practices of the prepaid calling card industry.

NCL believes that both the House bill, HR 3402, and Senator Bill Nelson's bill, S. 2998, on prepaid calling cards, would go far in addressing the false promises and deception associated with these cards. In regard to unlawful conduct described in Section (b)(2) of HR 3402, we suggested the language be expanded to say not just "distribute" but includes those who *sell, resell, issue* as well as distribute the cards. Anecdotal evidence suggests that the simple threat of regulation has already increased pressure on the prepaid calling card industry to reform its marketing practices.[12] We've also seen evidence through the IDT settlement in Florida that if one company is forced to disclose accurately how many minutes a card will provide and what the surcharges and fees will be, they will lose market share to the other firms who are shading the truth. Therefore, we need to create a level playing field where all participants are required to provide accurate information.

Beyond Disclosure: What More Can We Do To Protect Consumers

While NCL supports efforts requiring require full disclosure of terms and conditions on these prepaid calling cards, we find that the terms themselves, when they are disclosed, are too often

unconscionable.

For example, the text in fine print on the back of my $5.00 "Africa Sky" card states the following:

> *All of the following fees will reduce the number of available minutes and the value of the card. Use of a toll free number from a pay phone will incur a $.99 per call fee. Per minute rate will be .02 higher for calls placed using toll free access numbers. Call time for multiple calls is calculated by rounding the last minute up to the closest multiple of 3 and then adding 1 minute except that if your call lasts less than 1 minute you will be charged only for a minute. If available minutes are not all used up on the first call the following fees will apply (1) the multiple call rate will be 40% higher and will apply to all calls (see poster for details) (2) a fee per call of $.59 will apply to each call; and 3) on midnight after the first call a fee of $.69 will be deducted and then weekly thereafter. Card Expires Three Months After First Use. . . Rates and Fees are Introductory and are subject to change anytime. . . .*

The same or similar text is found on most of the cards. So, though we have the terms disclosed, albeit in fine print, we have a company that is rapidly subtracting money from the user's original purchase. A 40% higher rate is imposed after the first call; a fee of 59 cents per call will apply to each one after the first call; and after midnight of the first call, the fee is 69 cents, which will be deducted weekly thereafter. This is from an original $5.00 card. No wonder users find that two or three weeks—or sooner—after first use, the card has no credit remaining. Notice the card also contains this catch-all phrase "*Rates and Fees are Introductory and are subject to change anytime...*" leaving the card distributors the option of changing the rules whenever they wish.

Worse still is the "Majestic DMV" Card I purchased for $2.00:

> 1) *A .99 fee applies on the 1st day of use and every 5 days thereafter; 2) Calls made through toll free access numbers are subject to a fee of up to 4 cents a minute 3) payphone surcharge of .99 4) A destination surcharge of between 20-60% of the total call; and/or 5) a fee of .10-.99 for connected calls, .15/minute maximum domestic call rate (before applicable charges and fees); minutes and/or seconds are billed at a minimum of one minute and up to 5 minute increments, plus any applicable fees. Card*

expires 3 months after first use or 12 months after activation.

As a consumer advocate, I've often found it useful to look at consumer protection measures in other countries. I lived in Australia two years ago and used prepaid cards for calls to the United States. My experience was uniformly positive—the Australian prepaid cards tended to deliver the minutes they promise, and they were good for multiple uses. *Choice Magazine*, Australia's counterpart to our *Consumer Reports*, tested these international calling cards and found that indeed, many delivered good value and low rates without connection fees or added charges. When I arrived back in the United States and began buying cards here, I found that their value tended to disappear after the first call. When I read the fine print, I understood why.

I also consulted the document *Consumer Protection in the European Union—Ten Basic Principles*—and note that the Fifth Principle is relevant to our discussion of prepaid calling cards:

> *Contracts Should Be Fair To Consumers*
> *Have you ever signed a contract without reading all the small print? What if the small print says the deposit you just paid is non-refundable – even if the company fails to deliver its side of the bargain? What if it says you cannot cancel the contract unless you pay the company an extortionate amount in compensation? EU law says these types of unfair contract terms are prohibited. Irrespective of which EU country you sign such a contract in, EU law protects you from these sorts of abuses.*

We could apply the EU's notion of contract fairness to this issue. NCL supports HR 3402 disclosure requirements and hopes that they will satisfactorily address the problem of consumers paying good money for a prepaid calling card that fails to deliver the service. An open marketplace where all prepaid calling card companies are providing accurate information may do the trick; the market has a way of working very effectively consumers have accurate information upon which to compare rates.

NCL would like to suggest, however, that after passage of your bill, the FTC closely monitor the industry and in a year's time, report on whether disclosure is addressing the problem adequately.

The Greek Diogenes called the market "a place set apart where men can deceive each other." We must impose some limits on that paradigm. If after a year we still see failure to accurately disclose rates and unconscionable terms when the rates are disclosed, we would urge this Committee to consider stronger regulation of this industry.

NCL Policy Recommendations Related to Disclosure and HR 3402

The National Consumers League strongly supports HR 3402 and its provisions to give enforcement authority to the Federal Trade Commission under the "unfair or deceptive act or practice," clauses of the Federal Trade Commission Act. While prepaid calling cards generally offer savings on international long distance calling versus traditional "Dial 1," 10-10 dial-around and wireless long distance calling,[13] these savings are no excuse for fraud or deception.

We also support FTC's call to appoint a monitor to oversee the prepaid calling card business,[14] and a requirement that the FTC report back to Congress on a periodic basis regarding the status of its efforts to enforce the terms of the proposed legislation.

As a general proposition, we applaud the requirements included in the Florida Attorney General's June 2008 settlement with prepaid card companies, such as:

- Ceasing all deceptive advertising
- Providing 100% of the minutes advertised
- Not using hidden fees or misleading minute calculations to increase their profits at consumers' expense
- Printing disclosures for a given card in any language used to advertise that card
- Printing the exact number of minutes available and the card's expiration date (if applicable) on the card
- Prohibiting naming of card surcharges to resemble taxes
- Requiring one-minute increment billing

While HR 3402 requires disclosure of the name of the prepaid calling card service provider, we recommend that this section of the bill be expanded to include requiring the address of card originator and a toll free number, and that operators answering the phone be able to speak the language in which the card was advertised. The requisite disclosures should be in the same language. We also support requiring that the disclosure text on the calling card itself, packaging,

or other promotional material (including online) be in same language used to advertise the card.

Further Recommended Action If Disclosure Requirements Are Not Sufficient

If after one year, the FTC reports back to Congress with evidence indicating that greater disclosure is not reducing the consumer abuses in the industry, we recommend that further action be considered by this Committee, with the Federal Trade Commission given the authority to enforce these provisions:

- Require all market entrants to be licensed and post a bond before marketing cards to consumers. That bond would go into a fund to compensate consumers who are victims of fraud. Those companies that market prepaid calling cards should also be required to provide a name, address and place of incorporation. Right now, the barriers to entry are so low and the penalties for not making good on the value of the cards are so minimal that it's simply open season on consumers. We believe requiring a bond will act to keep many bad actors out of the industry.
- Require all market entrants to have a 24 hour, 7 days a week toll free number that has a live person on the other end who must be knowledgeable about the use of the card.
- Require that fees and surcharges imposed be related to actual costs. Congress has imposed rules on other industries that were charging consumers outrageous fees – the moving van industry, payday lenders, and funeral homes, to name a few. If, in a year's time, this Committee finds that disclosure is not easing the deception and rip-offs that plague this industry, the Committee should consider imposing stronger regulations on prepaid calling card companies and the many fees and surcharges they impose on consumers.
- Require that all cards have an expiration date and that this date be no shorter than one year after activation. If a seller fails to make a disclosure on expiration, the card should be valid indefinitely.
- Require sellers to list the minimum charge per call and the balance in minutes and dollars remaining on the card.
- Require sellers to inform consumers, via a website or toll-free phone number, of any proposed changes in terms and conditions, with consumers given the chance to reject these changes and receive a refund on the card with no fee imposed for requesting such a refund within an appropriate grace period of no less than 30 days after posting of the proposed change. Prepaid calling card providers should also be required to prominently list a

mailing address to which customers can direct refund requests and/or a website with a refund form that the consumer can access easily.

- Require uniform terms in all prepaid calling card contracts so that consumers can comparison shop. Companies should not be allowed to confuse consumers by using a variety of terms for charges such as "administrative fee" or "service fee."
- The amounts involved in prepaid phone card transactions are too small for any one individual to bring a case to court. The only meaningful way to allow consumers to hold prepaid card sellers accountable is through use of the class action process. Consumers need to be guaranteed a private right of action and the ability to band together as a class to bring cases against dishonest prepaid phone card providers.

Conclusion

We strongly support HR 3402 and commend this Committee for holding the hearing today. By requiring much better disclosure on prepaid calling cards, this bill will help to mitigate the deception and fraud associated with these cards. We also support further monitoring of the industry by the FTC, which will in turn report to the members of this Committee.

NCL also urges Congress to find a way to require that prepaid calling card companies go beyond simple disclosure of their onerous rates. The most vulnerable consumers—military families, immigrants, low income families —rely on these cards and spend their hard-earned money only to see the value of the cards disappear quickly after first use. NCL believes we can do better by consumers. We support the disclosure required under this bill and hope that it works. If we need to take stronger action, this bill's requirements will represent an excellent first step.

Thank you, Mr. Chairman, for giving the National Consumers League this opportunity to comment on your bill. We commend you for your pro-consumer record and look forward to working with you and your staff to see this bill enacted into law.

Issue Timeline

We have provided a timeline of enforcement actions and legal settlements pertaining to prepaid calling cards below.

1986	Prepaid calling cards introduced to the North American market.[15]
1996	U.S. prepaid card sales reach $1.1 billion[16]
April 2001	New York Attorney General Eliot Spitzer announces settlement with five companies accused of deceptively marketing prepaid telephone cards throughout upstate New York. This settlement was part of Spitzer's ongoing efforts to combat illegal marketing practices of prepaid phone card companies dating back to 1999.[17]
2006	Newark, NJ-based IDT Corp., the largest prepaid calling card company in the U.S. reports $2.2 billion in total sales.[18]
2007	U.S. prepaid market reaches $4 billion in revenue
January 2007	IDT Corp. settles federal class action suit brought on behalf of hundreds of phone card customers alleging fraudulent and deceptive advertising practices.[19]
March 2007	IDT files lawsuit against 9 competitors, alleging that they provide 40% less time than advertised. Epana Networks, Dollar Phone, and Locus Telecommunications quickly reach settlement with IDT, agreeing to cease any misleading marketing practices. Six other companies named in the suit, including CVT Prepaid Solutions Inc. issue an open letter to the industry, claiming that IDT's suit is "nothing but an underhanded ploy to regain lost market share by intimidation."[20]
July 2007	Florida Attorney General Bill McCollum announces investigation of 10 prepaid

calling card companies for fraudulent or deceptive advertising.[21]

August 2007 Representative Eliot Engel (D-NY) introduces H.R. 3402 "Calling Card Consumer Protection Act."[22]

March 2008 FTC asks U.S. District Court for the District of New Jersey to halt allegedly illegal marketing practices of prepaid card companies CTA Inc., Clifton Telecard Alliance One LLC, and Mustafa Qattous.[23]

May 8, 2008 Senator Bill Nelson (D-FL) introduces S. 2998 "Prepaid Calling Card Consumer Protection Act of 2008."[24]

May 23, 2008 Texas Attorney General Greg Abbott announces filing of legal enforcement action against prepaid calling card company Next-G Communications, Inc. over allegedly deceptive marketing practices employed by the company.[25]

Footnotes

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[22] U.S. House. 110th Congress, 1st session. *H.R. 3402, Calling Card Consumer Protection Act*. ONLINE. Thomas.gov. Available at http://www.thomas.gov/cgi-bin/bdquery/z?d110:HR03402:@@@L&summ2=m& [Retrieved on July 25, 2008].
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Mr. RUSH. Ms. Zaragoza, you have 5 minutes.

STATEMENT OF YVETTE ZARAGOZA, SMALL BUSINESS PROGRAM MANAGER, LATINO ECONOMIC DEVELOPMENT CORPORATION

Ms. ZARAGOZA. Good morning, Mr. Chairman, and thank you very much for the opportunity to support this bill.

In my previous place of employment I was a business manager, and we bought pre-paid cards from distributors and sold them to more than 100 convenience stores, retail stores, Laundromats, music places. Ninety percent of them, more than 90 percent of them, were owned by Latino or immigrants; and the majority of them that were located in what you would consider lower-income neighborhoods. So I am here to provide an insight on the field, the reality of the field, which is very complex and pretty different from any other industry.

So part of my duties as a business manager was to handle complaints from end consumers and from the small businesses every month. I would visit stores, maybe 10 to 15 stores every week. And part of our role was to educate end consumers and also business owners on the rules of the game, so to speak, because there are several good companies in the industry, and we know specifically who those companies are. But there are other bad companies. As Mrs. Greenberg said, they tend to appear and disappear without any notice. So the way it works basically is that a card will be launched with the introductory fees. It would be heavily advertised in Latino or Spanish-speaking TV or radio shows and also posters, the big posters. And after a while, this is a word-of-mouth business. People tend to speak to each other and they recommend each other the cards. So at the beginning they offer what they promise, but then when they are at the peak of their demand, basically, then we know that that is when the cards will start having hidden fees. They will lower their minutes. So that is when they really make all their money, the distributors.

So most of the consumers can't really keep up with that, even savvy consumers. They sort of wait and some of them know what is the process, but most of them really don't and they get ripped off. And many times just the channel for complaint is so burdensome because for a $2 card, for example, the convenience store probably was sold the card at 1.56 and then probably the wholesaler was sold the card at 1.52. So sometimes it is not even worth claiming or putting a claim on the calling card. Some retail stores would take the card and some of them wouldn't, but then the end result is that the distributors never lose. They never lose the money. They never give credit.

So I think I outlined in my written testimony some of the suggestions which included stop the use of deceptive marketing practices, disclosure of terms and fees, and then use of the Spanish language for the fine print. Why? Because from the 200 or 300 cards that the wholesaler would manage at any given moment, which could be up to 500, they are all different. They all have their own cycle. And you know exactly which ones are for Africa, which ones are for Latin American countries. So I think the issue that was brought up about languages, I think you can really do it because some of

them would be specially in French, some of them would be specifically in Spanish.

Then of course, compliance with advertised minutes and stop using the hidden fees. But then one thing that I think would work pretty well is to register each brand of pre-paid calling card and have that company be accountable. Some of them sometimes don't even print the name of the company.

So that would be all, and thank you very much for your attention.

[The prepared statement of Ms. Zaragoza follows:]

STATEMENT OF YVETTE ZARAGOZA

Good Morning, Mr. Chairman.

My name is Yvette Zaragoza and I am a Small Business Program Manager at the Latino Economic Development Corporation. I would like to thank you for the opportunity to give testimony in favor of more regulation of the calling card industry before the House subcommittee on Commerce, Trade and Consumer Protection, because this is a real problem affecting the Latino community in the Washington, DC metropolitan area. My testimony will be based on my inside knowledge of the industry through my previous job as well as my personal experience.

In my previous place of employment, I was a Business Manager for a phone card wholesale company in the metropolitan area. We bought prepaid phone cards from distributors and sold them to more than 100 mini-markets, neighborhood stores, and convenience stores in Maryland, District of Columbia, and Virginia. At least 95% of the businesses were owned by Latinos and other minority groups; the majority of them were located in low-income neighborhoods and their customers represented a wide range of nationalities, mostly recent immigrants.

The reality in the field is very complex and pretty different from any other industry. The target market for prepaid calling cards is composed by some of the most vulnerable consumer groups, including low-income workers and non-English speakers. The marketing efforts are directed to this target market in Spanish but vital information, such as the terms and conditions of use, are disclosed in English. When using the calling cards, customers face hidden fees, rounding the time up to four minutes, and a lower number of minutes than those advertised or even mentioned by the phone card operator system before making the connection. Roughly half of the cards sold have a face value of $2, making it almost worthless for the customer to spend 10 to 15 minutes to talk to a customer representative of the company, if they can reach them. Even if it was worth the time, there are no clear channels to place formal complaints and no reason for the customer to believe their complaint will be heard.

As a Business Manager of the wholesale company, I received numerous complaints from end customers and business owners every month. Part of our role as responsible wholesalers was to give small business owners an insight on the "rules of the game" in the industry, and educate the end customers on the "good" and "bad" cards in the industry, which changed from month to month, or sometimes from week to week.

On one hand, there are several "good" companies in the business. They launch prepaid calling cards that offer a reasonable number of minutes for the money. They charge small or no connection fees and when the customer makes the phone call, the connection is pretty good, and therefore, they can talk for the time that was advertised. Most of these companies have been in the industry for many years.

On the other hand, the "bad" companies usually offer "introductory fees." These are outrageous amount of minutes for very little money with no connection fees when they are launched, and these terms are heavily advertised, usually in Spanish TV, radio shows and posters. The "introductory fees" hold true usually for a certain period of time and then, at the peak of their demand and without notice, the number of minutes decreases and the connection fees increase. Some cards might even disappear completely from circulation leaving the customer, the convenience stores and the wholesalers with "invalid" or disconnected cards and therefore bearing the loss.

Some retail stores would give their customers credit and pass the "bad" calling cards to the wholesaler. When the wholesaler tries to pass the credit to the distributor, at least 40% of the time, it wouldn't work. The wholesaler wouldn't get credit for those cards and consequently take the loss.

Most of the customers can't keep track of the change of terms on the new cards. They purchase the most popular cards that either give them much fewer minutes than advertised or no minutes at all because the connection is so bad that they have to hang up after a couple of minutes, and when they call again, they are charged a connection fee. These customers are frustrated and helpless because there is no clear way to get their money back or a channel to make a formal complaint, and no certainty that the complaint would even be heard. In addition to that there are language barriers and lack of knowledge of the US system.

A very small portion of the consumers are knowledgeable of the prepaid calling card scams and call the same country frequently so they have a good idea of how many minutes $2 should give them for their call. They complain about specific cards but know how the "system" works, so they take the time to inquire about the "good" cards at the moment for their country. These consumers try different cards until they find one that works for their country, at least for some time. When they realize the conditions change, they look for a new card. The general perception of this small group of consumers is that, at the end of the day, they got their money's worth in minutes.

As a native Peruvian, for years I used to communicate with my family using prepaid calling cards and I have been a victim of the scams. Every Spanish speaking relative, neighbor, friend and client that I had the opportunity to talk to about the subject has had the same experience. This is especially true not only for low-income families who cannot afford a land line and standard international rates; it is also true for other groups such as military families and ex-Peace Corps volunteers. Personally, once I stopped working in the calling card industry, it was very hard for me to keep up with the new cards and their reputation and I finally opted for the international services of a reputable firm such as Nextel.

In summary, prepaid calling cards are an invaluable resource for the immigrant community and low-income workers to communicate with their loved ones. However, based on my personal and professional experience with the Latino community, the industry needs to be regulated, especially in the following aspects:

- Use of deceptive marketing practices
- Disclosure of terms and fees charged to the consumer and their expiration date (if that is the case)
- Use of the Spanish language for the fine print
- Compliance with the advertised minutes
- Use of hidden fees
- Registration of each prepaid calling card (issuing company, customer service line and address) and expected time of circulation in the market

Thank you, Mr. Chairman for giving me the opportunity to speak on behalf of the Latino community and express our strong support of the Prepaid Calling Card Consumer Protection Act of 2008.

Mr. RUSH. Thank you so very much. Dr. Marlowe, you are recognized for 5 minutes.

STATEMENT OF JULIA MARLOWE, PROFESSOR EMERITUS, DEPARTMENT OF HOUSING AND CONSUMER ECONOMICS, UNIVERSITY OF GEORGIA

Ms. MARLOWE. Thank you very much, and I appreciate this opportunity to address the Committee on the subject of pre-paid telephone cards.

In my role as professor at the University of Georgia in the Department of Housing and Consumer Economics, my most recent research has been with pre-paid telephone cards. In our investigation, we used over 250 cards in two different funded studies, and that information has been published in a number of scholarly and lay publications.

The cards are convenient. They are a low-cost way to call, but there are problems. And I just want to say that we found in using these cards many of the things that Mrs. Zaragoza mentioned to be the case.

The biggest problem has to do with these fees. They often are unclear. They may be deceptive. There is no standardization of terminology. One of the most common practices is for a card, such as this one, to say no connection fee. However, the back of this card says—this card is in English and Spanish, the fine print is also in English and Spanish—it says a post-call fee applies after each call. What is the difference between a connection fee and a post-call fee? It is really the same thing.

So what they do is they have these per-call fees. They may call them connection fees, post-call fees, hang-up fees, long-talking fees, communication fees. They have all kinds of things.

The other fee that is often given is some kind of periodic fee, and these can be assessed daily, weekly, semimonthly, monthly, sometimes a combination. This much for the first few days and this much for the next month, and whatever.

The periodic fees have a lot of different terminology, too. The most common one is a maintenance fee. But they may call it a maintenance fee, they may call them administration fees, they may call them a tax, they may call it a service fee. And I didn't mention, some cards have a service fee per call and then a service fee per month. So some of them have numbers of these—they will have a maintenance fee and an administrative fee and so forth. So that is a problem.

Standardization of terms would help to alleviate some of the confusion. We have been talking a lot about having fees disclosed. We actually found a lot of the fees disclosed, and even when fees are disclosed, problems persist. Now, let me give you one example we encountered in our study. It is also in my written testimony.

A card was advertised as providing 1.9 cents a minute. It cost $5. The consumer expects to receive 263 minutes. In the fine print on the same poster where the 1.9 cents a minute was advertised, the fine print says there will be a 49-cent monthly maintenance fee, a 69-cent connection fee. We made two calls with the card. The second call 5 weeks after the first one. Deducting the 26 minutes for the maintenance fee and the 36 minutes twice for the connection fee, we would expect to get 163 minutes. That is what we got. The fees were disclosed. They were accurate. However, our actual cost was 3.1 cents a minute, not 1.9 cents a minute which was advertised.

How many consumers would do all these calculations? Should these consumers have to do these calculations? Why do these fees exist? Some cards don't have fees. We used several cards that say, no hidden surcharges, no monthly fees, and we found that in fact you got all the minutes they said you were going to get.

So my basic point is it is impossible to say how much the cost per minute is, it is impossible to say how many minutes you are going to get as long as you have the fees because the cost depends upon the way the consumer uses the cards. And in our second study, we purchased three cards of each brand. We used three different methodologies, and when we used the card all at once for one call, we were more likely to get all the minutes. But if you don't, then all these things happen. So I don't see any need for the fees.

I think I have said enough.

[The prepared statement of Ms. Marlowe follows:]

Testimony of :

Dr. Julia Marlowe, Associate Professor Emeritus
Department of Housing and Consumer Economics
University of Georgia

Submitted to the:

House Subcommittee on Commerce, Trade, and Consumer Protection of the Energy and Commerce

Tuesday, September 16, 2008

Introduction

Thank you for the opportunity to talk with you today about research that my colleagues and I conducted on prepaid telephone cards. Prepaid phone cards are a convenient and inexpensive way to make telephone calls. Despite the potential benefits, consumers are often confused about, and ultimately dissatisfied with these cards. The increase in the immigrant population in the United States, especially Latino consumers, has led to the marketing of some cards specifically to the Spanish-speaking consumer.[1,2] There is evidence that consumers who use cards to call Spanish-speaking countries face much higher prices than expected.[3] This information was the impetus for the University of Georgia study of prepaid telephone cards.

I understand that H.R. 3402 seeks to "...ensure that all advertising is truthful, accurate, and reasonably discloses the terms and conditions of prepaid telephone calling cards..."[4] For the most part, H.R. 3402 addresses the current consumer problems with the cards; however, my remarks attempt to provide a few caveats with respect to truthful disclosure. Information disclosure is complex, because costs vary for reasons ranging from location called to whether the call is placed from a pay phone or to a cell phone. It is practically impossible to determine how many minutes a consumer will receive, because minute rounding and fees charged depend upon how the consumer uses the card.

Problems with Disclosing Minutes Available

Consumers may receive minutes as promised, but problems arise with fees. Fees are added costs which increase the per-minute cost, so disclosing that there is a fee does not solve the problem. Consider the following example of one card we encountered in our study:

A poster advertises 1.9¢ per minute for calls made with a specific card. The card cost $5.00 so the consumer should receive 263 minutes. The fine print on the poster stated that there is a monthly maintenance fee of 49¢ and a connection fee of 69¢ per call. The connection fee results

in a deduction of 36.316 minutes per call, and a deduction of 25.79 minutes each month for the maintenance fee. We used the card twice over a period of five weeks and received 163 minutes, for a cost of 3.1¢ per minute. Deducting the connection fee twice and the maintenance fee once does equal 163 minutes so the disclosures are accurate. Most consumers would not do these calculations.[5]

My question is why are there fees at all? As long as there are fees, even disclosed ones, it is impossible to state the exact number of minutes the consumer will receive. A simpler solution would be for the providers to charge more for the cards and have no fees whatsoever. There are cards available that have no fees, with the exception of using the card at a pay phone.

Problems with Fees and other Stated Terms

Almost all cards state that rates and fees are subject to change at any time. Expiration dates are not always given. Minute rounding may be as high as eight, and three is common.

Basically, there are three categories of charges: minute rounding, per-call fees and periodic fees. Minute rounding is reasonable if the provider uses one minute rounding. There are many different names for per-call fees. Often cards advertise "no connection fee" and at the same time state that they have a post-call fee, hang-up fee, communication fee, service fee per call, and/or long-talking fee.[6] All these are per-call charges and many cards charge more than one of them. There should be only one term for a per-call fee. Having more than one term is very confusing and in most cases deceptive. One card that claims "No Connection!" [fee] in fine print states, "An increased rate may apply at some point during extended calls." I would categorize this as a long-talking fee, but how does a consumer know when a call is "extended?" Elimination of per-call fees would solve these problems.

There is even more confusion with respect to periodic fees. Periodic fees may occur daily, weekly, semi-monthly, monthly, or a combination of periods. These fees may be called a tax, a maintenance fee, service fee, administrative fee, local company charge, or the card may just state something like "A 59¢ semi-monthly fee applies."[7] Some cards assess several of these fees.

Though the fees may be disclosed, wording is often unclear, such as "maintenance fees may apply." The consumer can't know when or if a fee will be charged. If the amount of the fee is listed (79¢ for example), the number of minutes deducted must be calculated by the consumer.[8] With respect to fees, the fact that there is no standardization of terms, results in confusion at best and deception at worst. Only one term should be allowed for a periodic charge; however, the best solution to this problem would be the elimination of any kind of periodic fee.

Customer Service

Our research found that calling customer service was not always helpful. We called the customer service number for 236 cards. For about one-half of these cards, customer service was available 24 hours a day; however, personnel could not always answer questions we asked. Some even

gave incorrect information, such as telling us that there was no extra charge to use a pay phone when there is. We were not able to talk with a customer service person for approximately 33% of the cards.[9] Mandating that customer service personnel provide information is a start, but enforcement would need to be in place to assure consumers that customer service can indeed provide necessary information.[10]

Two University of Georgia Studies

I make the statements above as a result of findings from two studies. Problems with prepaid telephone cards surfaced from findings of a study of consumer fraud targeted to Hispanic immigrants. Participants in the study complained that they did not get the minutes they expected and that they could not get answers from calling the customer service number.[11] A study [Study 1] was undertaken to analyze information available prior to purchase of pre-paid phone cards and from customer service personnel, as well as to determine expected and actual cost per minute.[12] A second study [Study 2], funded by the Georgia Governor's Office of Consumer Affairs, was conducted to verify or disprove advertised claims with prepaid telephone cards.[13]

Study 1: The first study used 236 cards to collect information from customer service using a questionnaire developed by the researchers. All cards were targeted to a Spanish-speaking market and were under $10. Twenty data collectors were recruited from the University of Georgia Hispanic Student Association. All the data collectors were fluent in both English and Spanish, had someone they could call in a Spanish-speaking country and were required to attend two training sessions. After talking with customer service, data collectors used the cards to call Spanish-speaking countries. They were instructed to use each card twice, ending the first call when they had talked one-half of the minutes stated as available. In a few cases, there were not enough minutes remaining to make a second call. Stop watches were used to record the times of the calls; then we calculated the expected cost per minute and actual cost per minute for each card. A key finding from the study is that the average expected cost per minute was 15¢ but the average actual cost was 28¢ per minute. Table 1 provides some of the findings from this study. The research methodology and complete results are available in the article by Marlowe and Rojo (2005) at the American Council on Consumer Interests web site.

Study 2: A second study, funded by the Georgia Governor's Office of Consumer Affairs, sought to verify or disprove advertised claims of minutes. I met with several individuals at the Federal Trade Commission in D. C. to discuss methodology for this study.[14] As a result, three different methodologies were used with each brand of card. Advertisements were sampled in the Athens, Georgia area and 11 different brands of cards with advertised claims were selected for the study. Three cards of each brand were purchased. These cards were all under $25; some were targeted to a domestic market and others for international calls. Not all international cards were targeted to Spanish-speaking countries. Data collectors were instructed to use one brand of card three different ways: 1) use all minutes at once (avoiding multiple per-call charges), 2) use the card 10 times within a 1-2 week period (to get an idea of extensiveness of per-call charges or excessive minute rounding), and 3) use the card twice, with the second call made some time after the periodic fee period (to assess effect of periodic charges).

Findings of this study reveal that consumers are more likely to receive all the advertised minutes if they use a card only once. Most calls cost the most per minute if the card was use calls were made 10 times. Table 2 provides advertised versus actual cost per minute data for the 11 brands of cards by calling method used. Note that five brands of cards did deliver on the advertised claim when the card was used once and conversation lasted until minutes expired. The AT&T card provided the minutes advertised (allowing for minute rounding with using the card 10 times) for all three methods. However, it is very interesting to note that the lowest priced cards were not the "name brands." I cannot explain why Call N Carry, Digamé, Fenomenal, and CCI Georgia engage in deceptive advertising, because they have a lower actual cost product for Method 1 and two of these brands had low cost for all three methods. There is no need to overstate the costs.

Participants in the consumer fraud study of Hispanic immigrants made statements, such as (paraphrased) "you don't get the minutes they say you do" and "the Wall Mart cards are not good."[15] These kind of statements indicate that some consumers have figured out the market through repeated experience. Regulation might actually benefit those phone card providers who now engage in deceptive advertising by requiring accurate claims.

Conclusions

Because accurate and complete information typically isn't available, it is impossible for consumers to make informed decisions before using the cards.[16] Some of the prepaid phone card providers give accurate information, but others do not. Our research documents that information is often confusing, incomplete and even deceptive. Consumers who use all a card's minutes for one call are likely to experience the lowest cost per minute. While the best-known carriers (Sprint, AT&T and Net2Phone) were truthful, they also charged more per minute than some of the deceptive phone card providers. Currently, the market is competitive and there are low-cost providers, but such information can only be gained by actually using the cards. And some cards are very expensive; per-call fees and high minute rounding are particularly problematic.

Legislation should help equalize the practices among card providers. However, careful wording of what is meant by truthful disclosure of minutes available is imperative if per-call and periodic fees are allowed. If fees are allowed, there must be standardization of terms and only one term for each kind of fee. The combination of a competitive market and savvy consumers suggests that efficiency gains should be possible if consumers have better information prior to purchase.

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[6] Marlowe, Julia and Rojo, Martina (2005). "Consumer Problems with Prepaid Telephone Cards," *Consumer Interests Annual. Volume 51*: 126-142.

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[8] See Table 6; Marlowe, Julia (2006). Op. Cit.

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[13] Marlowe, Julia (2006). Op. Cit.

[14] Discussion with Jock Chung, Joel Brewer, Laura Koss, and Debbie Kelly at the Federal Trade Commission in Washington, D.C. March 2006.

[15] Marlowe, Julia and Atiles, Jorge H. (2003). Op. Cit.

[16] For background information on the theory of information search and experience goods, see, for example, Stigler, George J. (1961). "The Economics of Information," *The Journal of Political Economy, Vol. 69* (3): 213-225; & Nelson, Philip (1970). "Information and Consumer Behavior," *The Journal of Political Economy, 78* (2): 311-329.

Table 1: Means and Standard Deviation for Selected Variables

Variable	N[a]	Mean	Standard Deviation	Minimum	Maximumb
Initial # of minutes stated	233	88 86	71 05	5	487
Actual # of minutes	234	47 98	38 63	1	314
Expected average cost per minutec	234	$ 0.15	0.20	0.01	1.43
Actual average cost per minute[d]	234	$ 0.28	0.52	0 02	5.00

[a] For 2 cards, information was available from customer service, but it was not possible to place calls with the card. For one card, the initial number of minutes was not given.
[b] One card had 487 initial available minutes and was used to make 12 calls.
[c] Expected cost per minute was calculated by dividing the price of the card by the number of minutes stated as available.
[d] Actual cost per minute was calculated by dividing the price of the card by the number of minutes actually received from using the card.

Table 2: Advertised and Actual Cost per Minute of Prepaid Telephone Cards by Method Used

Brand[a]	**Advertised cost per min.**	**Method 1: (once)**	**Method 2: (10 times)**	**Method 3: (twice)**	**City called**
Call N Carry - long calls	1.9¢	2.2¢	5.35¢	3.1¢	Macon, GA
Digamé	1.4¢	2.4¢	4.89¢	2.4¢	Mexico City
Fenomenal	1.7¢	2.97¢	4.87¢	4.24¢	Xalapa, MEX
CCI Georgia	5¢	5¢	12.6¢	10¢	Xalapa, MEX
Kroger	6.9¢	6.9¢	7.66¢	6.1¢	Macon, GA
Silver Star	2 8¢	6.97¢	11.42¢	3.82¢	Xalapa, MEX
AT&T WalMart	7¢	7¢	7.19¢	7¢	Maryville, TN
Sprint	7.9¢	7.9¢	8.59¢	7.99¢	Atlanta, GA
Call N Carry- no connect fee	9.9¢	10¢	18.7¢	13.9¢	Macon, GA
Arriba Mexico	6.7¢	11.9¢	17.56¢	18.3¢	Xalapa, MEX
Net2Phone[b]	19¢	16.45¢	16 45¢	18.38¢	Gujarat, INDIA

[a] Brands are in order of lowest cost per minute for Method 1.
[b] When the card was used, there was a statement that a sale was underway and therefore additional minutes were available.

Mr. RUSH. Mr. Eichberger, you are recognized now for 5 minutes.

STATEMENT OF JOHN EICHBERGER, VICE-PRESIDENT, GOVERNMENT RELATIONS, NATIONAL ASSOCIATION OF CONVENIENCE STORES

Mr. EICHBERGER. Thank you very much, Mr. Chairman, members of the subcommittee. As the chairman said, I am John Eichberger with the National Association of Convenience Stores. We are an international trade association representing the convenience petroleum retailing industry. In the United States, our industry operates about 145,000 locations, 60 percent of which are owned by single-store operators, which means we are a very small, business-dominated industry but we have a significant impact. In fact, in 2007, we employed about 1.7 million workers and generated more than half a trillion dollars in sales through our channel of trade.

I want to begin this morning by commending the sponsors of H.R. 3402 for their efforts in protecting the rights of consumers to have their reasonable expectations fulfilled when they purchase pre-paid calling cards. We strongly support efforts that promote consumer confidence by reducing deceptive and fraudulent practices with respect to the sale of any product, pre-paid calling cards or whatever else may sell through our stores.

Over the past decade, calling cards have become a much more significant part of our industry. In 2007, our industry sold more than $350 million worth of these products. It is important for our members that the products they sell fulfill the promise to the customers, especially since the bulk of our customers are repeat customers. We have a relationship with them that we depend upon for our survival. These relationships can be damaged if a customer believes she has been ripped off by buying a product that did not live up to its advertised value. This is why NACS supports efforts to ensure that the calling cards we sell meet the customers' reasonable expectations.

It is important to note that neither NACS nor its members are in a position to understand the intricacies of the telecommunications industry. My purpose today, however, is to simply explain how our industry is involved in the business and to support the efforts of the bill's sponsors to eliminate consumer deception and fraud. We applaud the provisions in the bill to protect honest retailers from liability associated from any deceptive practice employed by the card issuers. This is an appropriate and welcome component. As the Committee prepares for the consideration of the bill, we ask that you would consider a couple other minor modifications that will build upon these provisions that are currently in place for the retailers.

In our industry, many convenience stores are supplied by multi-product distributors, and we use the term distributors as the wholesale deliveries. I believe some of the terminology using distributors may have a slightly different connotation, so I apologize if there is any confusion. I hope to clarify it here. These companies to which I am referring may deliver products as diverse as potato chips, candy bars, car fresheners, or pre-paid calling cards at the same time to their retail customers. These third-party distributors

are not the companies who issue the cards. They do not provide the service, nor do they produce the accompanying materials that come with those cards. They simply act as middle men between the service provider and the retailer. NACS believes that these individuals should not be held liable for practices over which they have no control, similar to where the bill already protects retailers. We also suggest there be a clarification of liability in the Advertising and Other Promotional Materials section of the bill.

We fully support the requirement that all terms and conditions be properly and clearly disclosed on all promotional materials. My colleagues on the panel pointed out several different components. We agree with that. The consumer should know exactly what they are buying and have no concerns or confusion about what product and value they are getting for their purchase. However, it is important that the legislation recognize the fact that neither retailers nor third-party distributors should be held liable for violations of these disclosure requirements on point-of-sale materials unless they themselves produced the material. Keep in mind, retailers do not have the ability to read the promotional material they have and assure that it satisfies statutory requirements, neither do the third-party distributors. Therefore, unless they are altering the materials, we do not believe they should be held liable for those provisions. We have provided staff with some suggested language for the bill that we believe would address these areas of concern. We hope the Committee will see fit to include these modifications as the bill moves forward.

Mr. Chairman, the victims of deceptive practices in this business are frequently those who can least afford it and have the smallest ability to protect themselves or obtain remedy. NACS applauds the interest of this subcommittee on this topic, and I appreciate the opportunity to share our views and I look forward to your questions. Thank you.

[The prepared statement of Mr. Eichberger follows:]

NACS

TESTIMONY OF

JOHN EICHBERGER
VICE PRESIDENT, GOVERNMENT RELATIONS

NATIONAL ASSOCIATION OF CONVENIENCE STORES

BEFORE THE
SUBCOMMITTEE ON COMMERCE, TRADE AND CONSUMER PROTECTION
OF THE
COMMITTEE ON ENERGY AND COMMERCE
OF THE
U.S. HOUSE OF REPRESENTATIVES

REGARDING H.R. 3402
CALLING CARD CONSUMER PROTECTION ACT

SEPTEMBER 16, 2008

The Association for Convenience & Petroleum Retailing
1600 Duke Street • Alexandria, VA 22314-3436 • (703) 684-3600 • FAX (703) 836-4564 • www.nacsonline.com

Mr. Chairman and Members of the Subcommittee, my name is John Eichberger. I am Vice President of Government Relations for the National Association of Convenience Stores (NACS). I appreciate the opportunity to appear before you today and to provide to you NACS' views on H.R. 3402, the "Calling Card Consumer Protection Act."

NACS is an international trade association representing the convenience store industry. The industry as a whole operates about 145,000 stores in the United States, generated $577.4 billion in sales in 2007 and employs approximately 1.7 million workers. This really is an industry of small businesses. More than 60 percent of convenience stores are owned by one store operators. NACS has members in every state and Congressional district in the United States.

Mr. Chairman, at the outset NACS wishes to commend the sponsors of H.R. 3402 for their efforts to protect the right of consumers to have their reasonable expectations fulfilled when they purchase prepaid calling cards. As a representative of responsible retailers, NACS strongly supports efforts to promote consumer confidence by reducing deceptive or fraudulent practices with respect to the sale of any product.

- **Prepaid Calling Cards and the Convenience Store Industry**

Over the past decade, prepaid calling cards have become a significant sales item in many, if not most, convenience stores. Convenience stores are present in virtually all of the country's neighborhoods and often are the only facilities open at all times. As a consequence, consumers frequently rely on their neighborhood convenience store for items such as prepaid calling cards. In 2007, the industry sold more than $350 million worth of these cards.

It is important to us as it would be to any responsible retailer that the products convenience stores sell fulfill their promise to our customers. The bulk of the convenience store industry sales are made to "regular customers," i.e., people who frequently shop at our locations.

The key to successful retailing is establishing a "relationship" with a consumer in which that consumer develops positive expectations for its purchases and has those expectations fulfilled on a consistent basis. The fulfillment of reasonable expectations is the "value proposition" offered to and accepted by consumers at retail locations and which forms the basis for regular patronage by that particular consumer. The thing most likely to break a consumer's "habit" of patronizing a particular location is that establishment's failure to fulfill a customer's expectations with respect to transactions at that location. Perceiving that he or she has been "ripped off" – not getting what he or she reasonably expected – is the single incident most likely to change a customer's perception of a store and to break the patronage habit.

With respect to items like prepaid calling cards, NACS members are in one crucial way in a position virtually identical to that of an end user. NACS members must accept the representations of those who provide the cards as to the amount of service that will be received by the ultimate user of these devices. Retailers are simply not able, on an independent basis, to test these items to determine if they fulfill the claims made in their advertising. Retailers, in good faith, accept the claims of prepaid calling card providers. Given the ability that a provider's deceptive or fraudulent practice has to injure a retailer's relationship with its customers, and therefore its economic well being, NACS strongly supports efforts by this Subcommittee to attack such practices.

- **NACS' Position on H.R. 3402**

Neither NACS nor its members are in a position to understand the intricacies of the telecommunications industry, its charges, and its needs—any more than we are experts in the homogenization and pasteurization of a gallon of milk. As a consequence, my primary purpose in appearing today is to explain how our industry is involved in the prepaid calling card business and to support the efforts of the bill's sponsors to eliminate consumer deception and fraud perpetuated by unscrupulous providers in that business.

NACS believes that the bill's proposed reliance upon the Federal Trade Commission ("FTC") to promulgate and enforce a regulatory regime by which the bill's objectives may be achieved is appropriate. The FTC really is America's consumer protection agency. It has broad and deep experience with respect to the marketing of consumer products. The standards that it employs to establish and prove consumer injury are widely known and accepted. As a consequence, NACS believes it is the "right tool" for this job and urges the Subcommittee to proceed accordingly.

As the Committee prepares for consideration of this legislation, NACS would like to suggest you consider some minor modifications. In our industry, many convenience stores are supplied by multi-product distributors. These companies may deliver to a store products as diverse as potato chips, candy bars, car fresheners and pre-paid calling cards, all at the same time. These third party distributors are not the companies who provide the service or produce the cards and accompanying materials. They simply act as middle-men between the service provider and the retailer. It is NACS opinion that these individuals should be included in the exemption articulated in Sec. 2 (4) of the bill defining "prepaid telephone calling card distributor."

In addition, NACS would also suggest additional clarification of liability associated with Sec. 4 (b)(1)(C)—Advertising and Other Promotional Materials. NACS fully supports the requirement that all terms and conditions be properly disclosed on all promotional materials. However, it is important that the legislation recognize the fact that retailers should not be held liable for violations of these disclosure requirements on point of sale materials. It is not reasonable to assume that a convenience store manager will be adequately familiar with the applicable statute to ensure proper disclosure on these materials. Likewise, third party distributors, such as those I described earlier, should not be held liable for such inaccuracies unless they themselves were the producer of the materials.

Mr. Chairman, the victims of deceptive practices in this business are frequently those who can least afford it and have the smallest ability to protect themselves or obtain remedy. NACS applauds the interest of this Subcommittee on this topic.

Thank you for the opportunity to share NACS views on this topic. I will be happy to respond to any questions.

Mr. RUSH. I thank the gentleman, and I thank all the witnesses for their fine testimony. The chair recognizes himself now for 5 minutes for questioning.

Ms. Greenberg, you referred to a "floor" for disclosure requirements on these pre-paid calling cards. But could it be the case here that conflicting or inconsistent state and federal requirements all which is designed to fit on a wallet-sized card could cause consumer confusion? Is this is an area where one set of tough but extreme line and economical disclosure requirements might make more sense?

Ms. GREENBERG. Mr. Chairman, I do think certainly when there are states taking action, there can be some confusion within the industry, but I think it would be a terrible mistake to preempt state activity. And I think this is a classic case where the States were ahead of the Federal Government. States have been working on this, passing legislation, Attorneys General across the states. I think there are 18 states at this point who have taken action. They have taken it upon themselves early on, including in your State of Illinois, where the Attorney General likened the industry to if there were Olympic awards for fraud, this industry would be right up there.

In 2004, the State of Illinois took very strong steps to curtail the abuses of this industry. So what we believe is that it is really important that the Federal Government set some basic standards, both for disclosure and then as I said in my statement, come back and look at whether disclosure is working because as we can see, sure, you can disclose some terrible terms but in my view they are unconscionable terms and they rip consumers off. So disclosure only takes you so far in protecting consumers.

So the States just have been a great engine for consumer protection, and it is always our policy to ask the Federal Government to set a minimum standard so all states have to comply with that, and then let states who are interested in providing more protections for their citizens have the opportunity to do that.

Mr. RUSH. You stated that until recently there has been lax enforcement against pre-paid calling cards at both the federal and state level. Can you explain to us what changed to improve enforcement and are there still roadblocks to robust enforcement and will this bill fix it?

Ms. GREENBERG. Well, I think this bill has many important provisions in it. It does give the FTC the ability to go forward in some areas and give the federal agency jurisdiction that it doesn't now have. It would also call attention to the fact that the Federal Government and Congress is taking this area of consumer fraud very seriously.

So I think that is a very good start. You have a patchwork of enforcement. That has already been referred to. You have some States that have acted, other States haven't. You have the FTC, they have taken some good stands. There has been a very good class action suit which has resulted in a $20 million settlement. So it is patchwork. There are some consumers that have absolutely no protection. So I think we are going in the right direction with this bill. I do think it will set a floor, and I hope that answers your question. Thank you, Mr. Chairman.

Mr. RUSH. Thank you. Dr. Marlowe, do you have any sense of how abuse in the marketing of these cards affects the Latino community in particular?

Ms. MARLOWE. Yes, I do. The first study we did, we only purchased cards that were in the Spanish language. They may have been in English and Spanish, but we purchased over 250 cards and we were actually able to use 236 of them. Some of the abuses were, I have a card that says cargos no de conexion, no connection fee. But the fine print on the back in Spanish says los cargos conexion applicara, connection fees apply. So I suppose they could read the fine print and know that there is some discrepancy here, but obviously those kinds of things were happening.

The other thing that we did is we called the customer service number for every single card. Our data collectors were fluent in English and Spanish, and they called and talked in Spanish. In some cases, the person that answered the number couldn't speak Spanish. One-third of the time customer service was not there. I can document. In fact, it is in the publications that there are some abuses.

Mr. RUSH. Thank you. The chairman's time is up. The chair now recognizes the ranking member for 5 minutes.

Mr. WHITFIELD. Thank you, Mr. Chairman, and thank you all for your testimony this morning. Could you tell us which states have the most effective laws or regulations relating to this issue to protect the public from the fraudulent sale of these phone cards?

Ms. GREENBERG. Yes, I can speak to some of that. I know that Texas and Florida in particular, the Attorneys General in both states have taken pre-paid calling card companies to court and assessed a number of penalties and arranged for various injunctive relief to stop certain activities to do much better in forward disclosure. But the last time we checked, it was about 18 states who had taken some action. The State of Illinois, 2004, passed legislation. The governor signed it. And they require certification of calling card companies which is an important consumer protection. I got a couple of more——

Mr. WHITFIELD. So 32 states have not acted——

Ms. GREENBERG. Something along those lines, yes.

Mr. WHITFIELD. Dr. Marlowe?

Ms. MARLOWE. My colleagues, Mark Budnitz, who is a consumer law professor, and Martina Rojo who is also a consumer law professor, did a review of state legislation and administrative regulations and it is in this publication and I will leave this for the Committee. There is a review of all states.

Mr. WHITFIELD. And for those of you familiar with the action taken by the 18 states, how does our bill that we are considering today compare with the provisions in those laws? Is there a glaring weakness in this bill or is it stronger than those or is it about the same or do any of you——

Ms. MARLOWE. I can't comment on that. My colleagues probably could, but I can't.

Mr. WHITFIELD. Ms. Greenberg?

Ms. GREENBERG. Yes, one of the features that you see in some of the state settlements and bills is a requirement for certification or a licensing requirement for some of these operators.

Mr. WHITFIELD. In order to sell these cards you have to be licensed?

Ms. GREENBERG. Yes, and the toll-free numbers have to be available. That is included in this legislation, too. And of course, this has the other feature of giving the Federal Trade Commission additional jurisdiction. But there are some similarities and there is very specific focus on disclosure in this bill, and that is also required in the state laws.

Mr. WHITFIELD. Now, you mentioned in your testimony I believe the $20 million class action.

Ms. GREENBERG. There was class action brought by attorneys in New York City that resulted in a settlement. It was a $20 million settlement with some money set aside for compensating—and some other provisions. And I don't know if that has been finalized, but it certainly appears in the news.

Mr. WHITFIELD. I take it there must be thousands of companies that are distributing these cards. Would that be correct?

Ms. GREENBERG. I don't know if it is thousands.

Ms. MARLOWE. I met with Howard Segermark who was head of, for a while, a now-defunct trade association for pre-paid cards. That was about 8 years ago or so. And he estimated over 500 companies at that time. Given that the industry has grown, there may be more than that now.

Mr. WHITFIELD. Over 500? OK. Now, Ms. Zaragoza, what are some reasons that people are using these cards? So many people have cell phones today but why would they use these cards?

Ms. ZARAGOZA. Well, most of these people, they really don't—some of them can access the Internet and buy cards from the Internet. They are not computer savvy, they don't have Internet at home, they don't have a land line, they don't have cell phones, or if they do, their minutes are very limited. So one of the features of these cards is that you can call from a phone booth, so you are not wasting your minutes.

Mr. WHITFIELD. Yes. OK. And Mr. Eichberger, would you just mention once again the two issues that you are concerned about, you recommended some changes in this legislation about?

Mr. EICHBERGER. Specifically I can summarize it in one main point. If you are not responsible for issuing the cards, servicing the cards, or printing the promotional materials, you should not be held liable for complying with the statute. If you have any culpability in it, then you stand the test of the law. But you should have the protection of the law so that you can go about your business the way you usually do.

Mr. WHITFIELD. OK. Mr. Chairman, my time is expired.

Mr. RUSH. The chair will recognize himself through unanimous consent for one additional question. Ms. Zaragoza, I just want to know, in your experiences working in this industry, can you think of one time that a consumer has been repaid, gotten their money back, because of either they weren't given the minutes advertised or their minutes hadn't been used up or the money hasn't been used up by hidden fees? Can you think of one instance where they would have returned the money?

Ms. ZARAGOZA. From the distributor, no, but some retail stores would, to preserve the relationship with the customer, they would

give credit to the customer; and then they will pass on that credit to the wholesaler which, if they wanted to preserve their account, they will have to give them the credit. But then when they go to the distributor, they, more than 40 percent of the time because I used to do that, too, like they wouldn't grant you the credit, so it is very difficult.

Mr. RUSH. Thank you very much. The chair really thanks the witnesses for taking the time out of their busy schedule to appear before this committee. Your testimony has been very helpful to us, and we intend to take the heart of your testimony into account as we proceed this afternoon in the markup of this bill. We really want to thank you so much, and you are now excused. Thank you again for your participation.

[Whereupon, at 11:20 a.m., the subcommittee was adjourned.]

[Material submitted for inclusion in the record follows:]

PREPARED STATEMENT OF HON. EDOLPHUS TOWNS

Thank you Chairman Rush and Ranking Member Whitfield for holding this important hearing today on the Calling Card Consumer Protection Act. I look forward to the testimony of both panels of witnesses. They all have long records of service in their fields and will offer important insights for us to consider.

The Calling Card Consumer Protection Act would be an important step in protecting some of our most vulnerable citizens from unscrupulous practices. In New York City and all over the country, calling cards are vital lifelines to immigrant communities and their families back home. There is a great deal of trust that goes into buying one of these cards. You have to trust that it will have the proper amount of minutes and that you are actually getting what you thought you paid for. There are major opportunities for fraud and abuse and that is why I cosponsored this bill. I hope this hearing can illuminate some of the ways this bill can improve. I look forward to working with my colleagues and commend Congressman Engel on his dedication to this issue.

Thank you and I yield back the balance of my time.

PREPARED STATEMENT OF HON. MARSHA BLACKBURN

I thank the chairman for holding this important hearing today, and for scheduling an open markup on H.R. 3402 this afternoon. Every member of this subcommittee will agree that calling-card fraud is a heinous act perpetrated often against vulnerable populations throughout the United States.

In tests conducted by the FTC, prepaid calling cards delivered only 50% of the average advertised time in 87 separate tests. The Commission also found cost-per minute rates can skyrocket up to 87% higher than a customer might expect.

Worse still, many cards marketed directly towards non- English speaking customers offer strikingly poor performance, leading to an estimated $1 million in everyday loss for Hispanic customers.

"Bad actors" peddling fraudulent cards to vulnerable communities not only damage the families they seek to rip off, they also limit market share for corporate citizens who play by the rules and respect the rule of law. These companies pay taxes, employ working Americans, and produce a service millions depend on to communicate internationally. They deserve market protection no less than the customers seeking a quality product in exchange for an honest buck.

H.R. 3402 takes a well-intentioned step to ensure customers receive the service they paid for. The FTC clearly needs additional regulatory authority to enforce appropriate market standards. I don't say that very often, but in this case basic statutory language can vastly improve consumer protection.

The FTC should, for example, be able to promulgate limited regulations to require card distributors to disclose agreement terms on the back of a calling card. This is a common sense tool that will empower consumers to make sound decisions, and will prevent bad actors from "hiding the ball" and withholding critical information.

However, new regulatory power at the FTC may not solve anything if a patchwork system of state regulations competes with a Federal standard. H.R. 3402 would therefore benefit from a federal preemption amendment to streamline existing regu-

lations in eleven states. While no doubt well-meaning, each regulatory system creates additional and potentially unnecessary costs for calling-card distributors.

A strong Federal standard need not weaken state standards. In fact, it is likely to improve state standards lacking appropriate consumer protections.

Mr. Chairman I applaud your willingness to tackle this important issue, and respectfully yield back the balance of my time.